NORTHEAST BANCORP /ME/
Form 10-K
September 29, 2008

FORM 10-K

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

(Mark One)

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For fiscal year ended June 30, 2008

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number (1-14588)

NORTHEAST BANCORP
(Exact name of registrant as specified in its charter)

Maine	01-0425066
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
500 Canal Street, Lewiston, Maine	04240
(Address of principal executive offices)	(Zip Code)
Registrant's telephone number, including area code:	(207) 786-3245

Securities registered pursuant to Section 12(b) of the Act:

Title of each class:	Name of each exchange on which registered:
Common Stock, $1.00 par value	NASDAQ

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer as defined in Rule 405 of the Securities Act. Yes_ No X

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes_ No X

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):
Large Accelerated Filer _ Accelerated filer _ Non-accelerated filer _ Smaller Reporting Company X

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

The aggregate market value of the Registrant's common shares held by non-affiliates, as of December 31, 2008, was approximately $33,119,594 based on the last reported sales price of the Company's common shares on the NASDAQ exchange as of the close of business on such date. Although directors and executive officers of the registrant and its subsidiaries were assumed to be "affiliates" of the registrant for the purposes of this calculation, this classification is not to be interpreted as an admission of such status. On September 11, 2007, the Company changed its listing from AMEX to NASDAQ. There were 2,315,182 common shares of the registrant outstanding as of September 19, 2008.
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DOCUMENTS INCORPORATED BY REFERENCE

The following documents, in whole or in part, are specifically incorporated by reference in the indicated Part of this Annual Report on Form 10-K:

Document	Form 10-K Reference Location
Proxy Statement for the 2008 Annual Meeting of Shareholders	III

This Annual Report on Form 10-K contains certain forward-looking statements within the meaning of Section 27A of the Securities Exchange Act of 1933 and Section 21E of the Securities Act of 1934 and is subject to risks, uncertainties, and other factors which could cause actual results to differ materially from those expressed or implied by such forward-looking statements. See "Item 1. Business -Forward Looking Statements and Risk Factors."

PART I

Item 1. Business

Overview and History

Northeast Bancorp ("us", "our", "we", or the "Company"), a Maine corporation chartered in April 1987, is a bank holding company registered under the Bank Holding Company Act of 1956 (the "BHCA"). Prior to 1996, the Company operated under the name Bethel Bancorp. The Company's primary subsidiary and principal asset is its wholly-owned banking subsidiary, Northeast Bank (the "Bank" or "Northeast Bank"), which has eleven banking branches. The Bank offers property and casualty insurance products through the Bank's wholly owned subsidiary, Northeast Bank Insurance Group, Inc. ("NBIG"). NBIG has fourteen insurance agency offices, four of which are located in our banking branches. In addition, we also offer investment brokerage services, including financial planning products and services, through our office in Falmouth, Maine. The investment brokerage services are offered through a division of the Bank.

Northeast Bank, which was originally organized in 1872 as a Maine-chartered mutual savings bank and was formerly known as Bethel Savings Bank F.S.B. ("Bethel"), is a Maine state-chartered bank and a member of the Federal Reserve System. From 1987 to August 2004, Northeast Bank was a federal savings bank and the Company was a unitary savings and loan holding company registered with the Office of Thrift Supervision ("OTS"). In August 2004, Northeast Bank's charter was converted into a Maine state-chartered universal bank, and the Company became a bank holding company under the BHCA. In connection with the conversion of its charter, Northeast Bank applied for and was granted membership in the Federal Reserve System. Accordingly, the Company and Northeast Bank are currently subject to the regulatory oversight of the Federal Reserve Board ("FRB") and the State of Maine Bureau of Financial Institutions.

As of June 30, 2008, the Company, on a consolidated basis, had total assets of approximately \$598 million, total deposits of approximately \$363 million, and stockholders' equity of approximately \$40 million. Unless the context otherwise requires, references herein to the Company include the Company and its subsidiary on a consolidated basis.

Strategy

Northeast Bancorp through its subsidiary, Northeast Bank, the Bank's subsidiary, NBIG, and third party affiliations, provides a broad range of financial services to individuals and companies in western and south-central Maine and Rochester, NH. Although historically the Bank had been primarily a residential mortgage lender, over the last decade the Bank has expanded its commercial loan business, increased its line of financial products and services, and expanded its market area. Management's strategy is to continue modest, but profitable, growth by increasing our loan and deposit market share in our existing markets in western and south-central Maine, closely managing the yields on earning assets and rates on interest-bearing liabilities, introducing new financial products and services, increasing the number of bank services per household, increasing non-interest income from expanded investment and insurance brokerage and trust services, and controlling the growth of non-interest expenses. Management believes that this strategy will increase core earnings in the long term by providing stronger interest margins, additional non-interest income and increased loan volume. We believe that the local character of the Bank's business and its "community bank" management philosophy allows it to compete effectively in its market area.

Our community banking strategy emphasizes the development of long-term full banking relationships with customers at each branch location by increasing the number of products and services with each customer and providing consistent, high quality service from:

- employees with local decision-making authority;
- employees who are familiar with the customers' needs, their business environment and competitive demands; and
- employees who are able to develop and customize personalized financial solutions that are tailored to the customer's needs.

With the goal of providing a full range of banking, financial planning, investment brokerage, and property and casualty insurance services to our customers and in an effort to develop strong, long-term primary banking relationships with businesses and individuals, we have expanded our commercial banking operations by selectively making commercial loans to small and medium sized companies. In this regard, our business development efforts have been directed towards full service credit packages and financial services, as well as competitively priced mortgage packages. In our effort to attract and maintain strong customer relationships, we also have continually expanded the financial products and services that we make available to our customers. In particular, we expanded our insurance division through acquisitions in order to provide a broader array of insurance products to our customers, and we have continued to maintain an investment banking services division to provide financial planning products and service to them as well.

The Bank is subject to examination and comprehensive regulation by the Maine Bureau of Financial Institutions (the "Maine Bureau") and the FRB, and its deposits are insured by the Federal Deposit Insurance Corporation (the "FDIC") to the extent permitted by law. The Bank also is a member of the Federal Home Loan Bank ("FHLB") of Boston.

The principal executive offices of Northeast Bancorp and the Bank are located at 500 Canal Street, Lewiston, Maine, 04240, and their telephone number is (207) 786-3245.

Market Area

The Bank is headquartered in Lewiston, Maine with full service branches in Auburn, Augusta, Bethel, Brunswick, Buckfield, Harrison, Lewiston (2), Mechanic Falls, Portland, and South Paris, Maine. The Bank's investment brokerage division has an office in Falmouth, Maine from which investment, insurance and financial planning products and services are offered. NBIG has offices in Auburn, Anson, Augusta, Berwick, Bethel, Jackman, Livermore Falls, Mexico, Rangeley, Scarborough, South Paris, Thomaston, and Turner, Maine and an office in Rochester, New Hampshire from where the Bank's insurance division offers personal and commercial casualty and property insurance products. The Company's primary market area, which covers western and south central regions of the State of Maine, is characterized by a diverse economy that has experienced an economic decline growth in recent years.

Market for Services

Management believes that the Bank's principal markets are: (i) the residential real estate market within its primary market area; (ii) small-to-medium sized businesses within its primary market area; (iii) the growing consumer loan market, including indirect automobile dealer and recreational vehicle loans; and (iv) the growing consumer demand for a wide range of other consumer-oriented financial services and products such as financial planning services, investments, life insurance, property and casualty insurance, trust services, college loans and other similar products.

Businesses are solicited through the personal efforts of the officers and directors of both Northeast Bancorp and the Bank. We believe that a locally-based, independent bank is often perceived by the local business community as possessing a clearer understanding of local commerce and its needs. We also believe that we are able to make prudent lending decisions more quickly than our competitors without compromising asset quality or profitability.

Competition

We encounter intense competition in our market area in making loans, attracting deposits, and selling other customer products and services. The deregulation of the banking industry, the ability to create financial services holding companies to engage in a wide range of financial services other than banking, and the widespread enactment of state laws which permit multi-bank holding companies, as well as the availability of nationwide interstate banking, has created a highly competitive environment for financial services providers. In one or more aspects of our business, we compete with other savings banks, commercial banks, credit unions, mutual funds, insurance companies, brokerage and investment banking companies, finance companies, and other financial intermediaries operating in Maine and elsewhere. Many of our primary competitors, some of which are affiliated with large bank holding companies or other larger financial-based institutions, have substantially greater resources, larger established customer bases, higher lending limits, extensive branch networks, numerous ATMs and greater advertising and marketing budgets. They may also offer services that we do not currently provide.

The principal factors in competing for deposits are convenient office locations, flexible hours, interest rates and services, and Internet banking, while those relating to loans are interest rates, the range of lending services offered and lending fees. Additionally, we believe that an emphasis on personalized financial planning and advice tailored to individual customer needs, together with the local character of the Bank's business and its "community bank" management philosophy will enhance our ability to compete successfully in our market areas. Further, we also offer a wide range of financial services to our customers, including not only basic loan and deposit services, but also investment services, trust services, and insurance products. We believe that our ability to provide such services and advice, and to provide the financial services and products required by our customers, will be an attractive alternative to consumers in our market area.

Lending Activities

General

The primary source of income generated by the Bank is from the interest earned from our loan portfolio. The principal lending activities of the Bank are the origination and purchase of conventional mortgages for the purpose of constructing, financing, or re-financing one-to-four family residential properties and commercial properties. The majority of the properties securing the mortgage loan portfolio are located in the State of Maine. However, in an effort to diversify the geographic scope of the real estate collateral held by it, the Bank does purchase, in the secondary market, residential mortgage loans collateralized by properties in other states. Interest rates and origination fees charged on loans originated by the Bank are generally competitive with other financial institutions and other mortgage originators in its general market area.

Although residential and commercial real estate lending remains a strong component of the Bank's lending operations, consistent with our business strategy, we also actively seek an increased volume of commercial and consumer loans. Commercial loans are originated for commercial construction, acquisition, remodeling and general business purposes. In this regard, the Bank, among other things, also originates loans to small businesses in association with the Small Business Administration, Rural Development Administration and Finance Authority of Maine. Consumer loans include those for the purchase of automobiles, boats, home improvements and personal investments. We also pursue quality indirect lending through local automobile and recreational vehicle dealerships.

Residential Lending

The major component of the Bank's lending activities consists of the origination of single-family residential mortgage loans collateralized by owner-occupied property, most of which is located in its primary service areas. The Bank offers a variety of mortgage loan products. Its originations generally consist of adjustable rate mortgages ("ARMs") or fixed rate mortgage loans having terms of 15 years or 30 years amortized on a monthly basis, with principal and interest due each month. The Bank holds in portfolio all adjustable rate mortgage loans. Fixed rate loans are sold into the secondary market. Additionally, the Bank offers home equity loans and home equity lines of credit.

The Bank offers adjustable rate mortgages with rate adjustments tied to the weekly average rate of one, three and five year U.S. Treasury securities with specified minimum and maximum interest rate adjustments. The interest rates on a majority of these mortgages are adjusted yearly with limitations on upward adjustments of 2% per adjustment period and 6% over the life of the loan. The Bank generally charges a higher interest rate if the property is not owner-occupied. It has been the Bank's experience that the proportions of fixed-rate and adjustable-rate loan originations depend in large part on the interest rate environment. As interest rates fall, there is generally a reduced demand for variable rate mortgages and, as interest rates rise, there is generally an increased demand for variable rate mortgages.

Fixed rate and adjustable rate mortgage loans collateralized by single family residential real estate generally have been originated in amounts of no more than 80% of appraised value. The Bank may, however, lend up to 95% of the value of the property collateralizing the loan, but if made in excess of 80% of the value of the property, they must be insured by private or federally guaranteed mortgage insurance. In the case of mortgage loans, the Bank requires mortgagee's title insurance to protect against defects in its lien on the property that collateralize the loan. The Bank in most cases requires title, fire, and extended casualty insurance to be obtained by the borrower, and, where required by applicable regulations, flood insurance. The Bank maintains its own errors and omissions insurance policy to protect against loss in the event of failure of a mortgagor to pay premiums on fire and other hazard insurance policies.

Although the contractual loan payment period for single-family residential real estate loans is generally for a 15 to 30 year period, such loans often remain outstanding for significantly shorter periods than their contractual terms. The Bank generally does not charge a penalty for prepayment of mortgage loans. Mortgage loans originated by the Bank customarily include a "due on sale" clause giving the Bank the right to declare a loan immediately due and payable in the event, among other events, that the borrower sells or otherwise disposes of the real property subject to a mortgage. In general, the Bank enforces due on sale clauses. The Bank generally applies the same underwriting criteria to residential mortgage loans whether purchased or originated. In its loan purchases, the Bank generally reserves the right to reject particular loans from a loan package being purchased and does reject loans in a package that do not meet its underwriting criteria. In connection with loan purchases, the Bank receives various representations and warranties from the sellers of the loans regarding the quality and characteristics of the loans. In determining whether to purchase or originate a loan, the Bank assesses both the borrower's ability to repay the loan and the adequacy of the proposed collateral. On originations, the Bank obtains appraisals of the property securing the loan. On purchases, the Bank reviews the appraisal obtained by the loan seller or originator. On purchases and originations, the Bank reviews information concerning the income, financial condition, employment and credit history of the applicant.

We have adopted written, non-discriminatory underwriting standards for use in the underwriting and review of every loan considered for origination or purchase. These underwriting standards are reviewed and approved annually by our board of directors. Our underwriting standards for fixed rate residential mortgage loans generally conform to standards established by Fannie Mae ("FNMA") and the Federal Home Loan Mortgage Corporation (the "FHLMC"). A loan application is obtained or reviewed by the Bank's underwriters to determine the borrower's ability to repay, and confirmation of the more significant information is obtained through the use of credit reports, financial statements, and employment and other verifications.

Commercial Real Estate Lending

The Bank originates both multi-family and commercial real estate loans. Multi-family and commercial property loans generally are made in amounts up to 80% of the lesser of the appraised value or purchase price of the property. Although the largest multi-family or commercial loan in our portfolio at June 30, 2008 was $3,363,464, most of these loans have balances under $500,000.

The Bank's permanent commercial real estate loans are secured by improved property such as office buildings, medical facilities, retail centers, warehouses, apartment buildings, condominiums and other types of buildings, which are located in its primary market area. Multi-family and commercial real estate loans generally have fixed or variable interest rates indexed to FHLB and prime interest rates with notes having terms of 3 - 5 years. Mortgage loan maturities have terms up to 20 years.

Loans secured by multi-family and commercial real estate generally are larger and involve greater risks than one-to-four family residential mortgage loans. Because payments on loans secured by multi-family and commercial properties often are dependent on successful operation or management of the properties, repayment of such loans may be subject to a greater extent to adverse conditions in the real estate market or the economy. We seek to minimize these risks in a variety of ways, including limiting the size of our multi-family and commercial real estate loans and generally restricting such loans to our primary market area. In determining whether to originate multi-family or commercial real estate loans, we also consider such factors as the financial condition of the borrower and the debt service coverage of the property. The Company intends to continue to make multi-family and commercial real estate loans as the market demands and economic conditions permit.

Commercial Lending

The Bank offers a variety of commercial loan services, including term loans, lines of credit and equipment and receivables financing. A broad range of short-to-medium term commercial loans, both collateralized and uncollateralized, are made available to businesses for working capital (including the support of inventory and receivables), business expansion (including acquisitions of real estate and improvements), and the purchase of equipment and machinery. Equipment loans are typically originated on both a one year line of credit basis and on a fixed-term basis ranging from one to five years. The purpose of a particular loan generally determines its structure.

The Bank's commercial loans primarily are underwritten in the Company's market areas on the basis of the borrower's ability to make repayment from the cash flow of their business and generally are collateralized by business assets, such as accounts receivable, equipment, and inventory. As a general practice, the Bank takes as collateral a security interest in any available real estate, equipment, or other business assets, although such loans may be made on an uncollateralized basis. Collateralized working capital loans are primarily secured by short-term assets whereas term loans are primarily secured by long-term assets.

The availability of funds for the repayment of commercial loans may be substantially dependent on the success of the business itself. Further, the collateral underlying the loans, which may depreciate over time, usually cannot be appraised with as much precision as residential real estate, and may fluctuate in value based on the success of the business.

Consumer Loans

Consumer loans made by the Bank have included automobiles, recreational vehicles, boats, second mortgages, home improvements, mobile home loans, home equity lines of credit, personal (collateralized and uncollateralized) and deposit account collateralized loans. The Bank's consumer loan portfolio consists primarily of loans to individuals for various consumer purposes, but includes some business purpose loans, primarily small trucks and automobiles, which are payable on an installment basis. Most of these loans are for terms of up to 60 months and, although generally collateralized by liens on various personal assets of the borrower, they may be originated without collateral. Consumer loans are made at fixed and variable interest rates and may be made based on up to a 7 year amortization schedule.

Consumer loans are attractive to us because they typically have a shorter term and carry higher interest rates than that charged on other types of loans. Consumer loans, however, do pose additional risks of collectability when compared to traditional types of loans granted by banks such as residential mortgage loans. In many instances, the Bank is required to rely on the borrower's ability to repay since the collateral may be of reduced value at the time of collection. Accordingly, the initial determination of the borrower's ability to repay is of primary importance in the underwriting of consumer loans.

Indirect automobile lending consists of automobile loans made by the Bank through the purchase of contracts from automobile dealers. Generally, the Bank will obtain fixed-rate automobile loans indirectly through various automobile dealerships located in its market areas. These automobile dealers are selected by us. Currently most of these loans were originated by 105 dealers located in our market area. Because the collateral is a deteriorating asset, the initial determination of the borrower's ability to pay is of primary importance. The indirect origination of consumer loan products generally requires funding of dealer reserves. These reserves are maintained for the benefit of the dealer who originated such loans, but such funding is subject to performance of certain loan conditions. The dealer is generally responsible to the Bank for the amount of the reserve only if a loan giving rise to the reserve becomes delinquent or the loan has been prepaid. The same process applies to indirect recreational vehicle lending.

Construction Loans

The Bank originates residential construction loans to finance the construction of single-family dwellings. Most of the residential construction loans are made to individuals who intend to erect owner-occupied housing on a purchased parcel of real estate. The Bank's construction loans to individuals typically range in size from $100,000 to $300,000. Construction loans also are made to contractors to erect single-family dwellings for resale. Construction loans are generally offered on the same basis as other residential real estate loans, except that a larger percentage down payment is typically required.

The Bank also may make residential construction loans to real estate developers for the acquisition, development and construction of residential subdivisions. The Bank has limited reliance on this type of loan. Such loans may involve additional risk attributable to the fact that funds will be advanced to fund the project under construction, which is of uncertain value prior to completion, and because it is relatively difficult to evaluate accurately the total amount of funds required to complete a project.

The Bank finances the construction of individual, owner-occupied houses on the basis of written underwriting and construction loan management guidelines. Construction loans are structured either to be converted to permanent loans with the Bank at the end of the construction phase or to be paid off upon receiving financing from another financial institution. Construction loans on residential properties are generally made in amounts up to 80% of appraised value. Construction loans to developers generally have terms of up to 12 months. Loan proceeds on builders' projects are disbursed in increments as construction progresses and as inspections warrant. The maximum loan amount for construction loans is based on the lesser of the current appraisal value or the purchase price for the property.

Loans collateralized by subdivisions and multi-family residential real estate generally are larger than loans collateralized by single-family, owner-occupied housing and also generally involve a greater degree of risk. Payments on these loans depend to a large degree on the results of operations and management of the properties, and repayment of such loans may be more subject to adverse conditions in the real estate market or the economy.

Loan Origination and Processing

Loan originations are derived from a number of sources. Residential loan originations can be attributed to real estate broker referrals, mortgage loan brokers, direct solicitation by the Bank's loan officers, present depositors and borrowers, builders, attorneys, walk-in customers and, in some instances, other lenders. Loan applications, whether originated through the Bank or through mortgage brokers, are underwritten and closed based on the same standards, which generally meet FHLMC underwriting guidelines. Consumer and commercial real estate loan originations emanate from many of the same sources. The legal lending limit of the Bank, as of June 30, 2008, was approximately $7.7 million.

The loan underwriting procedures followed by the Bank conform to regulatory specifications and are designed to assess the borrower's ability to make principal and interest payments and the value of any assets or property serving as collateral for the loan. Generally, as part of the process, a bank loan officer meets with each applicant to obtain the appropriate employment and financial information as well as any other required loan information. Upon receipt of the borrower's completed loan application, the Bank then obtains reports with respect to the borrower's credit record, and orders and reviews an appraisal of any collateral for the loan (prepared for the Bank through an independent appraiser). The loan information supplied by the borrower is independently verified. Loan officers or other loan production personnel in a position to directly benefit monetarily through loan solicitation fees from individual loan transactions do not have approval authority. Once a loan application has been completed and all information has been obtained and verified, the loan request is submitted to a final review process. As part of the loan approval process, all uncollateralized loans of more than $25,000 and all new collateralized loans of more than $750,000 require pre-approval by the Bank's loan committee. Loans to one borrower are subject to limits depending on our internal risk ratings.

Loan applicants are notified promptly of the decision of the Bank by telephone and a letter. If the loan is approved, the commitment letter specifies the terms and conditions of the proposed loan including the amount of the loan, interest rate, amortization term, a brief description of the required collateral and required insurance coverage. Prior to closing any long-term loan, the borrower must provide proof of fire and casualty insurance on the property serving as collateral which insurance must be maintained during the full term of the loan. Title insurance is required on loans collateralized by real property. Interest rates on committed loans are normally locked in at the time of application for a 30 to 45 day period.

Other Subsidiaries

The Company acquired a wholly-owned subsidiary, ASI Data Services, Inc. (ASI), through two stock purchases during 1993-1994. ASI initially provided data processing services to the Company and its subsidiaries. The Company's board transferred the assets and operations of ASI to the Bank in 1996, and ASI now is an inactive corporate subsidiary.

NBIG, a Maine corporation and a wholly-owned subsidiary of the Bank, was originally formed in 1982 and was formerly known as Northeast Financial Services, Inc. ("NFS"). It transitioned from an entity for real estate development projects, which terminated in fiscal 2005, to acquiring insurance agencies. Subsequent to the 2004 acquisition of Solon-Anson Insurance Agency, Inc. ("Solon Anson") by NFS, Solon-Anson was merged into NFS in April, 2005. NFS's name was then changed to Northeast Bank Insurance Group, Inc. in May 2005. NBIG now supports the Bank's insurance agencies, which allows the Bank to deliver insurance products to its customers. At June 30, 2008, investment in and loans to this subsidiary constituted 2.30% of the Company's total assets.

Employees

As of June 30, 2008, the Company, the Bank and its subsidiary together employed 226 full-time and 32 part-time employees. The Company's employees are not represented by any collective bargaining unit. The Company believes that its relations with its employees are good.

SUPERVISION AND REGULATION

The banking industry is extensively regulated under both federal and state law. This regulatory framework is intended primarily to protect depositors and the federal deposit insurance funds, and not for the protection of shareholders. The following discussion summarizes certain aspects of the regulatory framework applicable to the Company and Northeast Bank. To the extent that the following information describes statutory and regulatory provisions, it is qualified in its entirety by reference to the particular statutory and regulatory provisions.

Bank Holding Company Regulation

General. As a bank holding company registered under the Bank Holding Company Act of 1956 (the "BHCA"), the Company is subject to the regulation and supervision of, and inspection by, the Federal Reserve Board ("FRB"), its primary regulator. The Company also is registered as a Maine financial institution holding company under Maine law and is subject to regulation and examination by the Superintendent of Financial Institutions of the State of Maine ("Superintendent"). The Company is required to file reports with, and provide other information regarding its business operations and those of its subsidiaries to, the FRB and the Superintendent.

The BHCA prohibits a bank holding company, with certain limited exceptions, from (i) acquiring or retaining direct or indirect ownership or control of more than 5% of the outstanding voting stock of any company which is not a bank or bank holding company, or (ii) engaging directly or indirectly in activities other than those of banking, managing or controlling banks, or performing services for its subsidiaries unless such non-banking business is determined by the FRB to be so closely related to banking or managing or controlling banks as to be properly incident thereto. Generally, permissible activities for bank holding companies include, among other things, factoring accounts receivable, acquiring and servicing loans, leasing personal property, performing certain data processing services, acting as an agent or broker in selling credit life insurance and certain other types of insurance in connection with credit transactions, and conducting certain insurance underwriting activities. The BHCA does not place territorial limits on permissible non-bank activities of bank holding companies. In making determinations of what non-banking activities are permissible, the FRB is required to weigh the expected benefit to the public, such as greater convenience, increased competition or gains in efficiency, against the possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interest or unsound banking practices. Generally, bank holding companies, such as the Company, are required to obtain prior approval of the FRB to engage in any new activity not previously approved by the FRB. Further, despite prior approval, the FRB reserves the power to order any bank holding company or its subsidiaries to terminate any activity when the FRB has reasonable grounds to believe that continuation of such activity constitutes a serious risk to the financial soundness, safety, or stability of the bank holding company or any of its bank subsidiaries.

Financial Modernization. The Gramm-Leach-Bliley Financial Modernization Act of 1999 (the "GLB Act"), which amended the BHCA, significantly relaxed previously existing restrictions on the activities of bank holding companies and their subsidiaries to:

- allow bank holding companies that qualify as "a financial holding company" to engage in a substantially broader range of activities that are financial in nature;
- allow insurers and other financial service companies to acquire banks;
- remove various restrictions that apply to bank holding company ownership of securities firms and mutual fund advisory companies; and
- establish the overall regulatory structure applicable to bank holding companies that also engage in insurance and securities operations.

Under the GLB Act, an eligible bank holding company may elect to be a "financial holding company" and thereafter engage in a range of activities that are financial in nature and that are not permissible for bank holding companies. These activities, which can be conducted either directly or through a subsidiary, include those that are "financial in nature", such as insurance underwriting, securities underwriting and dealing and making merchant banking investments in commercial and financial companies. A financial holding company also may engage in any activity that the FRB determines by rule or order to be financial in nature, incidental to such financial activity, or complementary to a financial activity and does not pose a substantial risk to the safety and soundness of an institution or the financial system generally. In addition to these activities, a financial holding company may engage in those activities permissible for a bank holding company.

In order for a bank holding company to be eligible for financial holding company status, all of the subsidiary insured depository institutions must be "well-capitalized" and "well-managed" and have at least a satisfactory rating on its most recent Community Reinvestment Act of 1977 ("CRA") review. A bank holding company seeking to become a financial holding company must file a declaration with the FRB that it elects to become a financial holding company. If, after becoming a financial holding company, any of the insured depository institution subsidiaries should fail to continue to meet these requirements, the financial holding company would be prohibited from engaging in activities not permissible for bank holding companies unless it was able to return to compliance within a specified period of time.

Although Northeast Bank, our sole banking subsidiary, meets the capital, management, and CRA requirements, the Company has not made a declaration to elect to become a financial holding company and at this time has no plans to do so.

Banking Acquisitions. The BHCA requires, among other things, the prior approval of the FRB in any case where a bank holding company proposes to (i) acquire direct or indirect ownership or control of more than 5% of the outstanding voting stock of any bank or bank holding company (unless it already owns a majority of such voting shares), (ii) acquire all or substantially all of the assets of another bank or bank holding company, or (iii) merge or consolidate with any other bank holding company. The FRB will not approve any acquisition, merger, or consolidation that would result in a monopoly, or which would have a substantially anti-competitive effect, unless the anti-competitive impact of the proposed transaction is clearly outweighed by a greater public interest in meeting the convenience and needs of the community to be served. The FRB also is required to consider the financial and managerial resources and future prospects of the holding companies and banks, the projected capital adequacy on a post-acquisition basis, and the acquiring institution's performance under the CRA.

In addition, Maine law requires the prior approval of the Superintendent for (i) the acquisition of more than 5% of the voting shares of a Maine financial institution or any financial institution holding company that controls a Maine financial institution, or (ii) the acquisition by a Maine financial institution holding company of more than 5% of a financial institution or a financial institution holding company domiciled outside the State of Maine.

Interstate Banking and Branching. The Reigle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the "Interstate Banking and Branching Act") provides that bank holding companies which meet specified capital and management adequacy standards, and any state-imposed age requirements, are eligible to acquire banks in states other than their home states unless, as a result of such acquisition, the bank would control more than 10% of the total deposits of insured depository institutions in the United States or more than 30% of such deposits in that state (or other applicable state law limits).

Further, the Interstate Banking and Branching Act authorizes adequately capitalized and managed banks to cross state lines to merge with other banks, subject to certain restrictions, thereby creating interstate branches. A bank also may open new branches in a state in which it does not directly have banking operations if that state has enacted a law permitting de novo branching.

Maine law expressly authorizes interstate banking combinations that are approved by the Superintendent and do not result in deposit concentrations exceeding 30% of the total deposits of the State of Maine (unless such limitation is waived by the Superintendent). Further, interstate branch acquisitions and the establishment of de novo branches also are authorized under Maine law. However, if an out-of-state financial institution seeks to establish or acquire branches in Maine, the laws of the jurisdiction of such financial institution must expressly authorize, under conditions no more restrictive than the State of Maine, the Maine financial institution to engage in interstate branch acquisitions or establishment of de novo branches in that state.

Source of Strength; Safety and Soundness. Under FRB policy, the Company is expected to act as a source of financial strength to, and commit resources to support, Northeast Bank. In addition, any capital loans by a bank holding company to its subsidiary banks are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary banks. In the event of a bank holding company's bankruptcy, any commitment by the bank holding company to a Federal bank regulatory agency to maintain the capital of a subsidiary bank will be assumed by the bankruptcy trustee and entitled to a priority of payment.

There are a number of obligations and restrictions imposed on bank holding companies and their depository institution subsidiaries by law and regulatory policy that are designed to minimize potential loss to the depositors of such depository institutions and the FDIC insurance funds in the event of a depository institution default. For example, under the Federal Deposit Insurance Company Improvement Act of 1991 ("FDICIA"), to avoid receivership of an insured depository institution subsidiary, a bank holding company is required to guarantee the compliance of any insured depository institution subsidiary that may become "undercapitalized" with the terms of any capital restoration plan filed by such subsidiary with its appropriate Federal bank regulatory agency up to the lesser of (i) an amount equal to 5% of the institution's total assets at the time the institution became undercapitalized or (ii) the amount that is necessary (or would have been necessary) to bring the institution into compliance with all applicable capital standards as of the time the institution fails to comply with such capital restoration plan. See "-- Capital Adequacy Guidelines - Classification of Banking Institutions" and "- Enforcement, Policies and Actions".

In addition, the "cross-guarantee" provisions of FDICIA require insured depository institutions which are under common control to reimburse the FDIC for any loss incurred, or reasonably expected to be incurred, by the FDIC as a result of the default of a commonly controlled insured depository institution or for any assistance provided by the FDIC to a commonly controlled insured depository institution in danger of default. Accordingly, the cross-guarantee provisions enable the FDIC to access a bank holding company's healthy members of the FDIC. The FDIC may decline to enforce the cross-guarantee provisions if it determines that a waiver is in the best interest of the insurance fund. The FDIC's claims are superior to claims of stockholders of the insured depository institution or its holding company but are subordinate to claims of depositors, secured creditors and holders of subordinated debt (other than affiliates) of the commonly controlled insured depository institutions.

Under FDICIA, as amended, Federal banking regulatory agencies have adopted guidelines prescribing safety and soundness standards. These guidelines establish general standards relating to internal controls and information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth and compensation, fees and benefits. In general, the guidelines require, among other things, appropriate systems and practices to identify and manage the risk and exposures specified in the guidelines.

Bank Regulation

General. Northeast Bank is a Maine state-chartered banking corporation and a member of the Federal Reserve System and, as such, is subject to the supervision, examination, and regulation by the Maine Bureau of Financial Institutions and the FRB.

As a state-chartered commercial bank, Northeast Bank is subject to the applicable provisions of Maine law and the regulations adopted by the Maine Bureau of Financial Institutions. The FRB and the Maine Bureau of Financial Institutions regularly examine the operations of Northeast Bank and are given authority to approve or disapprove mergers, consolidations, the establishment of branches and similar corporate actions. Maine law and the Superintendant regulate (in conjunction with applicable federal laws and regulations), among other things, Northeast Bank's capital, permissible activities, reserves, investments, lending authority, the issuance of securities, payment of dividends, transactions with affiliated parties and borrowing. The federal and state banking regulators also have the power to prevent the continuance or development of unsafe or unsound banking practices or other violations of law.

Transactions with Affiliates. There are various legal restrictions on the extent to which the Company and any non-bank subsidiaries affiliated with Northeast Bank can borrow or otherwise obtain credit from Northeast Bank. Northeast Bank also is subject to certain restrictions on the purchase of, or investments in, the securities of, and purchase of assets from, the Company and of its non-bank subsidiaries, on loans or extensions of credit by a bank to third parties collateralized by the securities or obligations of the Company and any of its non-bank subsidiaries, on the issuance of guaranties, acceptances and letters of credit on behalf of the Company or any of its non-bank subsidiaries. Northeast Bank is subjected to further restrictions on most types of transactions with the Company and its non-bank subsidiaries which require the terms of such transactions to be substantially equivalent to the terms of similar transactions with non-affiliated entities.

Further, the Company and Northeast Bank are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit, lease or sale of property, or furnishing of services. For example, Northeast Bank may not generally require a customer to obtain other services from Northeast Bank or the Company, and may not require the customer to promise not to obtain other services from a competitor, as a condition to an extension of credit.

Loans to Insiders. Northeast Bank also is subject to certain restrictions imposed by federal and state banking regulatory agencies on extensions of credit to executive officers, directors, principal shareholders or any related interest of such persons. Sections 22(g) and 22(h) of the Federal Reserve Act, as amended, and Regulation O, promulgated by the FRB, provide that extensions of credit to such insiders (a) must be made on substantially the same terms, including interest rates and collateral as, and follow credit underwriting procedures that are not less stringent than those prevailing at the time for, comparable transactions with persons not covered above and who are not employees, (b) must not involve more than the normal risk of repayment or present other unfavorable features, and (c) may not exceed certain limitations on the amount of credit extended to such persons, individually and in the aggregate, which limits are based, in part, on the amount of Northeast Bank's capital. The regulators do allow small discounts on fees on residential mortgages for directors, officers, and employees. Northeast Bank also is subject to certain lending limits and restrictions on overdrafts to such persons and extensions of credit in excess of certain limits must be approved by the board of directors of Northeast Bank. A violation of these restrictions may result in the assessment of substantial civil monetary penalties on Northeast Bank or any officer, director, employee, agent or other person participating in the conduct of the affairs of Northeast Bank or the imposition of a cease and desist order.

Bank Subsidiaries' Activities. The powers of Maine-chartered banks include provisions designed to provide these banks with competitive equity to the powers of national banks. In addition, the GLB Act permits state banks to engage in activities that are permissible for subsidiaries of financial holding companies to the extent such activities are permitted under applicable state law. The GLB Act also expressly preserves the ability of state banks, such as Northeast Bank, to retain all existing subsidiaries. In order to form a financial subsidiary, a state bank must be "well capitalized." State banks with financial subsidiaries will be subject to certain capital deduction, risk management, and affiliate transaction rules. In this regard, FRB rules provide that state bank subsidiaries that engage only in activities that the bank could engage in directly will not be deemed to be a financial subsidiary.

Dividend Restrictions

The Company is a legal entity separate and distinct from Northeast Bank. The primary source of revenues and funds of the Company, including funds to pay dividends to our shareholders, have been and will likely continue to be from dividends, if any, paid to us by Northeast Bank. There are statutory and regulatory limitations on the payment of dividends by Northeast Bank to the Company as well as by the Company to its shareholders. As to the payment of dividends, Northeast Bank is subject to the laws and regulations of the State of Maine and to the regulations of the FRB.

If, in the opinion of the applicable federal bank regulatory authority, a depository institution or holding company under its jurisdiction is engaged in or is about to engage in an unsafe or unsound practice (which, depending on the financial condition of the depository institution or holding company, could include the payment of dividends), such authority may require, after notice and hearing (except in the case of an emergency proceeding where there is no notice or hearing), that such institution or holding company cease and desist from such practice. The Federal bank regulatory agencies have indicated that paying dividends that deplete a depository institution's or holding company's capital base to an inadequate level would be such an unsafe and unsound banking practice. Moreover, under FDICIA, an insured institution may not pay a dividend if payment would cause it to become undercapitalized or if it already is undercapitalized. See "- Capital Adequacy Guidelines - Prompt Corrective Regulatory Action". Moreover, the FRB and the FDIC have issued policy statements which provide that bank holding companies and insured depository institutions generally should only pay dividends out of current operating earnings.

At June 30, 2008, under dividend restrictions imposed under federal and state laws, Northeast Bank could declare, without obtaining governmental approvals, aggregate dividends to the Company of approximately $2,998,000.

Capital Adequacy Guidelines

Minimum Capital Requirements. The Company and Northeast Bank are required to comply with capital adequacy standards established by the FRB. There are two basic measures of capital adequacy for bank holding companies that have been promulgated by the FRB: a risk-based measure and a leverage measure.

The risk-based capital standards are designed to make regulatory capital requirements more sensitive to differences in credit and market risk profile among banks and bank holding companies, to account for off-balance sheet exposure and to lessen disincentives for holding liquid assets. Under these standards, assets and off-balance sheet items are assigned to broad risk categories, each with appropriate weights. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance sheet items. In addition, the Federal bank regulatory agencies may from time to time require that a banking organization maintain capital above the minimum limits, whether because of its financial condition or actual or anticipated growth. FRB policy also provides that banking organizations generally, and in particular those that are experiencing substantial internal growth or actively making acquisitions, are expected to maintain capital positions that are substantially in excess of the minimum supervisory levels, without significant reliance on intangible assets.

These risk-based capital standards define a two-tier capital framework. Under these regulations, the minimum ratio of total capital ("Total Capital") to risk-weighted assets (including certain off-balance sheet activities, such as stand-by letters of credit) is 8%. At least one-half of the Total Capital must be "Tier 1 Capital," consisting of common equity, retained earnings or undivided profits, qualifying non-cumulative perpetual preferred stock, and a limited amount of cumulative perpetual preferred stock and minority interests in the equity account of consolidated subsidiaries, less certain goodwill items and other intangible assets (i.e., at least 4% of the risk weighted assets). The remainder ("Tier 2 Capital") may consist of (a) the allowance for credit losses of up to 1.25% of risk-weighted risk assets, (b) preferred stock that does not qualify as Tier 1 Capital, (c) qualifying hybrid capital instruments, (d) perpetual debt, (e) mandatory convertible securities, and (f) subordinated debt and intermediate term-preferred stock up to 50% of Tier 1 Capital. Assets and off-balance sheet items are assigned to one of four categories of risk weights, based primarily on relative credit risk. The minimum guideline for Tier 1 Capital is 4.0%. At June 30, 2008, the Company's consolidated Tier 1 Capital ratio was 7.31% and its Total Capital ratio was 11.91%.

In addition, the FRB has established minimum leverage ratio guidelines for bank holding companies. The guidelines provide for a minimum Tier 1 Capital to average assets (less goodwill and certain other intangible assets) ("Leverage Ratio") of at least 3% plus an additional cushion of 100 to 200 basis points. The Company's Leverage Ratio at June 30, 2008, was 9.94%.

Federal bank regulatory agencies also have adopted regulations which require regulators to take into consideration concentrations of credit risk and risks from non-traditional activities, as well as an institution's ability to manage those risks, when determining the adequacy of an institution's capital. Other factors taken into consideration include: interest rate exposure; liquidity, funding and market risk; the quality and level of earnings; the quality of loans and investments; the effectiveness of loan and investment policies; and management's overall ability to monitor and control financial and operational risks, including concentrations of credit and non-traditional activities. This evaluation is made as part of the institution's regular safety and soundness examination. Further, each Federal banking agency prescribes standards for depository institution holding companies relating to internal controls, information systems, loan documentation, credit underwriting, interest rate exposure, asset growth, compensation, maximum rates of classified assets to capital, minimum earnings sufficient to absorb losses and other standards as they deem appropriate. In addition, pursuant to the requirements of FDICIA, Federal bank regulatory agencies all have adopted regulations requiring regulators to consider interest rate risk (when interest rate sensitivity of an institution's assets does not match its liabilities or its off-balance sheet position) in the evaluation of a bank's capital adequacy.

Northeast Bank is subject to substantially similar risk-based and leverage capital requirements as those applicable to the Company. As of June 30, 2008, Northeast Bank was in compliance with applicable minimum capital requirements.

Classification of Banking Institutions. Among other things, FDICIA provides Federal bank regulatory agencies with broad powers to take "prompt corrective action" with respect to depository institutions that do not meet minimum capital requirements. The extent of those powers depends upon whether the institutions in question are "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized," or "critically undercapitalized." A depository institution's capital tier will depend upon where its capital levels are in relation to various relevant capital measures, which include a risk-based capital measure and a leverage ratio capital measure, and certain other factors.

The Federal bank regulatory agencies have adapted regulations establishing relevant capital measures and relevant capital levels. Under these regulations, a bank will be considered:

	Total Risk-based Capital Ratio	Tier 1 Risk-based Capital Ratio	Leverage Ratio	Other
Well Capitalized	10% or greater	6% or greater	5% or greater	Not subject to any order or written directive to meet and maintain a specific capital level for any capital measure
Adequately Capitalized	8% or greater	4% or greater	4% or greater (3% in the case of a bank with a composite CAMEL rating of 1)	
Undercapitalized	less than 8%	less than 4%	less than 4% ((3% in the case of a bank with a composite CAMEL rating of 1)	
Significantly Undercapitalized	less than 6%	less than 3%	less than 3%	
Critically Undercapitalized				Ratio of tangible equity to total assets is less than or equal to 2%

Under certain circumstances, a depository institution's primary Federal bank regulatory agency may use its authority to reclassify a "well classified" bank as "adequately capitalized" or subject an "adequately capitalized" or "undercapitalized" institution to supervisory actions applicable to the next lower capital category if it determines that the bank is in an unsafe or unsound condition or deems the bank to be engaged in an unsafe or unsound practice and not have corrected the deficiency. The banking agencies are permitted to establish individual minimum capital requirements exceeding the general requirements described above. Generally, failing to maintain the status of a "well capitalized" or "adequately capitalized" depository institution subjects the institution to restrictions and limitations on its business that become progressively more severe as capital levels decrease. At June 30, 2008, Northeast Bank met the definition of a "well capitalized" institution.

Prompt Corrective Regulatory Action. Federal banking regulators are required to take "prompt corrective action" if an insured depository institution fails to satisfy certain minimum capital requirements and other measures deemed appropriate by the federal banking regulators. See "- Capital Adequacy Guidelines" and "- Enforcement Policies and Actions." Failure to meet the capital adequacy guidelines could subject a banking institution to capital raising requirements. A bank is prohibited from making any capital distribution (including the payment of a dividend) or paying a management fee to its holding company if the bank would thereafter be "undercapitalized". Limitations exist for "undercapitalized" depository institutions regarding, among other things, asset growth, acquisitions, branching, new lines of business, acceptance of brokered deposits and borrowings from the Federal Reserve System. These institutions also are required to submit a capital instruction plan that includes a guarantee from the institution's holding company. See "Bank Holding Company Regulation - Source of Strength; Safety and Soundness". A "significantly undercapitalized" depository institution may be subject to a number of requirements and restrictions, including orders to sell a sufficient quantity of voting stock to become "adequately capitalized," requirements to reduce total assets and cessation of receipt of deposits from correspondent banks. The appointment of a receiver or conservator may be required for "critically undercapitalized" institutions.

Enforcement Policies and Actions

The enforcement powers available to Federal banking regulators and the Supervisor over commercial banks and bank holding companies are extensive. This enforcement authority includes, among other things, the ability to assess civil money penalties, to issue cease-and-desist or removal orders, to initiate injunctive actions against banking organizations and affiliated parties, and, in extreme cases, to terminate deposit insurance. In general, these enforcement actions may be initiated for violations of laws and regulations and unsafe or unsound practices. Other actions or inactions may provide the basis for enforcement action, including misleading or untimely reports filed with the Federal bank regulatory agencies. Current law generally requires public disclosure of final enforcement actions.

Community Reinvestment Act

Bank holding companies and their subsidiary banks are subject to the provisions of the CRA and the regulations promulgated thereunder by the appropriate Federal bank regulatory agency. Under the terms of the CRA, Northeast Bank has a continuing and affirmative obligation consistent with its safe and sound operation to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community, consistent with the CRA. The CRA requires each appropriate Federal bank regulatory agency, in connection with its examination of a subsidiary depository institution, to assess such institution's record of meeting the credit needs of its community and to take such record into account in its evaluation of certain applications by that institution. The CRA also requires all institutions to make public disclosure of their CRA ratings. Further, such assessment also is part of the FRB's consideration of applications to acquire, merge or consolidate with, or assume the liabilities of, another banking institution or its holding company, or to open or relocate a branch office. In the case of a bank holding company applying for approval to acquire a bank or a bank holding company, the FRB will assess the record of each subsidiary bank of the applicant bank holding company in considering the application. Pursuant to current CRA regulations, an institution's CRA rating is based on its actual performance in meeting community needs. In particular, the rating system focuses on three tests: (a) a lending test, which evaluates the institution's record of making loans in its service areas; (b) an investment test, which evaluates the institution's record of investing community development projects, affordable housing, and programs benefiting low or moderate income individuals and businesses; and (c) a service test, which evaluates the institution's delivery of services through its branches, ATMs, and other offices. The current CRA regulations also clarify how an institution's CRA performance will be considered in the application process. Northeast Bank received a "satisfactory" CRA rating in its most recent examination.

FDIC Insurance Premiums

Northeast Bank is required to pay quarterly FDIC deposit insurance assessments. Under the FDIC's risk-based insurance system, insured institutions are currently assessed premiums based on the institution's capital position and other supervisory factors. Each financial institution is assigned to one of three capital groups - well capitalized, adequately capitalized or undercapitalized - and further assigned to one of three subgroups - within a capital group, on the basis of supervisory evaluations by the institution's primary federal and, if applicable, state supervisors and other information relevant to the institution's financial condition and the risk posed to the applicable FDIC deposit insurance fund. The actual assessment rate applicable to a particular institution (and any applicable refund) will, therefore, depend in part upon the risk assessment classification so assigned to the institution by the FDIC.

Gramm-Leach-Bliley Act

The GLB Act, enacted in 1999, amended and repealed portions of the Glass-Steagall Act and other federal laws restricting the ability of bank holding companies, securities firms, and insurance companies to affiliate with each other and enter into new lines of business. The GLB Act established a comprehensive framework to permit financial companies to expand their activities, including through affiliations, and to modify the federal regulatory structure governing some financial services activities. The increased authority of financial firms to broaden the type of financial services that they may offer to customers and to affiliates with other types of financial service companies may lead to further consolidation in the financial services industry. However, it also may lead to additional competition in these markets in which we operate by allowing new entrants into various segments of those markets that were not the traditional competitors in the segments. Furthermore, the authority granted by the GLB Act may encourage the growth of larger competitors.

With respect to bank securities activities, the GLB Act repeals the exemption from the definition of "broker" previously afforded to banks and replaces it with a set of limited exemptions that permits certain activities which have been performed historically by banks to continue. Further, the GLB Act amends the securities laws to include banks with the general definition of dealer. However, pending the passage of final regulations regarding the definition of “broker” and “dealer”, banks retain their current exemption from the definition.

In addition, the GLB Act imposes regulations on financial institution with respect to customer privacy. The GLB generally prohibits disclosure of customer information to non-affiliated third parties unless the customer had been given the opportunity to object and has not objected to such disclosure. Financial institutions are further required to provide written disclosure of their privacy policies to customers at the time the banking relationship is formed and annually thereafter. Financial institutions, however, are required to comply with state law if it is more protective of customer privacy than the GLB Act. The privacy provisions became effective in July 2001.

The GLB Act contains a variety of other provisions including a prohibition against ATM surcharges unless the customer has first been provided notice of the imposition and amount of the fee. The GLB Act reduces the frequency of CRA examinations for smaller institutions and imposes certain reporting requirements on depository institutions that make payment to non-governmental entities in connection with the CRA.

Anti-Money Laundering and Anti-Terrorism Legislation

Congress enacted the Bank Secrecy Act of 1970 (the "BSA") to require financial institutions, including the Company and Northeast Bank, to maintain certain records and to report certain transactions to prevent such institutions from being used to hide money derived from criminal activity and tax evasion. The BSA establishes, among other things: (a) record keeping requirements to assist government enforcement agencies in tracing financial transactions and flow of funds; (b) reporting requirements for Suspicious Activity Reports and Currency Transaction Reports to assist government enforcement agencies in detecting patterns of criminal activity; (c) enforcement provisions authorizing criminal and civil penalties for illegal activities and violations of the BSA and its implementing regulations; and (d) safe harbor provisions that protect financial institutions from civil liability for the cooperative efforts.

The USA Patriot Act of 2001 (the "USA Patriot Act") is intended to strengthen the ability of U.S. law enforcement agencies and the intelligence communities to work cohesively to combat terrorism on a variety of fronts. The USA Patriot Act amended the BSA and incorporates anti-terrorist financing provisions into the requirements of the BSA and its implementing regulations. Under the USA Patriot Act, FDIC insured banks and commercial banks are required to increase their due diligence efforts for correspondent accounts and private banking customers. The USA Patriot Act requires banks to engage in additional record keeping or reporting, requiring identification of owners of accounts, or of the customers of foreign banks with accounts, and restricting or prohibiting certain correspondent accounts. Among other things, the USA Patriot Act requires all financial institutions, including the Company and Northeast Bank to institute and maintain a risk-based anti-money laundering compliance program that includes a customer identification program, provides for information sharing with law enforcement and between certain financial institutions by means of an exemption from the privacy provision of the GLB Act, prohibits U.S. banks and broker-dealers from maintaining accounts with foreign "shell" banks, establishes due diligence and enhanced due diligence requirements for certain foreign correspondent banking and foreign private banking accounts and imposes additional record keeping requirements for certain correspondent banking arrangements. The USA Patriot Act also grants broad authority to the Secretary of the Treasury to take actions to combat money laundering, and federal bank regulators are required to evaluate the effectiveness of an applicant in combating money laundering in determining whether to approve any application submitted by a financial institution. The Company and Northeast Bank have adopted policies, procedures, and controls to comply with the BSA and the USA Patriot Act, and they engage in very few transactions of any kind with foreign financial institutions or foreign persons.

The Department of the Treasury's Office of Foreign Asset Control ("OFAC") administers and enforces economic and trade sanctions against targeted foreign countries, entities and individuals based on U.S. foreign policy and national security goals. As a result, financial institutions, including the Company and Northeast Bank, must scrutinize transactions to ensure that they do not represent obligations of, or ownership interests in, entities owned or controlled by sanctioned targets. In addition, the Company and Northeast Bank restrict transactions with certain targeted countries except as permitted by OFAC.

Sarbanes-Oxley Act

The Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley Act") implemented a broad range of corporate governance and accounting measures, executive compensation disclosure requirements, and enhanced and timely disclosure obligations for corporate information, all of which are designed to ensure that the stockholders of corporate America are treated fairly and have full and accurate information about the public companies in which they invest. All companies that file periodic reports with the SEC are affected by the Sarbanes-Oxley Act.

Specifically, the Sarbanes-Oxley Act and various regulations promulgated thereunder, established among other things:

- the creation of an independent accounting oversight board to oversee the audit of public companies and auditors who perform such audits;
- auditor independence provisions which restrict non-audit services that independent accountants may provide to their audit clients ;
- additional responsibilities regarding financial statements for the chief executive officer and chief financial officer of the reporting entity;
- a prohibition on personal loans to directors and officers, except certain loans made by financial institutions on non-preferential terms and in compliance with other bank regulatory requirements;
- additional corporate governance and responsibility measures which (a) require the chief executive officer and chief financial officer to certify financial statements and to forfeit salary and bonuses in certain situations, and (b) protect whistleblowers and informants;
- enhance independence and expertise requirements of members of audit committees;
- expansion of the audit committee's authority and responsibility by requiring that the audit committee (a) have direct control of the outside auditor, (b) be able to hire and fire the auditor, and (c) approve all non-audit services;
- mandatory disclosure by analysts of potential conflicts of interest; and
- enhanced penalties for fraud and other violations.

On September 11, 2007, the Company changed its listing from the American Stock Exchange to the NASDAQ Stock Exchange. Both exchanges have adopted corporate governance rules that have been approved by the SEC.

The Company has taken steps to comply with the provisions of the Sarbanes-Oxley Act and the regulations adopted thereunder. Based on our total assets, we are first required to provide management’s assessment of the company’s internal control over financial reporting in our annual report on Form 10-K filed for our first fiscal year ending on or after December 15, 2007 (i.e., fiscal year 2008). In addition, we are required to obtain an attestation report by our auditors for the annual report on Form 10-K filed for our first fiscal year ending on or after December 15, 2009 (i.e., fiscal year 2010). Compliance with the foregoing provisions is expected to increase our administrative costs.

Monetary Policy and Economic Control

The commercial banking business is affected not only by legislation, regulatory policies, and general economic conditions, but also by the monetary policy of the FRB. Changes in the discount rate on member bank borrowing, availability of borrowing at the "discount window," open market operations, the imposition of changes in reserve requirements against member banks' deposit and assets of foreign branches and the imposition of and changes in reserve requirements against certain borrowings by banks and their affiliates are some of the instruments of monetary policy available to the FRB. These monetary policies are used in varying combinations to influence overall growth and distributions of bank loans, investments and deposits, and these policies may affect interest rates charged on loans or paid on deposits. The monetary policies of the FRB have had a significant effect on the operating results of commercial banks and are expected to do so in the future. The monetary policies of these agencies are influenced by various factors, including inflation, unemployment, short-term and long-term changes in the international trade balance and in the fiscal policies of the United States Government. Future monetary policies and the effect of such policies on the future business and earnings of Northeast Bank cannot be predicted.

Industry Restructuring

For well over a decade, the banking industry has been undergoing a restructuring process which is anticipated to continue. The restructuring has been caused by product and technological innovations in the financial services industry, deregulation of interest rates and increased competition from foreign and nontraditional banking competitors, and has been characterized principally by the gradual erosion of geographic barrier to intrastate and interstate banking and the gradual expansion of investment and lending authorities for bank institutions.

Members of Congress and the administration may consider additional legislation designed to institute reforms to promote the viability of the industry. Such legislation could revise the federal regulatory structure for insured depository institutions; others could affect the nature of products, services, and activities that bank holding companies and their subsidiaries may offer or engage in, and the types of entities that may control depository institutions. There can be no assurance as to whether or in what form any such future legislation might be enacted, or what impact such legislation might have upon the Company or Northeast Bank.

STATISTICAL DISCLOSURE

The additional statistical information contained in Item 8(b) of this Form 10-K, "Financial Statements and Supplementary Data" as it relates to the disclosures required by Industry Guide 3 under the Securities Act of 1933, as amended, is incorporated herein by reference.

FORWARD-LOOKING STATEMENTS AND RISK FACTORS

This Annual Report on Form 10-K (including the Exhibits hereto) contains certain "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, such as statements relating to our financial condition, prospective results of operations, future performance or expectations, plans, objectives, prospects, loan loss reserve adequacy, simulation of changes in interest rates, capital spending and interest and non-interest revenue sources. These statements relate to expectations concerning matters that are not historical facts. Accordingly, statements that are based on management's projections, estimates, assumptions, and judgments constitute forward-looking statements. These forward-looking statements, which are based on various assumptions (some of which are beyond the Company's control), may be identified by reference to a future period or periods, or by the use of forward-looking terminology such as "believe", "expect", "estimate", "anticipate", "continue", "plan", "intend", "objective", "goal", "project", or other similar terms or variations on those terms, or the future or conditional verbs such as "will", "may", "should", "could", and "would". In addition, the Company may from time to time make such oral or written "forward-looking statements" in future filings with the Securities and Exchange Commission (including exhibits thereto), in its reports to shareholders, and in other communication made by or with the approval of the Company.

Such forward-looking statements reflect our current views and expectations based largely on information currently available to our management, and on our current expectations, assumptions, plans, estimates, judgments, and projections about our business and our industry, and they involve inherent risks and uncertainties. Although we believe that these forward-looking statements are based on reasonable estimates and assumptions, they are not guarantees of future performance and are subject to known and unknown risks, uncertainties, contingencies, and other factors. Accordingly, we cannot give you any assurance that our expectations will in fact occur or that our estimates or assumptions will be correct. We caution you that actual results could differ materially from those expressed or implied by such forward-looking statements due to a variety of factors, including, but not limited to, those related to the economic environment, particularly in the market areas in which the Company operates, competitive products and pricing, fiscal and monetary policies of the U.S. Government, changes in government regulations affecting financial institutions, including regulatory fees and capital requirements, changes in prevailing interest rates, acquisitions and the integration of acquired businesses, credit risk management, asset/liability management, changes in technology, changes in the securities markets, and the availability of and the costs associated with sources of liquidity. Accordingly, investors and others are cautioned not to place undue reliance on such forward-looking statements.

Potential risks, uncertainties, and other factors which could cause the Company's financial performance or results of operations to differ materially from current expectations or such forward-looking statements include, but are not limited to:

a) general economic conditions, either nationally or in the markets where the Company or its subsidiaries offer their financial products or services, may be less favorable than expected, resulting in, among other things, a deterioration of credit quality or in a decreased demand for our products or services;
b) A significant increase in competitive pressures in the banking and financial services industry and, more particularly, a significant increase in competition in the Company's market areas as described

under "Business -- Market for Services and Competition";

c) changes in the interest rate environment which could reduce our margins and increase defaults in our loan portfolio, including those described under "Management's Discussion and Analysis of Results of Operations and Financial Condition --Risk Management", and also may have a negative impact on the Company's interest rate exchange agreement;
d) the adequacy of the allowance for loan losses and the Bank's asset quality, including those matters described in "Management's Discussion and Analysis of Results of Operations and Financial Condition -- Results of Operations";
e) changes in political conditions or changes occurring in the legislative or regulatory environment that adversely affects the businesses in which we are engaged, including the impact of any changes in laws and regulations relating to banking, securities, taxes, and insurance;
f) changes in technology;
g) the ability to increase market share and to control expenses, and changes in consumer spending, borrowing, and saving habits;
h) changes in trade, tax, monetary, or fiscal policies, including the interest rate policies of the FRB;
i) money market and monetary fluctuations, and changes in inflation or in the securities markets;
j) future acquisitions and the integration of acquired businesses and assets;
k) changes in the Company's organizational structure and in its compensation and benefit plans, including those necessitated by pressures in the labor market for attracting and retaining qualified personnel;
l) the effect of changes in accounting policies and practices, as may be adopted by regulatory agencies as well as the Financial Accounting Standards Board;
m) unanticipated litigation, regulatory, or other judicial proceedings;
n) the success of the Company at managing the risks involved in the foregoing;
o) other one-time events, risks and uncertainties detailed from time to time in the filings of the Company with the Securities and Exchange Commission; and
p) continue deversification of income streams.

All written or oral forward-looking statements that are made or attributable to us are expressly qualified in their entirety by this cautionary notice. Such forward-looking statements speak only to the date that such statements are made, and the Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events.

The Company's results are strongly influenced by general economic conditions in its market areas in the western, central, and mid-coastal regions of the State of Maine. Deterioration in these conditions could have a material adverse effect on the quality of the Bank's loan portfolio and the demand for its products and services. In particular, changes in the real estate or service industries, or a slow-down in population growth, may adversely impact the Company's performance. See "Item 7. Management's Discussion and Analysis of Results of Operations and Financial Condition."

All forward-looking statements presume a continuation of the existing regulatory environment and monetary policy. The banking industry is subject to extensive state and federal regulation, and significant new laws or regulations, or changes in or repeals of existing laws or regulations may cause results of the Company to differ materially. Further, federal monetary policy, particularly as implemented by the FRB, significantly affect credit conditions for the Bank and its customers. Such changes could adversely impact the Company's financial results. In addition, the Sarbanes-Oxley Act of 2002 and the numerous rulemaking initiatives adopted or proposed in connection therewith or in reaction thereto have significantly increased the regulatory burdens of publicly held companies. Accordingly, the cost of compliance with, and the personnel necessary to satisfy the obligations imposed by, these regulatory initiatives may divert resources from our core business operations and may adversely affect our profitability. See "Item 1. Business Supervision and Regulation."

A significant source of risks arise from the possibility that losses will be sustained because borrowers, guarantors, and related parties fail to perform in accordance with the terms of their loans. The Bank has adopted underwriting and credit monitoring procedures and credit policies, including the establishment and review of the allowance for loan losses, that management believe are appropriate to minimize the risks in assessing the likelihood of nonperformance, tracking loan performance, and diversifying the Bank's loan portfolio. However, such policies may not prevent unexpected losses that could adversely affect the Company's results and the allowance for loan losses may not be adequate in all instances. See "Item 7. Management's Discussion and Analysis of Results of Operations and Financial Condition - Results of Operations,"" - Financial Condition," and" - Risk Management." Further, certain types of lending relationships carry greater risks of nonperformance and collectability, such as commercial and consumer loans. For a discussion of the risks associated with such lending relationships, see "Item 1. Business -- Lending Activities."

ITEM 1.a. Risk Factors

The following discusses risks that management believes are specific to our business and could have a negative impact on the Company’s financial performance. When analyzing an investment in the Company, the risks and uncertainties described below, together with all of the other information included or incorporated by reference in this report, should be carefully considered. This list should not be viewed as comprehensive and may not include all risks that may affect the financial performance of the Company:

Changes in interest rate risk may have adverse impact on the Company’s profitability.

The Company’s profitability is largely a function of the spread between the interest rates earned on interest-earning assets and the interest rates paid on deposits and other interest-bearing liabilities. Like most financial institutions, the Company’s net interest income and margin will be affected by general economic conditions and other factors, including fiscal and monetary policies of the Federal government and competition, that influence market interest rates and the Company’s ability to respond to changes in such rates. At any given time, the Company’s assets and liabilities may be such that they are affected differently by a change in interest rates. As a result, an increase or decrease in rates, the length of loan terms or the mix of adjustable- and fixed- rate loans or investment securities could have a positive or negative effect on its net income, capital and liquidity. Although management believes it has implemented strategies and guidelines to reduce the potential effects of changes in interest rates on results of operations, any substantial and prolonged change in market interest rates, including the slope of the interest rate curve, could adversely affect operating results.

Changes in economic conditions and the composition of the Company's loan portfolio could lead to higher charge-offs or an increase in the Company's provision for loan losses and may reduce the Company's net income.

As a lender, the Company is exposed to the risk that its borrowers may be unable to repay their loans and that any collateral securing the payment of their loans may not be sufficient to assure repayment in full. Credit losses are inherent in the lending business and could have a material adverse effect on the operating results of the Company. Adverse changes in the economy or business conditions, either nationally or in the Company's market areas, could increase credit-related losses and expenses and/or limit growth. Substantially all of the Company's loans are to businesses and individuals in its limited geographic area and any economic decline in this market could impact the Company adversely. We make various assumptions and judgments about the collectibility of our loan portfolio and provide for an allowance for loan losses based on a number of factors. If these assumptions are incorrect, the allowance for loan losses may not be sufficient to cover losses, thereby having an adverse effect on operating results, and may cause the Company to increase the allowance in the future by increasing the provision for loan losses. The Company has adopted underwriting and credit monitoring procedures and credit policies that management believes are appropriate to control these risks; however, such policies and procedures may not prevent unexpected losses that could have a material adverse affect on the Company's financial condition or results of operations.

Impairment risk may impact our profitability.

The Company regularly purchases U.S. Government-sponsored enterprise debt securities, U.S. Government-sponsored enterprise issued mortgage-backed securities, corporate debt securities and equity securities. The Company is exposed to the risk that the issuers of these securities may experience significant deterioration in credit quality which could impact the market value of the issue. The Company periodically evaluates its investments to determine if market value declines are other-than-temporary. Once a decline is determined to be other-than-temporary, the value of the security is reduced and a corresponding charge to earnings is recognized.

Strong competition within our markets may impact our profitability.

The financial services industry is highly competitive, with competition for attracting and retaining deposits and making loans coming from other banks and savings institutions, credit unions, mutual fund companies, insurance companies and other non-bank businesses. Many of the Company's competitors are much larger in terms of total assets and market capitalization, have a higher lending limit, greater access to capital and funding and offer a broader array of financial products and services. In light of these factors, the Company's ability to continue to compete effectively is dependent upon its ability to maintain and build relationships through top quality service.

The banking business is heavily regulated.

The banking industry is heavily regulated under both federal and state law. Banking regulations, designed primarily for the safety of depositors, may limit a financial institution's growth and the return to its investors, by restricting such activities as the payment of dividends, mergers with or acquisitions by other institutions, expansion of branch offices and the offering of securities. The Company is also subject to capitalization guidelines established by federal law and could be subject to enforcement actions to the extent that its subsidiary bank is found, by regulatory examiners, to be undercapitalized. It is difficult to predict what changes, if any, will be made to existing federal and state legislation and regulations or the effect that such changes may have on the Company's future business and earnings prospects. Any substantial changes to applicable laws or regulations could also subject the Company to additional costs, limit the types of financial services and products it may offer, and inhibit its ability to compete with other financial service providers.

If we do not maintain strong internal controls and procedures, it may impact our profitability.

Management diligently reviews and updates its internal controls, disclosure controls and procedures, and corporate governance policies and procedures. This system is designed to provide reasonable, not absolute, assurances that the internal controls comply with appropriate regulatory guidance. Any undetected circumvention of these controls could have a material adverse impact on the Company's financial condition and results of operations.

We are subject to litigation in the normal course of our business, which may impact profitability.

Although there is currently no litigation to which the Company is a party, future litigation that arises during the normal course of business could be material and have a negative impact on the Company's earnings. Future litigation could also adversely impact the reputation of the Company in the communities that it serves.

Attracting and retaining skilled personnel may impact the quality of services to customers.

Attracting and retaining key personnel is critical to the Company's success, and difficulty finding qualified personnel could have a significant impact on the Company's business due to the lack of required skill sets and years of industry experience. Management is cognizant of these risks, and succession planning is built into the Company's long-range strategic planning process.

Item 2. Properties

The principal executive and administrative offices of the Company and the Bank are located at 500 Canal Street, Lewiston, Maine ("Headquarters Building"). In 2005, the Bank entered into a 15 year lease with respect to the Headquarters Building, and we moved our principal executive and administrative offices to this four story building located in downtown Lewiston. We lease the entire building, a total of 27,000 square feet. For the first ten years of the lease, the annual rent expense is approximately $264,000. In addition to executive and administrative offices, this building also houses our operations, loan processing and underwriting, loan servicing, accounting, human resources and commercial lending departments. We also opened a 500 square foot branch office in this building.

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In addition to the branch office located in our Headquarters Building, we have 10 additional banking branches located, and fourteen insurance agency offices located in the State of Maine except one insurance agency office that is located in New Hampshire as set forth below.

Branch Locations	Ownership
232 Center Street, Auburn	Lease (1)
235 Western Avenue, Augusta	Fee Simple
11 Main Street, Bethel	Fee Simple
168 Maine Street, Brunswick	Fee Simple
2 Depot Street, Buckfield	Fee Simple
46 Main Street, Harrison	Fee Simple
882 Lisbon Street, Lewiston	Lease (2)
500 Canal Street, Lewiston	Lease (3)
26 Pleasant Street, Mechanic Falls	Fee Simple
77 Middle Street, Portland	Lease (4)
235 Main Street, South Paris	Fee Simple

Insurance Agency Locations	
59 Main Street, Anson, Maine	Fee Simple
232 Center Street, Auburn, Maine*	Lease (1)
235 Western Avenue, Augusta, Maine*	Fee Simple
4 Sullivan Square, Berwick, Maine	Lease (5)
11 Main Street, Bethel, Maine*	Fee Simple
346 Main Street, Jackman, Maine	Lease (6)
28 Main Street, Livermore Falls, Maine	Lease (7)
89 Main Street, Mexico, Maine	Fee Simple
2568 Main Street, Rangeley, Maine	Fee Simple
59 South Main Street, Rochester, New Hampshire	Lease (8)
423 U. S. Route 1, Scarborough, Maine	Lease (9)
235 Main Street, South Paris, Maine*	Fee Simple
472 Main Street, Thomaston, Maine	Lease (10)
10 Snell Hill Road, Turner, Maine	Fee Simple

*Each of these insurance agency locations are situated in an existing bank branch location at the address indicated.

(1) Lease term is ten years and expires May 1, 2016.
(2) Lease term is 15 years and expires January 14, 2014.
(3) Lease term is 15 years and expires July 15, 2020.
(4) Lease term is five years and expires September 30, 2012.
(5) Lease term is 21 years and expires December 31 2028.
(6) Lease term is one year and automatically renews in September each year.
(7) Lease is a tenant at will.
(8) Lease term is one year and automatically renews in December each year.
(9) Lease term is three years and expires July 31, 2010.
(10) Lease is a tenant at will.

The Bank's investment division leases space at 202 US Route One, Falmouth, Maine which has a term of five years and expires August 31, 2012. In addition, the Bank has purchased land in Windham, Maine and Northeast Bank Insurance Group, Inc. has purchased land in Jay, Maine.

On December 13, 2007 and January 8, 2008, Northeast Bank Insurance Group, Inc. (NBIG) purchased from a company owned by the president of NBIG the land and building of the leased insurance agency offices in Anson, Mexico and Rangeley, Maine and a land lot in Jay, Maine. The purchase price totaled $516,000. The purchase price for each transaction was based upon an independent third party appraisal, except for the price of the land lot. The purchase transaction was subject to approval by the Board of Directors of Northeast Bank, the sole owner of Northeast Bank Insurance Group.

On September 1, 2006, the Bank purchased its South Paris branch located at 235 Main Street, South Paris, Maine from a director of Northeast Bancorp for a purchase price of $400,000. The price was determined by an independent, third-party appraisal. The consideration paid was $297,000 in cash and 5,000 shares of Northeast Bancorp common stock (valued at $103,000 based on the $20.60 share price on August 31, 2006). This branch was previously leased from the director. This acquisition was not material to the balance sheet or the results of operations.

Item 3. Legal Proceedings

There are no pending legal proceedings to which the Company is a party or to which any of its property is subject. There are no material pending legal proceedings, other than ordinary routine litigation incidental to the business of banking, to which the Bank is a party or of which any of the Bank's property is the subject. There are no material pending legal proceedings to which any director, officer or affiliate of the Company, any owner of record beneficially of more than five percent of the common stock of the Company, or any associate of any such director, officer, affiliate of the Company or any security holder is a party adverse to the Company or has a material interest adverse to the Company or the Bank.

Item 4. Submission of Matters to a Vote of Security Holders

There were no matters submitted to a vote of the Company's shareholders during the fourth quarter of the fiscal year ended June 30, 2008.

Executive Officers of the Registrant

The name, age, and position of each executive officer of the Company and the Bank are set forth below along with such officer's business experience during the past five years. Officers are elected annually by the respective Boards of Directors of the Company and the Bank to hold office until the earlier of their death, resignation, or removal.

Name	Age	Position with Company and/or Bank
James D. Delamater	57	President and Chief Executive Officer (1)
Pender J. Lazenby	58	Chief Risk Officer
Marcel Blais	49	Chief Operating Officer
Robert S. Johnson	56	Chief Financial Officer (1)
Suzanne Carney	41	Clerk

(1) Each of these individuals serves both the Company and the Bank in the same capacities as indicated above.

James D. Delamater has been President, Chief Executive Officer, and a director of the Company and the Bank, since 1987.

Marcel Blais has been the Senior Vice President of the Bank - Retail Banking since 1998. Mr. Blais joined the Company in 1997 as the Vice President of the Bank - Branch Administration. Prior to joining the Company he served as Vice President of Atlantic Bank from 1995 to 1997, and as Vice President - Branch Manager of Casco Bank from 1977 until 1995.

Robert S. Johnson has been the Chief Financial Officer of the Bank since December 2001. Prior to joining the company he served as Mortgage Controller of Banknorth Group from 1998 to 1999 and as President and Chief Financial Officer of Pepperell Bank & Trust from 1999 to 2001.

Pender J. Lazenby has been a director of the Company and the Bank since 2003. Mr. Lazenby has also served as the Senior Vice President Chief Risk Officer since February 2005 and prior to joining the Company served in a variety of positions with Fleet Boston and Bank Boston prior to its acquisition in 1999.

Suzanne Carney has been Clerk of the Bank since March 1999 and has been with the Company since 1994 in the Accounting Division.

There is no family relationship between any of the directors or executive officers of the Company.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchase of Equity Securities

On September 11, 2007, the Company changed its listing from AMEX to NASDAQ. The common stock of Northeast Bancorp currently trades on the NASDAQ under the symbol "NBN". As of the close of business on September 1, 2008, there were approximately 2,315,182 shares of common stock outstanding held by approximately 420 stockholders of record.

The following table sets forth the high and low closing sale prices of the Company's Common Stock as reported on AMEX, and dividends paid during each quarter for periods indicated.

2007 – 2008	High	Low	Div Pd
Jul 1- Sep 30	18.63	15.82	.090
Oct 1 - Dec 31	17.30	13.72	.090
Jan 1 - Mar 31	15.53	13.31	.090
Apr 1 - Jun 30	14.79	11.17	.090

2006 - 2007	High	Low	Div Pd
Jul 1- Sep 30	21.39	19.18	.090
Oct 1 - Dec 31	19.77	18.20	.090
Jan 1 - Mar 31	20.30	18.34	.090
Apr 1 - Jun 30	18.89	16.60	.090

On September 19, 2008, the last reported sale price of the Company's Common stock as quoted on NASDAQ was $12.50. Holders of the Company's Common stock are entitled to receive dividends when and if declared by the Board of Directors out of funds legally available therefore, the amount and timing of future dividends payable on the Company's Common Stock will depend on, among other things, the financial condition of the Company, regulatory considerations, and other factors. The Company is a legal entity separate from the Bank, but its revenues are derived primarily from the Bank. Accordingly, the ability of the Company to pay cash dividends on its stock in the future generally will be dependent upon the earnings of the Bank and the Bank's ability to pay dividends to the Company. The payment of dividends by the Bank will depend on a number of factors, including capital requirements, regulatory limitations, the Bank's results of operations and financial condition, tax considerations, and general economic conditions. National banking laws regulate and restrict the ability of the Bank to pay dividends to the Company. See "Item 1.Business - Supervision and Regulation".

Stock repurchases under the 2006 Stock Repurchase Plan for the year ended June 30, 2008 totaled 137,800 shares at an average price per share of $16.79

Unregistered Sales of Equity Securities and Use of Proceeds

The following table provides the information on any purchase made by or on behalf of the Company of shares of Northeast Bancorp common stock during the indicated periods.

Period (1)	Total Number Of Shares Purchased (2)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Program	Maximum Number of Shares that May Yet be Purchased Under The Program (3)
Apr. 1 – Apr. 30	-	-	-	58,400
May 1 – May 31	-	-	-	58,400
Jun. 1 – Jun. 30	-	-	-	58,400

(1) Based on trade date, not settlement date.

(2) Represents shares purchased in open-market transactions pursuant to the Company's 2006 Stock Repurchase Plan.

(3) On December 15, 2006, the Company announced that its Board of Directors of the Company approved the 2006 Stock Repurchase Plan pursuant to which the Company is authorized to repurchase in open-market transactions up to 200,000 shares from time to time until the plan expires on December 31, 2008, unless extended.

Item 6. Selected Financial Data

	At or for the Year Ended June 30,				
	2008	2007	2006	2005	2004
	(Dollars in thousands except for Per Share Data)				
Selected operations data:					
Interest income	$ 35,398	$ 35,682	$ 35,456	$ 32,674	$ 28,124
Interest expense	21,051	20,097	16,761	13,967	12,079
Net interest income	14,347	15,585	18,695	18,707	16,045
Provision for loan losses	836	989	1,226	1,302	962
Other operating income (1)	10,510	7,903	6,578	5,083	4,670
Net securities gains	293	42	17	68	201
Other operating expenses (2)	21,855	20,075	18,209	16,684	14,799
Income before income taxes	2,459	2,466	5,855	5,872	5,155
Income tax expense	528	579	1,851	1,853	1,643
Net income	$ 1,931	$ 1,887	$ 4,004	$ 4,019	$ 3,512
Consolidated per share data:					
Net income:					
Basic	$ 0.82	$ 0.77	$ 1.61	$ 1.60	$ 1.38
Diluted	$ 0.82	$ 0.76	$ 1.59	$ 1.57	$ 1.35
Cash dividends	$ 0.36	$ 0.36	$ 0.36	$ 0.36	$ 0.35
Selected balance sheet data:					
Total assets	$ 598,274	$ 556,801	$ 562,918	$ 575,900	$ 538,754
Loans receivable	409,194	425,571	435,663	461,052	432,594
Deposits	363,374	364,554	395,293	396,219	377,820
Borrowings	186,830	147,564	124,860	136,293	121,443
Total stockholders' equity	40,273	40,850	39,096	39,870	36,453
Other ratios:					
Return on average assets	0.33%	0.34%	0.70%	0.71%	0.71%
Return on average equity	4.63%	4.59%	9.95%	10.39%	9.50%
Average equity to average total assets	7.23%	7.37%	7.07%	6.86%	7.51%
Common dividend payout ratio	44.10%	46.77%	22.40%	22.65%	25.93%

(1) Includes primarily fees for deposit, investment brokerage and trust services to customers and gains on the sale of loans.
(2) Includes salaries, employee benefits, occupancy, equipment and other expenses.

Item 7. Management's Discussion and Analysis of Results of Operations and Financial Condition

The Management's Discussion and Analysis of Results of Operations and Financial Condition, which follows, presents a review of the consolidated operating results of Northeast Bancorp, Inc. (the "Company") for the fiscal years ended June 30, 2008, 2007 and 2006. This discussion and analysis is intended to assist you in understanding the results of our operations and financial condition. You should read this discussion together with your review of the Company's Consolidated Financial Statements and related notes and other statistical information included in this report. Certain amounts in the years prior to 2008 have been reclassified to conform to the 2008 presentation.

A NOTE ABOUT FORWARD LOOKING STATEMENTS

This report contains certain "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, such as statements relating to our financial condition, prospective results of operations, future performance or expectations, plans, objectives, prospects, loan loss reserve adequacy, simulation of the impact of changes in interest rates, capital spending, and revenue sources. These statements relate to expectations concerning matters that are not historical facts. Accordingly, statements that are based on management's projections, estimates, assumptions, and judgments constitute forward-looking statements. These forward looking statements, which are based on various assumptions (some of which are beyond the Company's control), may be identified by reference to a future period or periods, or by the use of forward-looking terminology such as "believe", "expect", "estimate", "anticipate", "continue", "plan", "intend", “objective”, “goal”, “project”, or other similar terms or variations on those terms, or the future or conditional verbs such as "will", "may", "should", "could", and "would". In addition, the Company may from time to time make such oral or written "forward-looking statements" in future filings with the Securities and Exchange Commission (including exhibits thereto), in its reports to shareholders, and in other communications made by or with the approval of the Company.

Such forward-looking statements reflect our current views and expectations based largely on information currently available to our management, and on our current expectations, assumptions, plans, estimates, judgments, and projections about our business and our industry, and they involve inherent risks and uncertainties. Although we believe that these forward-looking statements are based on reasonable estimates and assumptions, they are not guarantees of future performance and are subject to known and unknown risks, uncertainties, contingencies, and other factors. Accordingly, we can not give you any assurance that our expectations will in fact occur or that our estimates or assumptions will be correct. We caution you that actual results could differ materially from those expressed or implied by such forward-looking statements due to a variety of factors, including, but not limited to, those related to the economic environment, particularly in the market areas in which the Company operates, competitive products and pricing, fiscal and monetary policies of the U.S. Government, changes in government regulations affecting financial institutions, including regulatory fees and capital requirements, changes in prevailing interest rates, acquisitions and the integration of acquired businesses, credit risk management, asset/liability management, changes in technology, changes in the securities markets, and the availability of and the costs associated with sources of liquidity. Accordingly, investors and others are cautioned not to place undue reliance on such forward-looking statements. For a more complete discussion of certain risks and uncertainties affecting the Company, please see "Item 1. Business - Forward-Looking Statements and Risk Factors" set forth in our Form 10-K. These forward-looking statements speak only as of the date of this report and we do not undertake any obligation to update or revise any of these forward-looking statements to reflect events or circumstances occurring after the date of this report or to reflect the occurrence of unanticipated events.

CRITICAL ACCOUNTING POLICIES

The Notes to the Consolidated Financial Statements contain a summary of Northeast Bancorp's significant accounting policies. The level of the allowance for loan losses is important to the presentation of the Company's results of operations and financial condition. The determination of what the loan loss allowance should be requires management to make subjective and difficult judgments, some of which may relate to matters that are inherently uncertain. Actual results may differ materially from these estimates and assumptions. See Note 1 to the Consolidated Financial Statements.

Allowance for Loan Losses

The allowance for loan losses represents management's estimate of probable losses inherent in the loan portfolio. This evaluation process is subject to numerous estimates and judgments. The frequency of default, risk ratings, and the loss recovery rates, among other things, are considered in making this evaluation, as are the size and diversity of individual large credits. Changes in these estimates could have a direct impact on the provision and could result in a change in the allowance. The larger the provision for loan loss, the greater the negative impact on our net income. Larger balance, non-homogeneous loans representing significant individual credit exposures are evaluated based upon the borrower's overall financial condition, resources, and payment record, the prospects for support from any financially responsible guarantors and, if appropriate, the realizable value of any collateral. The allowance for loan losses attributed to these loans is established through a process that includes estimates of historical and projected default rates and loss severities, internal risk ratings and geographic, industry, and other environmental factors. Management also considers overall portfolio indicators, including trends in internally risk-rated loans, classified loans, nonaccrual loans, and historical and forecasted write-offs; and a review of industry, geographic, and portfolio concentrations, including current developments. In addition, management considers the current business strategy and credit process, including credit limit setting and compliance, credit approvals, loan underwriting criteria, and loan workout procedures. Each portfolio of smaller balance, homogeneous loans, including residential real estate and consumer loans, is collectively evaluated for impairment. The allowance for loan losses is established via a process that includes historical delinquency and credit loss experience, together with analyses that reflect current trends and conditions. Management also considers overall portfolio indicators including historical credit losses, delinquent, non-performing and classified loans, trends in volumes, terms of loans, an evaluation of overall credit quality and the credit process, including lending policies and procedures and economic factors.

For a further description of our estimation process in determining the allowance for loan losses, see "Asset Quality" below.

GENERAL

Northeast Bancorp (the "Company") is a Maine corporation and a bank holding company registered with the Federal Reserve Bank of Boston ("FRB") under the Bank Holding Company Act of 1956. The Company also is a registered Maine financial institution holding company. The FRB is the primary regulator of the Company and the Company is also subject to regulation and examination by the Superintendent of the Maine Bureau of Financial Institutions. We conduct business from our headquarters in Lewiston, Maine and, as of June 30, 2008, from 11 banking offices, one financial center and 13 insurance agency offices all located in western and south-central Maine and one insurance agency located in Rochester, New Hampshire. At June 30, 2008, we had consolidated assets of $598.3 million and consolidated stockholders' equity of $40.3 million.

Northeast Bancorp's principal asset is all the capital stock of Northeast Bank (the "Bank"), a Maine state-chartered universal bank. Accordingly, the Company's results of operations are primarily dependent on the results of the operations of the Bank. In addition to the Bank's eleven branch offices, its investment brokerage division has an office in Falmouth, Maine from which investment, insurance and financial planning products and services are offered. The Bank's wholly-owned subsidiary, Northeast Bank Insurance Group, Inc., offers personal and commercial property and casualty insurance products. Four of its fourteen insurance agency offices operate in our Auburn, Augusta, Bethel, and South Paris, Maine branches.

Business Strategy

The principal business of the Bank consists of attracting deposits from the general public and applying those funds to originate or acquire residential mortgage loans, commercial loans, commercial real estate loans, indirect consumer loans and consumer loans. The Bank sells residential mortgage and commercial real estate loans into the secondary market. The Bank also invests in mortgage-backed securities, securities issued by United States Government-sponsored enterprises and municipal securities. The Bank emphasizes the growth of noninterest sources of income from trust management, financial planning, investment brokerage and insurance commissions. We increased insurance commissions in fiscal 2008 by expanding our insurance agency through acquisitions. The Bank's profitability depends primarily on net interest income, which is the difference between interest income earned from interest-earning assets (i.e. loans and investments) and interest expense incurred on interest-bearing liabilities (i.e. customer deposits and borrowed funds). Net interest income is affected by the relative balances of interest-earning assets and interest-bearing liabilities, and the rates received and paid on these balances.

Our goal is to continue modest, but profitable, growth by increasing our loan and deposit market share in our existing markets in western and south-central Maine, closely manage the yields on interest earning assets and rates on interest-bearing liabilities, introduce new financial products and services, increase the number of bank services per household, increase noninterest income from expanded trust, investment and insurance brokerage services and control the growth of noninterest expenses. It also is part of our business strategy to make targeted acquisitions in our current market areas from time to time when opportunities present themselves. For the twelve months ended June 30, 2008, we acquired three insurance agencies.

The Company's profitability is affected by the Bank's net interest income, which is affected by the measure known as interest rate spread, which is the difference between the average yield earned on its interest-earning assets and the average rate paid on its interest-bearing liabilities, or alternatively by interest margin, which is net interest income as a percentage of average interest-earning assets. Net income is also affected by the level of the provision for loan losses, noninterest income and noninterest expense of Northeast Bancorp and the Bank, and the effective tax rate. Noninterest income consists primarily of loan and deposit service fees, trust, investment brokerage and insurance brokerage fees and gains on the sales of loans and investments. Noninterest expenses consist of compensation and benefits, occupancy related expenses, deposit insurance premiums paid to the FDIC, and other operating expenses which include advertising, computer services, supplies, telecommunication and postage expenses.

Economic Conditions

We believe that our market area has generally witnessed an economic decline and a decrease in residential and commercial real estate values from 2007 through 2008. The economy and real estate markets in our market areas will continue to be significant determinants of the quality of our assets in future periods and our results of operations, liquidity and financial condition. We believe future economic activity will significantly depend on consumer confidence, consumer spending and business expenditures for new capital equipment, all of which are tied to strong employment.

EXECUTIVE SUMMARY

The following were significant factors comparing our results for fiscal 2008 to fiscal 2007:

- Three insurance agencies were acquired in twelve months ended June 30, 2008.

- Revenues from our investment brokerage, insurance, and trust and wealth management divisions increased by 28%.

- Net interest margins decreased to 270 basis points compared to 299 basis points in fiscal 2007, which resulting in a decrease in net interest income. Total earning assets increased $11.3 million as a result of a leverage strategy implemented in fiscal 2008 to slow the decrease in net interest income.

- The Company and the Bank are “well capitalized” under regulatory definitions. Risk based capital and leverage rations decreased compared to the prior year due to the recording of goodwill and other intangible assets resulting from the insurance agency acquisitions.

- The allowance for loan losses decreased by $100,000 in fiscal 2008, to $5,656,000, and, as a percentage of total loans, increased in fiscal 2008 to 1.38% compared to 1.35% in fiscal 2007 as total loans decreased $16.4 million in fiscal 2008.

- Net income increased to $1,931,289 for fiscal 2008 compared to $1,886,677 for fiscal 2007, an increase of $44,612.

RESULTS OF OPERATIONS

Comparison of Fiscal Years Ended June 30, 2008 and 2007

Overview

For the fiscal year ended June 30, 2008 ("fiscal 2008"), we reported net income of $1,931,289, or $0.82 per diluted share, as compared to $1,886,677, or $0.76 per diluted share, for the fiscal year ended June 30, 2007 ("fiscal 2007"), an increase of $44,612, or 2%. This increase was attributable to a decrease in the provision for loan losses and an increase in noninterest income which was partially offset by a decrease in net interest income due to a decrease in net interest margin and increased noninterest expense. The return on average assets was 0.33% in fiscal 2008 compared to 0.34% in fiscal 2007. The return on average equity was 4.63% in fiscal 2008 and 4.59% in fiscal 2007. The decrease in our return on average assets was due to the $19.3 million increase in average assets in fiscal 2008 compared to fiscal 2007. The increase in the return on average equity was due to increased net income for fiscal 2008 and a relatively constant level of shareholders' equity.

Net interest income decreased by 8% in fiscal 2008. This decrease was primarily due to a decrease in our net interest margin of 29 basis points compared to fiscal 2007. Average interest earning assets increased approximately $11.3 million as compared to the average interest earning assets in fiscal 2007 due to the increase in average available for sale securities of $31.8 million partially offset by a decrease in average loans of $18.7 million and a decrease in average interest-bearing deposits and regulatory stock of $1.8 million. Noninterest income increased 36% during fiscal 2008, primarily from increased insurance commission revenue, higher fees and services charges on loans and deposits and net securities gains. These increases were partially offset by lower brokerage commission revenue and lower gains on the sale of residential real estate and commercial real estate loans. The provision for loan losses decreased 15% primarily due to a decrease in total loans. Noninterest expense increased 9% during fiscal 2008, which was primarily due to increases in salaries and employee benefits expense, equipment expense, amortization of intangibles associated with the three insurance agency acquisitions in fiscal 2008, the full year impact of four insurance agency acquisitions completed in fiscal 2007, and other expenses.

Net Interest Income

Net interest income decreased by $1,238,688, or 8%, during fiscal 2008, primarily as a result of a decrease in net interest margin. Average interest earning assets increased $11.3 million during fiscal 2008 due to a $31.8 million increase in average investment securities that was partially offset by an $18.7 million decrease in average loans. Regulatory stock and interest-bearing deposits decreased $1.8 million. The decrease in average residential real estate, construction, commercial real estate and commercial loans of $22.6 million was partially offset by a $3.9 million increase in average consumer loans. The increase in average investment securities was due to increases in mortgage-backed securities used to pledge as eligible collateral primarily for structured repurchase agreements, and for FHLB advances, and securities sold under agreements to repurchase. Average interest-bearing deposits decreased by $13.8 million, or 4%, during fiscal 2008 primarily due to a decrease in average brokered deposits, which decreased by $19.3 million. Excluding the decrease in brokered deposits, average other deposits increased $5.5 million. Average short-term borrowings decreased during fiscal 2008 by $1.7 million, or 5%. Average borrowings increased, primarily due to structured repurchase agreements and debt incurred in the acquisition of insurance agencies. The yield on average interest earning assets decreased 19 basis points, to 6.60%, in fiscal 2008. The cost of funds increased 2 basis points, to 4.22%, due to an increase in the cost of interest-bearing deposits. Table 1 provided in Item 8 of this Form 10-K shows the average balances, yields and rates of assets, liabilities, and stockholders' equity of the Company for the past three years. The table below shows the changes from 2007 to 2008 in net interest income by category due to changes in rate and volume.

Rate/Volume Analysis for the Year Ended
June 30, 2008 versus June 30, 2007

	Difference Due to		
	Volume	Rate	Total
Investments	$ 1,574,259	$ 335,033	$ 1,909,292
Loans, net	(1,334,395)	(760,382)	(2,094,777)
FHLB deposits & other	(68,000)	(28,650)	(96,650)
Total interest-earning assets	171,864	(453,999)	(282,135)
Deposits	(549,860)	149,563	(400,297)
Repurchase agreements	(68,165)	(192,329)	(260,494)
Borrowings	1,818,309	(203,511)	1,614,798
Total interest-bearing liabilities	1,200,284	(246,277)	954,007
Net interest income	$ (1,028,420)	$ (207,722)	$ (1,236,142)

Rate/volume amounts which are partly attributable to rate and volume are spread proportionately between Volume and Rate based on the direct change attributable to rate and volume. Borrowings in the table above include FHLB advances, obligation under capital leases, structured repurchase agreements and junior subordinated debentures. The adjustments to interest income and yield required to make the presentation on a fully tax equivalent basis were $200,477 and $197,931 for the twelve months ended June 30, 2008 and 2007, respectively.

Provision for Loan Losses

The provision for loan losses in fiscal 2008 was $836,484, a decrease of $152,674, or 15%, compared to fiscal 2007. This decrease in the provision for loan losses reflects the overall decrease in loans of approximately $16.4 million. The impact of this decrease in loans on the provision for loan losses was partially offset by higher loan delinquency, higher classified and criticized loans, higher net losses, and non-performing loans for fiscal 2008. Net charge-offs were $936,500 in fiscal 2008 compared to $729,200 in fiscal 2007. This $207,300 increase was primarily in commercial real estate and indirect consumer loans. Net charge-offs to average loans outstanding was 0.23% in fiscal 2008 compared to 0.17% in fiscal 2007.

The allowance for loan losses at June 30, 2008 was $5,656,000 as compared to $5,756,000 at June 30, 2007, a decrease of $100,000, or 2%. The ratio of the allowance to total loans was 1.38% at June 30, 2008 compared to 1.35% at June 30, 2007. The ratio of the allowance for loan losses to non-performing loans was 73% at June 30, 2008 and 113% at June 30, 2007, reflecting a decrease of $100,000 in the allowance for loan losses and a $2,613,000 increase in non-performing loans, to $7,703,000, primarily due to non-performing residential real estate and commercial loans. Of total non-performing loans at June 30, 2008, $2,510,000 was current with principal and interest payments. Non-performing loans were 1.88% of total loans at June 30, 2008 as compared to 1.20% at June 30, 2007, also due to the increase in non-performing loans and a decrease in total loans. For additional information on the allowance for loan losses, see “Critical Accounting Policies” above, and see “Asset Quality” below for additional discussion on loans.

Noninterest Income

Noninterest income for the fiscal years ended June 30, 2008 and 2007 was $10,803,224 and $7,944,827, respectively, an increase of $2,858,397, or 36%, in fiscal 2008. Most of this increase was due to the increase in insurance commission income and gain from sale of securities.

Fees for other services to customers of $1,094,043 increased $51,395, or 5%, during fiscal 2008. This increase was due to higher ATM and debit card fee revenue as compared to fiscal 2007.

Net securities gains of $293,101 increased $250,752, or 592%, during fiscal 2008. The volume of securities sold in fiscal 2008 increased from fiscal 2007 due to restructuring the bond portfolio by selling U.S. government-sponsored enterprise bonds and replacing them with higher yielding mortgage-backed securities. Gains from the sale of equity and bond securities are subject to market and economic conditions, and there can be no assurance that gains reported in prior periods will be achieved in the future.

Gains on the sales of loans of $555,707 decreased $313,548, or 36%, during fiscal 2008. This decrease was primarily due to gains on the sales of commercial loans of $31,197 in fiscal 2008 compared to $455,680 in fiscal 2007. Gains on the sales of residential real estate loans were $524,510, an increase of $110,935 over fiscal 2007. Sold loan volume is subject to changing interest rates. Fixed rate residential real estate loans are sold to reduce our exposure to interest rate risk.

Investment commission revenue of $2,222,935 decreased $162,183, or 7%, during fiscal 2008. This decrease was primarily due to the equity market conditions in 2008.

Insurance commissions of $5,364,280 increased $3,033,845, or 130%, during the fiscal year 2008. The full year impact of the acquisition of the Palmer, Sturtevant & Ham, Southern Maine, and Russell insurance agencies acquired in fiscal 2007 accounted for $712,583 of the increase, and the partial year impact of the Hartford, Spence & Mathews and Hyler insurance agencies acquired in fiscal 2008 accounted for $1,663,949. The balance of the increase was due to contingent and growth bonus payments.

Bank owned life insurance ("BOLI") income of $457,198 increased $68,585, or 18%, during fiscal 2008. This increase was due to purchasing one new general account policy of $2,000,000 in bank owned life insurance and an increase in the average interest yield, net of mortality cost, to 3.99% in fiscal 2008 from 3.85% in fiscal 2007. The additions to cash surrender value are based on this average interest yield. These interest rates are determined by the life insurance companies and are reset quarterly or annually. Each policy is subject to minimum interest rates.

Other noninterest income of $721,589 decreased $84,935, or 11%, during fiscal 2008. This decrease was primarily due to the fiscal 2007 gain on sale of fixed assets of $73,963 from the sale of the former Lisbon Falls branch building and land, with no such corresponding transaction occurring in fiscal 2008 and a decrease in gains from the trading of covered call options of $10,639.

Noninterest Expense

Noninterest expense for fiscal years ended June 30, 2008 and 2007 was $21,854,454 and $20,075,186, respectively, an increase of $1,779,268, or 9%. The increase in fiscal 2008 was primarily due to an increase in salaries and employee benefits, intangible assets amortization and other expenses from the insurance agency acquisitions. Our efficiency ratio, which is noninterest expense as a percentage of the total of net interest income and noninterest income, increased to 86.9% during fiscal 2008 from 85.3% in fiscal 2007. The increase in operating expenses from the insurance agency acquisitions and the decrease in net interest income in fiscal 2008 compared to the prior year contributed to the increase in the efficiency ratio.

Salaries and employee benefits expense of $13,019,398 increased $997,361, or 8%, during the fiscal year 2008. This increase includes the salary and benefits of staff addition from insurance agency acquisitions of $1,275,909 partially offset by a decrease in deferred compensation expense of $233,478 and salary expense savings from unfilled positions. Total full-time equivalent employees were 244 compared to 214 at June 30, 2008 and 2007, respectively.

Occupancy expense of $1,792,827 increased $70,446, or 4%, during the fiscal year 2008. This increase was primarily due to increased ground maintenance, utilities and rent expense related to the lease insurance agencies acquired. These increases were partially offset by a decrease in amortization expense.

Equipment expense of $1,587,297 increased $56,021, or 4%, during the fiscal year 2008. The increase was due to higher depreciation and computer repairs and maintenance expense. These expenses were partially offset by lower furniture and equipment depreciation expense.

Other expense of $4,844,275 increased $359,367, or 8%, during fiscal year 2008. This increase was due to increases in professional fees, advertising expense, FDIC insurance, collections, deposit fraud losses, telephone, travel and dues and subscriptions expense. Other noninterest expense includes other-than-temporary write-downs on equity and non-marketable securities of $147,247 and $47,020, respectively, for fiscal 2008 compared to $50,442 and $248,482, respectively, in fiscal 2007, an aggregate decrease of $104,657. These other-than-temporary write-downs resulted from the periodic analysis by management of impaired securities whereby management determined that recovery of cost was unlikely within a reasonable period of time for certain equity and non-marketable securities. Also partially offsetting these increases were decreases of in postage and supplies expense.

The Company's effective tax rate was 21.5% and 23.5% for the fiscal years ended June 30, 2008 and 2007, respectively. See Note 12 in the Consolidated Financial Statements for additional information.

Comprehensive Income

The Company's comprehensive income was $2,541,763 and $2,594,600 during 2008 and 2007, respectively. Comprehensive income differed from our net income in 2008 and 2007 due to the change in the fair value of available-for-sale securities, net of income tax. In fiscal 2008, there was a net increase in fair value of $610,474 attributable to a decrease in net unrealized loss on available-for-sale securities, net of income tax. There was a net increase in fair value in fiscal 2007 of $707,923. See the Consolidated Statements of Changes in Shareholders' Equity and Note 16 in the Consolidated Financial Statements for additional information.

Comparison of Fiscal Years Ended June 30, 2007 and 2006

Overview

For the fiscal year ended June 30, 2007 ("fiscal 2007"), we reported net income of $1,886,677, or $0.76 per diluted share, as compared to $4,004,199, or $1.59 per diluted share, for the fiscal year ended June 30, 2006 ("fiscal 2006"), a decrease of $2,117,522, or 53%. This decrease was attributable to a decrease in net interest income due to a decrease in net interest margin and increased noninterest expense which were partially offset by a decrease in the provision for loan losses and an increase in noninterest income. The return on average assets was 0.34% in fiscal 2007 compared to 0.70% in fiscal 2006. The return on average equity was 4.59% in fiscal 2007 and 9.95% in fiscal 2006. The decrease in our return on average assets and return on average equity was due to decreased net income for fiscal 2007.

Net interest income decreased by 17% in fiscal 2007. This decrease was primarily due to a decrease in our net interest margin of 50 basis points compared to fiscal 2006, combined with a decrease in average interest earning assets of approximately $11.0 million as compared to the average interest earning assets in fiscal 2006. Of the decrease in average interest earning assets, average loans decreased $15.0 million and average interest-bearing deposits and regulatory stock decreased $0.6 million, partially offset by average investment securities, which increased $4.6 million. Noninterest income increased 20% during fiscal 2007 primarily from increased investment brokerage and insurance commission revenue, gains on the sale of residential real estate and commercial real estate loans and net securities gains. These increases were partially offset by lower fees and services charges on loans and deposits. The provision for loan losses decreased 19% primarily due to a decrease in loans. Noninterest expense increased 10% during fiscal 2007, which was primarily due to increases in salaries and employee benefits expense, equipment expense, amortization of intangibles associated with the four insurance agency acquisitions and other expenses.

Net Interest Income

Net interest income decreased by $3,110,245, or 17%, during fiscal 2007, primarily as a result of a decrease in net interest margin. Average interest earning assets decreased $11.0 million during fiscal 2007 due to a $15.0 million decrease in average loans that was partially offset by a $4.6 million increase in average investment securities. Regulatory stock and interest-bearing deposits decreased $0.6 million. The decrease in average residential real estate construction, commercial real estate and commercial loans of $22.9 million was partially offset by a $7.9 million increase in consumer loans. The increase in average investment securities was due to increases in mortgage-backed securities used to pledge as eligible collateral for FHLB advances, and securities sold under agreements to repurchase and municipal securities. Average interest-bearing deposits decreased by $13.5 million, or 4%, during fiscal 2007 primarily due to a decrease in average brokered deposits, which decreased by $18.8 million and reduced our dependency on wholesale funding. All other interest-bearing, non-maturing deposits decreased, in the aggregate amount of $14.1 million, offset by an increase in certificates of deposit of $19.4, for a net increase of $5.3 million. Average repurchase agreements increased during fiscal 2007 by $4.7 million, or 15%. Average borrowings increased, primarily due to debt incurred in the acquisition of insurance agencies. The yield on average interest earning assets increased 19 basis points, to 6.79%, in fiscal 2007. The cost of funds increased 75 basis points, to 4.20%, due to an increase in the cost of interest-bearing deposits. Table 1 provided in Item 8 of this Form 10-K shows the average balances, yields and rates of assets, liabilities, and stockholders' equity of the Company for the past three years. The table below shows the changes from 2006 to 2007 in net interest income by category due to changes in rate and volume.

Rate/Volume Analysis for the Year Ended
June 30, 2007 versus June 30, 2006

	Difference Due to		
	Volume	Rate	Total
Investments	$ 131,492	$ 375,969	$ 507,461

Loans, net	(1,075,851)	799,395	(276,456)
FHLB deposits & other	33,336	42,035	75,371
Total interest-earning assets	(911,023)	1,217,399	306,376
Deposits	(437,192)	2,775,059	2,337,867
Repurchase agreements	154,571	422,677	577,248
Borrowings	42,110	379,167	421,277
Total interest-bearing liabilities	(240,511)	3,576,903	3,336,392
Net interest income	$ (670,512)	$ (2,359,504)	$ (3,030,016)

Rate/volume amounts which are partly attributable to rate and volume are spread proportionately between Volume and Rate based on the direct change attributable to rate and volume. Borrowings in the table above include FHLB advances, obligation under capital leases and junior subordinated debentures. The adjustments to interest income and yield required to make the presentation on a fully tax equivalent basis were $197,931 and $117,702 for the twelve months ended June 30, 2007 and 2006, respectively.

Provision for Loan Losses

The provision for loan losses in fiscal 2007 was $989,158, a decrease of $237,255, or 19%, compared to fiscal 2006. This decrease in the provision for loan losses reflects the overall decrease in loans of approximately $10.0 million. The impact of this decrease in loans on the provision for loan losses was partially offset by higher loan delinquency, higher classified and criticized loans, higher net losses, and slightly lower non-performing loans for fiscal 2007. Net charge-offs were $729,200 in fiscal 2007 compared to $630,300 in fiscal 2006. This $98,900 increase was primarily in residential real estate and indirect consumer loans. Net charge-offs to average loans outstanding was 0.17% in fiscal 2007 compared to 0.14% in fiscal 2006.

The allowance for loan losses at June 30, 2007 was $5,756,000 as compared to $5,496,000 at June 30, 2006, an increase of $260,000, or 5%. The ratio of the allowance to total loans was 1.35% at June 30, 2007 compared to 1.26% at June 30, 2006. The ratio of the allowance for loan losses to non-performing loans was 113% at June 30, 2007 and 106% at June 30, 2006, reflecting an increase of $260,000 in the allowance for loan losses and a $105,000 decrease in non-performing loans, to $5,090,000, primarily due to non-performing commercial real estate loans. Of total non-performing loans at June 30, 2007, $2,038,000 million was current with principal and interest payments. Non-performing loans were 1.20% of total loans at June 30, 2007 as compared to 1.19% at June 30, 2006, also due to a decrease in total loans. For additional information on the allowance for loan losses, see "Critical Accounting Policies" above, and see "Asset Quality" below for additional discussion on loans.

Noninterest Income

Noninterest income for the fiscal years ended June 30, 2007 and 2006 was $7,944,827 and $6,594,881, respectively, an increase of $1,349,946, or 20%, in fiscal 2007. Most of this increase was due to the increase in investment brokerage and insurance commission income and gain from sale of loans.

Fees for other services to customers of $1,042,648 decreased $71,433, or 6%, during fiscal 2007. This decrease was due to lower transaction service fees and overdraft fee revenue as compared to fiscal 2006.

Net securities gains of $42,349 increased $25,014, or 144%, during fiscal 2007. The volume of securities sold in fiscal 2007 increased from fiscal 2006. Gains from the sale of equity and bond securities are subject to market and economic conditions, and there can be no assurance that gains reported in prior periods will be achieved in the future.

Gains on the sales of loans of $869,255 increased $560,478, or 182%, during fiscal 2006. This increase was primarily due to gains on the sales of commercial loans of $455,680. Gains on the sales of residential real estate loans were $413,575, an increase of $104,798 over fiscal 2006. Sold loan volume is subject to changing interest rates. Fixed rate residential real estate loans are sold to reduce our exposure to interest rate risk.

Investment commission revenue of $2,385,118 increased $615,818, or 35%, during fiscal 2007. This increase was primarily due to adding investment brokers and increased production from existing investment brokers.

Insurance commissions of $2,330,435 increased $413,613, or 21%, during the fiscal year 2007 due to the partial year impact of the acquisition of the Palmer, Sturtevant & Ham, and Southern Maine insurance agencies. The Russell Agency was acquired on June 28, 2007, the last business day of fiscal 2007.

Bank owned life insurance (BOLI) income of $388,613 increased $21,674, or 6%, during fiscal 2007. This increase was due to an increase in the average interest yield, net of mortality cost, to 3.85% in fiscal 2007 from 3.81% in fiscal 2006. The additions to cash surrender value are based on this average interest yield. These interest rates are determined by the life insurance companies and are reset quarterly or annually. Each policy is subject to minimum interest rates.

Other noninterest income of $806,524 decreased $197,473, or 20%, during fiscal 2007. This decrease was primarily due to the fiscal 2006 deposit premium received of $500,845 from the sale of the deposits and certain loans of the Lisbon Falls branch, with no such corresponding transaction occurring in fiscal 2007. This decrease was partially offset by an increase in trust fee revenue of $83,384, a change in gain on the sales of fixed assets of $202,326 and an increase in gains from the trading of covered call options of $31,412. The gain on the sale of fixed assets in fiscal 2007 of $73,963 was primarily from the sale of the former Lisbon Falls branch building and land compared to a loss on the sale of fixed assets in fiscal 2006 of $128,363.

Noninterest Expense

Noninterest expense for fiscal years ended June 30, 2007 and 2006 was $20,075,186 and $18,208,504, respectively, an increase of $1,866,682, or 10%. The increase in fiscal 2007 was primarily due to an increase in salaries and employee benefits and other expenses. Our efficiency ratio, noninterest expense as a percentage of the total of net interest income and noninterest income, increased to 85.3% during fiscal 2007 from 72.0% in fiscal 2006. The decrease in net interest income in fiscal 2007 compared to the prior year was a significant factor contributing to the increase in the efficiency ratio.

Salaries and employee benefits expense of $12,022,037 increased $1,384,279, or 13%, during the fiscal year 2007. This increase includes the incentive compensation paid based on the gains on the sales of commercial loans and insurance agency acquisition totaling $431,000, and the salary and benefits for new positions in residential real estate lending, investment brokerage and the insurance agencies. Total full-time equivalent employees were 214 compared to 201 at June 30, 2007 and 2006, respectively.

Occupancy expense of $1,722,381 increased $49,876, or 3%, during the fiscal year 2007. This increase was primarily due to mold remediation for our Bethel branch, the full year impact of the headquarters capital lease, increased amortization expense, increased utilities and real estate taxes. These increases were partially offset by a decrease in rent expense resulting from the consolidation of leased space during fiscal 2006.

Equipment expense of $1,531,276 increased $91,038, or 6%, during the fiscal year 2007. Software depreciation expense and software licensing amortization expense for Internet banking software and conversion fees for the insurance agency core system increased compared to fiscal year 2006. These expenses were partially offset by lower moving expenses compared to that incurred in fiscal year 2006 due to relocating staff and equipment to the Gateway Building in Lewiston.

Other expense of $4,484,908 increased $267,933, or 6%, during fiscal year 2007. This increase was due to increases in loan expense, primarily collection expenses incurred as delinquencies and workout loans increased during fiscal 2007, supplies expense, due to reprinting of forms for image processing of customer transactions, computer services expense, resulting from converting to image processing and a higher volume of investment brokerage transactions, and business insurance. Other noninterest expense includes other-than-temporary write downs on equity and non-marketable securities of $50,442 and $248,482, respectively, for fiscal 2007 compared to $38,394 and $42,257, respectively, in fiscal 2006, an aggregate increase of $218,273. These other-than-temporary write downs resulted from the periodic analysis by management of impaired securities whereby management determined that recovery of cost was unlikely within a reasonable period of time for certain equity and non-marketable securities. Partially offsetting these increases was a decrease of $51,698 in advertising expense and a decrease in dues and assessments of $47,356.

The Company's effective tax rate was 23.5% and 31.7% for the fiscal years ended June 30, 2007 and 2006, respectively. See Note 12 in the Consolidated Financial Statements for additional information.

Comprehensive Income

The Company's comprehensive income was $2,594,600 and $2,051,917 during 2007 and 2006, respectively. Comprehensive income differed from our net income in 2007 and 2006 due to the change in the fair value of available-for-sale securities, net of income tax. In fiscal 2007, there was a net increase in fair value of $707,923 due to a net unrealized loss on investments available-for-sale, net of income tax. There was a net decrease in fair value in fiscal 2006 of $1,952,282. See the Consolidated Statements of Changes in Shareholders' Equity and Note 16 in the Consolidated Financial Statements for additional information.

FINANCIAL CONDITION

The Company's total assets increased $41,472,670, or 7%, to $598,273,650 at June 30, 2008 compared to $556,800,980 at June 30, 2007. This increase was primarily due to a $48,134,907 increase in available for sale securities, partially offset by a decrease in total loans, primarily residential real estate and commercial loans. The funding of the securities was provided from structured repurchase agreements. Stockholders' equity totaled $40,273,312 and $40,849,878 at June 30, 2008 and 2007, respectively, a decrease of $576,566. Stockholders' equity was decreased by share repurchases and retirements of $2,314,330 and payment of cash dividends of $851,785 which were partially offset by net income of $1,931,289, a decrease in net unrealized losses on available-for-sale securities of $610,474, proceeds from the exercise of previously granted stock options of $45,125 and stock grant of $2,661.

Cash and Cash Equivalents

Average cash and cash equivalents (cash and due from bank and short-term investments) decreased $1,885,666, to $9,288,394, in fiscal 2008 as compared to $11,174,060 in fiscal 2007. This decrease was due to a decrease in short-term investments.

Investments Securities and Other Interest-earning Assets

The average balance of the available-for-sale securities portfolio was $116,558,331 and $84,705,459 for fiscal 2008 and fiscal 2007, respectively. This increase of $31,852,872, or 38%, was primarily due to a leverage strategy executed through increasing mortgage-backed securities funded with structured repurchase agreements. The structured repurchase agreements were imbedded primarily with purchased interest rate caps to reduce the interest rate risk our liability sensitive balance sheet (interest-bearing liabilities reprice more quickly than interest-bearing assets) has to rising interest rates. The portfolio is comprised of U.S. Government-sponsored enterprises, mortgage-backed securities, municipal securities, and equity and bank-issued trust preferred securities, with most of our investment portfolio consisting of federal agency mortgage-backed securities and short-term U.S. Government-sponsored enterprise bonds. See Item 8, Tables 2 and 3, for a detail of available-for-sale securities and investment maturities, respectively, and Note 8 of the Consolidated Financial Statements for details on the structured repurchase agreements.

All of the Company's securities are classified as available-for-sale and were carried at fair value of $134,482,977 and $86,348,070 as of June 30, 2008 and 2007, respectively. These securities had net unrealized losses after taxes of $1,304,072 at June 30, 2008 and $1,914,546 at June 30, 2007. See Note 2 to the Consolidated Financial Statements. These unrealized losses do not impact net income or regulatory capital, but are recorded as an adjustment to stockholders' equity, net of related deferred income taxes, and are a component of comprehensive income contained in the Consolidated Statements of Changes in Stockholders' Equity.

Loans

The average balance for loans, including loans held for sale, was $414,837,099 in fiscal 2008, compared to $433,576,281 in fiscal 2007. This decrease of $18,739,182, or 4%, in our average balance for loans at June 30, 2008, was attributable to decreases in average residential real estate, commercial real estate, commercial, and construction loans, partially offset by an increase in average consumer loans. See Item 8, Tables 4 and 5, for additional information on the composition of the loan portfolio and loan maturities, respectively.

Residential real estate loans averaged $144,084,050 in fiscal 2008, as compared to $147,432,431 in fiscal 2007. This decrease of $3,348,381, or 2%, was attributable to a decrease in residential real estate loans and home equity lines of credit. We continued to sell most of the 15 year and 30 year fixed rate residential real estate loans originated by us into the secondary market. Residential real estate loans were 34% of the total loan portfolio at both June 30, 2008 and 2007, respectively. Of residential real estate loans at June 30, 2008, approximately 34% were variable rate products, compared to 37% at June 30, 2007. This decrease in the percentage of variable rate products resulted from customers replacing variable rate products with fixed rate products, which were subsequently sold into the secondary market. We expect variable rate residential real estate loans to decrease, causing the liability sensitivity of the consolidated balance sheet to increase.

Commercial real estate and commercial loans both decreased during fiscal 2008. The decrease reflects the Bank tightening of its credit underwriting standards as delinquencies and classified and criticized commercial real estate and commercial loans increased, and priced the origination of these loans to reflect risk. Generally, competition for new and renewing commercial real estate and commercial loans has been intense. Frequently, the interest rates offered by competing banks appeared not to factor in credit risk.

Commercial real estate loans averaged $106,810,660 in fiscal 2008 and $116,384,948 in fiscal 2007. This decrease of $9,574,288, or 8%, reflects the factors noted above. Our focus was to lend primarily to small businesses within our market areas. This portfolio consists of loans secured primarily by income-producing commercial real estate and multifamily residential real estate. Commercial real estate loans were 27% and 26% of the total loan portfolio at June 30, 2008 and 2007, respectively. Approximately 95% of the commercial real estate loans were variable rate product, with this portfolio reflecting our desire to minimize the interest rate risk, compared to approximately 94% of this portfolio at June 30, 2007.

Construction loans averaged $5,629,860 in fiscal 2008 and $7,009,832 in fiscal 2007. This decrease of $1,379,972, or 20%, was primarily in commercial construction loans. Construction loans were 1% of the total loan portfolio at June 30, 2008 and 2007, respectively. Most construction loans are subject to interest rates based on the prime rate, have contractual maturities less than 12 months, and disbursements are made on construction-as-completed basis and verified by inspection. Approximately 37% of the construction loans were variable rate product at June 30, 2008, compared to approximately 60% at June 30, 2007.

Commercial loans averaged $36,385,671 in fiscal 2008 and $44,762,107 in fiscal 2007. This decrease of $8,376,436, or 19%, reflects the above factors and reduced warehouse lines of credit. Commercial loans were 8% and 10% of total loans at June 30, 2008 and 2007, respectively. Variable rate products comprised 67% and 58% of this loan portfolio at June 30, 2008 and 2007, respectively. The commercial loan credit risk exposure is highly dependent on the cash flow of the customer's business. The Company mitigates credit risk by strictly adhering to our underwriting and credit policies.

Consumer and other loans averaged $119,194,281 in fiscal 2008 and $115,314,393 in fiscal 2007. This increase of $3,879,888, or 3%, was attributable to new recreational vehicle loans. Consumer and other loans comprised 29% of the total loan portfolio at June 30, 2008 and 2007. Consumer and other loans, including indirect auto and recreational vehicle are mostly fixed rate products. At June 30, 2008 and 2007, we held $34,980,847 and $36,808,246 of indirect auto loans, respectively. Indirect auto, indirect RV and indirect mobile home loans together comprised approximately 95% of total consumer and other loans, at both June 30, 2008 and 2007. The detail of consumer loans at June 30, 2008 and 2007 appears in the following table. The Company underwrites all automobile dealer financed, recreational vehicle and mobile home loans to protect credit quality. The Company pays a nominal one-time origination fee on these loans. The fees are deferred and amortized over the contractual life of the loan as a yield adjustment. Management attempts to mitigate credit and interest rate risk by keeping the products offered short-term, earning a rate of return commensurate with the risk, and lending to individuals in the Company's known market areas. We did experience an increase in consumer loan delinquency from 1.69% to 2.73%, an increase in non-performing from $476,000 to $640,000, and an increase in the net charge-off of consumer loans from $443,000 to

$630,000 for the fiscal years ended June 30, 2007and 2008 respectively.

	Consumer Loans			
	June 30, 2008	% of Total	June 30, 2007	% of Total
Indirect Auto	$ 34,980,847	30%	$ 36,808,246	31%
Indirect RV	54,915,583	47%	51,611,223	43%
Indirect Mobile Home	21,759,537	18%	24,961,562	21%
Subtotal Indirect	111,655,967	95%	113,381,031	95%
Other	5,390,792	5%	5,499,692	5%
Total	$ 117,046,759	100%	$ 118,880,723	100%

BOLI averaged $11,240,716 in fiscal 2008 and $9,082,562 in fiscal 2007. One new general account policy was purchased in fiscal 2008 for $2,000,000. BOLI assets were invested in the general account of three insurance companies and separate accounts in a fourth insurance company. A general account policy's cash surrender value is supported by the general assets of the insurance company. A separate account policy's cash surrender value is supported by assets segregated from the general assets of the insurance company. Standard and Poor's rated these companies AA- or better at June 30, 2008. Interest earnings, net of mortality costs, increase the cash surrender value. These interest earnings are based on interest rates reset each year, subject to minimum interest rates. The increases in cash surrender value offset all or a portion of the increase in employee benefit costs. The increase in cash surrender value was recognized in other income and was not subject to income taxes. Borrowing on or surrendering the policy may subject the Bank to income tax expense on the increase in cash surrender value. For these reasons, management considers BOLI an illiquid asset. BOLI represented 26.76% of capital plus the allowance for loan losses at June 30, 2008.

Goodwill and intangible average assets were $4,306,182 and $6,819,158, respectively, for fiscal 2008, and $1,404,753 and $3,015,589, respectively, for fiscal 2007. These increases resulted from the acquisition of three insurance agencies during fiscal 2008. The allocation of the purchase price paid for the three insurance agency acquisitions in excess of tangible assets acquired added $1,545,110 to goodwill and $5,005,000 to intangibles in the form of customer lists and non-compete agreements. These intangibles are being amortized over lives from 7 to 19 years, with an average of 14.16 years. Goodwill and intangibles are subject to impairment testing annually. No impairment expense was recognized in fiscal 2008 or fiscal 2007. See Note 1 of the consolidited Financial Statements for additional information.

Deposits

Average demand deposit accounts were $33,317,154 for the year ended June 30, 2008 as compared to $35,420,046 in fiscal 2007. The decrease of $2,102,892, or 6%, was related to the loss of commercial real estate and commercial loan customers during fiscal 2008.

Average interest-bearing deposits decreased by $13,843,188, or 4%, during fiscal 2008 to $328,757,978. This decrease was primarily due to decreased brokered time deposits, NOW, and regular savings deposits, a total of $24,693,816. This decrease was partially offset by increases in average certificates of deposit balances of $6,423,506, or 3%, to $225,339,160, and average money market increased $4,427,122, or 47%, to $13,784,458. Both increases were due to promotions. These increases allowed the Bank to decrease brokered time deposits as they matured. Average brokered time deposit balances decreased $19,254,584, or 52%, to $18,097,886 in fiscal 2008 from $37,352,470 in fiscal 2007. NOW and savings balances declined as customers moved balances to higher yielding money market and time deposits. Average NOW accounts decreased $3,528,326, or 6%, during fiscal 2008 to $51,138,524. The average interest rate paid on NOW accounts decreased from 2.26% in fiscal 2007 to 1.99% in fiscal 2008. Average money market accounts increased $4,427,122, or 47%, to $13,784,458 in fiscal 2008. Average savings accounts decreased $1,910,906, or 9%, to $20,397,950 during fiscal 2008. The average interest rate paid on savings accounts decreased from 0.87% in fiscal 2007 to 0.79% in fiscal 2008. The average interest rate paid on money market accounts increased from 2.36% in fiscal 2007 to 3.05% in fiscal 2008. The average interest rate paid on certificates of deposit increased from 4.62% in fiscal 2007 to 4.72% in fiscal 2008. See Item 8, Table 10, for the scheduled maturities of certificates of deposit of $100,000 or more.

We use brokered time deposits as part of our overall funding strategy and as an alternative to retail certificates of deposits, FHLB advances, and junior subordinated debentures, to fund the growth of our earning assets. These deposits are limited by policy to 25% of total assets and individual brokered time deposit maturities do not exceed $5 million in any one month. We use five national brokerage firms to source time deposits, which are obtained through agents of the brokerage company soliciting customers from throughout the United States. The terms of these brokered time deposits allow for termination prior to maturity only in the case of the depositor’s death, have maturities generally beyond one year and have interest rates equal to or slightly above comparable FHLB advances. At June 30, 2008, outstanding brokered time deposits of $12,596,615 as a percentage of total assets was 2.11%, compared to 4.05% at June 30, 2007. The average interest rate paid on brokered time deposits increased from 4.69% in fiscal 2007 to 5.14% in fiscal 2008. Generally, interest rates paid on brokered time deposits exceed rates paid on FHLB advances with similar maturities, but the incremental interest expenses did not have a material impact on the results of operations for fiscal 2008.

Other Funding Sources

Short-term borrowings, which consist of securities sold under repurchase agreements and other sweep accounts, Federal Home Loan Bank of Boston (FHLB) advances, structured repurchase agreements and junior subordinated debentures are the Company's sources of funding other than deposits.

Average short-term borrowings during fiscal 2008 were $34,449,012, compared to $36,144,925 during fiscal 2007, a decrease of $1,695,913, or 5%. This liability was collateralized by U.S. government-sponsored enterprise and federal agency mortgage-backed securities. Other sweep accounts were subject to excess insurance coverage. See Note 8 to the Consolidated Financial Statements.

Average FHLB advances for fiscal 2008 were $82,062,405, compared to $79,209,913 in fiscal 2007. This increase was $2,852,492, or 4%. These advances had an average cost of 4.49% during fiscal 2008 compared to 4.76% during fiscal 2007. At June 30, 2008 and 2007, FHLB advances were $90,575,000 and $93,016,698, respectively. The Company had unused advance capacity with the FHLB of $25,008,000 at June 30, 2008. Management intends to increase available FHLB advance capacity by continuing to add qualifying securities. See Note 8 to the Consolidated

Financial Statements.

Average structured repurchase agreements for fiscal 2008 were $30,710,383. There was none in fiscal 2007. The structured repurchase agreements were collateralized by acquiring and pledging mortgage-backed securities as a leverage strategy to improve net interest income. They also had imbedded purchased interest rate caps with a notional amount of $50,000,000 and sold interest rate floors with a notional amount of $20 million with strike rates based on three month LIBOR. The purchased interest rate caps were utilized to reduce the interest rate risk exposure to rising interest rates. See Note 8 to the Consolidated Financial Statements for additional information.

The Bank has a secured line of credit under the Borrower in Custody program through the Fed Discount Window. Under the terms of this credit line, the Bank has pledged its indirect auto loans, and the line bears an interest rate equal to the then current federal funds rate plus 0.25%. At June 30, 2008, the credit availability under the Borrower in Custody program was $25,029,000. There were no borrowings outstanding under this credit line at June 30, 2008.

The following is a summary of the unused borrowing capacity of the Bank at June 30, 2008 available to meet our short-term funding needs:

Brokered time deposits	$ 136,972,000	Subject to policy limitation of 25% of total assets
Federal Home Loan Bank of Boston	$ 25,008,000	Unused advance capacity subject to eligible and qualified collateral
Fed Discount Window Borrower-in-Custody	$ 25,029,000	Unused credit line subject to the pledge of indirect auto loans
Total Unused Borrowing Capacity	$ 187,009,000	

We had outstanding $16,496,000 at June 30, 2008 and 2007, respectively, of junior subordinated debentures issued by us to affiliated trusts. See “Capital” for more information on junior subordinated debentures and affiliated trusts.

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ASSET QUALITY

We monitor our asset quality through lending and credit policies which require the regular independent review of our loan portfolio. We maintain an internal rating system which provides a process to regularly monitor the credit quality of our loan portfolio.

At June 30, 2008 and 2007, the allowance for loan losses was $5,656,000 and $5,756,000, respectively. The decrease in the allowance for loan losses was attributed to the decrease in loans in fiscal 2008 compared to fiscal 2007.

The allowance for loan losses as a percentage of total loans was 1.38% and 1.35% at June 30, 2008 and 2007, respectively. This increase of 3 basis points was attributable to a decline in loans in fiscal 2008 compared to fiscal 2007.

Classified loans, exclusive of non-performing loans, that could potentially become non-performing due to delinquencies or marginal cash flows were $2,680,000 and $2,542,000 at June 30, 2008 and 2007, respectively. Significant credit losses are not expected on these loans.

The following table reflects the annual trend of total delinquencies 30 days or more past due, including loans on non-accrual status, which are not delinquent, as a percentage of total loans:

06/30/08	06/30/07	06/30/06	06/30/05
3.64%	2.90%	2.09%	1.09%

The delinquency for the years prior to June 30, 2006 have been restated because the method of measuring past due loans changed to the number of days lapsed from the date of last payment from the number of payments past due. For the year ended June 30, 2005, the previously reported delinquency and current non-accrual loans were 0.96%.

Non-performing Assets

Total non-performing loans were $7,703,000 and $5,090,000 at June 30, 2008 and 2007, respectively. This increase of $2,613,000, or 51%, was attributable primarily to residential real estate and commercial loans. Of non-performing commercial real estate and commercial loans, $928,000 and $1,576,000, respectively, were current and paying as agreed. Many of these substandard loans were subject to a name-by-name review determining the risk of loss based on the liquidation of the collateral. This risk of loss is incorporated in determining the adequacy of the allowance for loan losses and represented approximately 13% of the allowance at June 30, 2008. The following table represents the non-performing loans as of June 30, 2008 and 2007.

Description	June 30, 2008	June 30, 2007
Residential real estate	$ 1,390,000	$ 477,000
Commercial real estate	2,358,000	2,033,000
Construction loans	101,000	-
Commercial loans	3,214,000	2,104,000
Consumer and other	640,000	476,000
Total non-performing	$ 7,703,000	$ 5,090,000

Non-performing loans as a percentage of total loans were 1.88% and 1.20% at June 30, 2008 and 2007, respectively. The allowance for loan losses was equal to 73% and 113% of total non-performing loans at June 30, 2008 and 2007, respectively. At June 30, 2008, non-performing loans included $2,510,000 of loans that are current and paying as agreed, but which the Bank maintains as non-performing until the respective borrowers have demonstrated a sustainable period of performance. Excluding these loans, the total delinquencies 30 days and more past due as a percentage of total assets would be 3.03% and 2.42% for June 30, 2008 and 2007, respectively.

See Item 8 Table 8 for a summary of non-performing assets for the last five years.

We continue to focus on asset quality issues and allocate significant resources to credit policy and loan review. The collection, workout and asset management functions focus on the reduction of non-performing assets. Despite this ongoing effort on asset quality, there can be no assurance that adverse changes in the real estate markets and economic conditions will not result in higher non-performing assets levels in the future and negatively impact our operations through higher provision for loan losses, net loan charge-offs, decreased accrual of income and increased noninterest expenses.

Residential real estate, commercial real estate, commercial, and consumer and other loans are generally placed on nonaccrual when reaching 90 days past due. Secured consumer loans are written down to realizable value and unsecured consumer loans are charged-off upon reaching 90 days past due. Based on our judgment, we may place on nonaccrual status loans which are currently less than 90 days past due or performing in accordance with their terms but are likely to present future principal and/or interest repayment problems and thus become classified as non-performing.

Net charge-offs were $936,000 during 2008, compared to $729,000 in 2007. Net charge-offs as a percentage of average loans outstanding were 0.23% and 0.17% in 2008 and 2007, respectively. The increase of $207,000 was due to higher gross charge-offs in indirect consumer loans and commercial real estate loans. See Item 8 Table 6 for more information concerning charge-offs and recoveries for the last five years.

Potential Problem Loans

Commercial real estate and commercial loans are periodically evaluated under an eight-point risk rating system. These ratings are guidelines in assessing the risk of a particular loan. We had classified commercial real estate and commercial loans totaling $15,801,000 and $15,011,000 at June 30, 2008 and 2007, respectively, as substandard or lower under our risk rating system. This increase was primarily due to commercial customer relationships experiencing weaknesses in the underlying businesses. These loans were subject to our internal name-by-name review for the risk of loss based on the liquidation of collateral. This risk of loss was included in determining the adequacy of the allowance for loan loss. At June 30, 2008, $4,550,000 of this amount was non-performing commercial real estate and commercial loans. The remaining $11,251,000 of commercial real estate and commercial loans classified as substandard at June 30, 2008 evidence one or more weaknesses or potential weaknesses and may become non-performing loans in future periods.

Management actively monitors the Bank's asset quality to evaluate the adequacy of the allowance for loan losses, charge-off loans against the allowance for loan losses when appropriate, establish specific loss allowances and change the level of the loan loss allowance. The process of evaluating the allowance involves a high degree of management judgment. The methods employed to evaluate the allowance for loan losses are quantitative in nature and consider such factors as the loan mix, the level of non-performing loans, delinquency trends, past charge-off history, loan reviews and classifications, collateral and the current economic climate. The liquidation value of collateral for each classified commercial real estate or commercial loan is considered in the evaluation of the allowance for loan loss.

Management believes that the allowance for loan losses is adequate considering the level of risk in the loan portfolio. While management believes that it uses the best information available to make its determinations with respect to the allowance, there can be no assurance that the Company will not have to increase its allowance for loan losses in the future as a result of changing economic conditions, adverse markets for real estate or other factors. Regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan losses. These agencies may require the Bank to recognize additions to the allowance for loan losses based on their judgments about information available to them at the time of their examination. No such adjustments were proposed by the Federal Reserve Bank of Boston or the Maine Bureau of Financial Institutions based on their 2008 examination.

At June 30, 2008, the Company had acquired assets of $678,350, compared to $0 at June 30, 2007. The increase of $678,350 was due to 28 indirect loans and one in substance foreclosure at June 30, 2008. The collateral for indirect loans is written down to its estimated realizable value once the loan reaches 90 days or more delinquent. We continue to carry it as a loan, on non-accrual status, until sold. Gains and losses on disposition are recognized as recoveries and additional charge-offs, respectively. Total indirect loans 90 days or more past due at June 30, 2008 and included in consumer loans were $811,000. See Note 5 of the Consolidated Financial Statements for addition information. Management periodically receives independent appraisals on acquired assets. As a result of this review and the review of the acquired assets portfolio, the Company believes the allowance for losses on acquired assets is adequate to state acquired assets at lower of cost or fair value less estimated selling costs.

A reserve for off-balance sheet credit risk was created in fiscal 2006. At June 30, 2007, this account balance was $178,818, compared to $16,070 at June 30, 2008. The adequacy of this balance is subject to an analysis similar to the analysis applied to allowance for loan losses by taking into consideration outstanding letters of credit and unadvanced construction loans. Compared to June 30, 2007, the unadvanced lines of credit for commercial and home equity loans, and commitments to make loans were excluded from the analysis at June 30, 2008 accounting for the decline in this reserve.

RISK MANAGEMENT

Asset-Liability Management

The Company's operating results are largely dependent upon its ability to manage interest rate risk. Interest rate risk can be defined as the exposure of the Company's net interest income to adverse movements in interest rates. Although the Company regularly manages other risks, such as credit and liquidity risk, in the normal course of its business, management considers interest rate risk to be its most significant market risk and it could potentially have the most material effect on the Company's financial condition and results of operations. The Company does not believe that it is exposed to significant market risk from trading activities because these activities are not material.

Asset-liability management is governed by policies reviewed and approved annually by the Board. The Board delegates responsibility for asset-liability management to the Asset Liability Management Committee (ALCO) which is comprised of members of senior management who set the strategic directives that guide the day-to-day asset-liability management activities. ALCO reviews and approves all major risk, liquidity and capital management programs, except for pricing, which is a subcommittee of ALCO members.

The Company continues to attempt to minimize the volatility of its net interest margin by managing the relationship of interest-rate sensitive assets to interest-rate sensitive liabilities. To accomplish this, management undertakes steps to increase the percentage of variable rate assets as a percentage of its total earning assets. The focus has been to originate variable rate commercial and commercial real estate loans, which reprice or mature more quickly than similar fixed-rate loans. Variable rate residential real estate loans are originated for the loan portfolio. Fixed rate residential real estate loans are originated for sale to the secondary market. Consumer loans, including indirect auto and recreational vehicle loans, are primarily originated with fixed rates. The Company's adjustable-rate loans are primarily tied to published indices, such as the Wall Street Journal prime rate and one-year U.S. Treasury Bills. Management considers the Bank's assets and liabilities well matched. The balance sheet is slightly liability sensitive.

The overall objective of interest rate risk management is to deliver consistent net interest income growth over a range of possible interest rate environments. We focus on interest rates, careful review of the cash flows of loans and deposits and other modeling assumptions and asset liability strategies to help attain our goals and objectives.

Another objective of interest rate risk management is to control our estimated exposure to interest rate risk within limits established by the asset/liability committee and approved by our Board. These limits reflect our tolerance for interest rate risk over a wide range of both short-term and long-term measurements. We also evaluate risk through liquidation or run-off measures of assets and liabilities on our balance sheet and stress test measures. Stress testing demonstrates the impact of very extreme but lower probability events. The combination of these measures gives management a comprehensive view of the possible risk to future earnings. We attempt to control interest rate risk by identifying and quantifying these risks.

Net interest income is our largest source of revenue. Net interest income sensitivity is our primary short-term measurement used to assess the interest rate risk of our on-going business. We believe that net interest income sensitivity gives us the best perspective on how day-to-day decisions affect our interest rate risk profile. We subject estimated net interest income over a 12 month period to various rate movements using a simulation model for various specified interest rate scenarios. Simulations are run quarterly and include scenarios where market rates are shocked up and down. Our base simulation assumes that rates do not change for the next 12 months. The sensitivity measurement is calculated as a percentage variance of the net interest income simulations to the base simulation results. The results are compared to policy guidelines and are disclosed in the following table.

Assuming a 200 basis point increase and decrease in interest rates starting on June 30, 2008, we estimate that our net interest income in the following 12 months would decrease by 1.38% if rates went up 200 basis points and increase by 2.00% if rates went down 100 basis points. This demonstrates the liability sensitivity of our balance sheet where the simulated increase in interest expense would be greater than the increase in interest income because our interest-bearing liabilities reprice more quickly than our interest-bearing assets. In a falling rate environment, the interest-bearing liabilities reprice downward more quickly than our interest-bearing assets. Also shown in the table are the results assuming a 200 basis point increase and a 100 basis point decrease starting June 30, 2008 and 200 basis point increase and decrease in interest rates starting June 30, 2007. The decrease in federal funds interest rates during fiscal 2008 to 2.00% caused the interest rate simulation for decreasing rates to change to 100 basis points from 200 basis points.

	Up 200 Basis Points	Down 100 Basis Points
June 30, 2008	-1.38%	2.00%

	Up 200 Basis Points	Down 200 Basis Points
June 30, 2007	-1.80%	4.60%

LIQUIDITY

On a parent Company only basis, our commitments and debt service requirements at June 30, 2008 consisted of junior subordinated notes issued to NBN Capital Trust II and NBN Capital Trust III totaling $6,186,000 due March 30, 2034 and junior subordinated debentures issued to NBN Capital Trust IV totaling $10,310,000 due February 23, 2035. NBN Capital Trust II issued $3,093,000 of junior subordinated notes with a variable interest rate based on three month LIBOR plus 2.80% and which reprice quarterly. The interest rate was 5.60% at June 30, 2008. NBN Capital Trust III also issued $3,093,000 of junior subordinated notes with a fixed interest rate of 6.50% until March 30, 2009, when the interest rate will become variable based on three month LIBOR plus 2.80%. NBN Capital Trust IV issued $10,310,000 of junior subordinated debentures with a fixed interest rate of 5.88% until February 23, 2010, when the interest rate will become variable based on three month LIBOR plus 1.89%. NBN Capital Trust II and III have a call option on March 30, 2009 and NBN Capital Trust IV has a call option on February 23, 2010.   See Note 18 to the Consolidated Financial Statements. Based on the interest rates at June 30, 2008, the annual aggregate payments to meet the debt service of the junior subordinated debentures is approximately $980,000.

Affiliated Trusts	Trust Preferred Securities	Common Securities	Junior Subordinated Debentures	Interest Rate	Maturity Date
NBN Capital Trust II	$ 3,000,000	$ 93,000	$ 3,093,000	5.60%	March 30, 2034
NBN Capital Trust III	3,000,000	93,000	3,093,000	6.50%	March 30, 2034
NBN Capital Trust IV	10,000,000	310,000	10,310,000	5.88%	February 23, 2035
Total	$ 16,000,000	$ 496,000	$ 16,496,000	5.94%	

The principal sources of funds for us to meet parent-only obligations are dividends from our banking subsidiary, which are subject to regulatory limitations, and borrowings from public and private sources. For information on the restrictions on the payment of dividends by our banking subsidiary, see Note 9 to the Consolidated Financial Statements.

For our banking subsidiary, liquidity represents the ability to fund asset growth, accommodate deposit withdrawals and meet other contractual obligations and commitments. Liquidity risk is the risk that a bank cannot meet anticipated or unexpected funding requirements or can meet them only at excessive cost. Liquidity is measured by the ability to raise cash when needed at a reasonable cost. Many factors affect a bank's ability to meet liquidity needs, including variation in the markets served, its asset-liability mix, its reputation and credit standing in the market and general economic conditions.

In addition to traditional deposits, the Bank has other liquidity sources, including the proceeds from maturing securities and loans, the sale of securities, asset securitizations and borrowed funds such as FHLB advances and brokered time deposits. We monitor and forecast our liquidity position. There are several interdependent methods used by us for this purpose, including daily review of federal funds positions, monthly review of balance sheet changes, monthly review of liquidity ratios, quarterly review of liquidity forecasts and periodic review of contingent funding plans.

At June 30, 2008, our banking subsidiary had $187 million of immediately accessible liquidity, defined as cash that could be raised within 7 days through collateralized borrowings, brokered deposits or security sales. This position represented 31% of total assets, compared to a policy minimum of 10%.

OFF-BALANCE SHEET ARRANGEMENTS & AGGREGATE CONTRACTUAL OBLIGATIONS

The Company 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, unused lines of credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit and interest-rate risk in excess of the amounts recognized in the condensed consolidated balance sheet. The contract or notional amounts of these instruments reflect the extent of the Company's involvement in particular classes of financial instruments.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit, unused lines of credit and standby letters of credit is represented by the contractual amount of those instruments. To control the credit risk associated with entering into commitments and issuing letters of credit, the Company uses the same credit quality, collateral policies, and monitoring controls in making commitments and letters of credit as it does with its lending activities. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation.

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 committed amounts do not necessarily represent future cash requirements. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if it is deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the counter party.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers.

Unused lines of credit and commitments to extend credit typically result in loans with a market interest rate.

A summary of the amounts of the Company's (a) contractual obligations, and (b) other commitments with off-balance sheet risk, both at June 30, 2008 follows:

		Payments Due by Period			
Contractual Obligations	Total	Less Than 1 Year	1-3 Years	4-5 Years	After 5 Years
FHLB advances	$ 90,575,000	$ 55,575,000	$ 5,000,000	$ 15,000,000	$ 15,000,000
Structured Repurchase Agreements	40,000,000	-	40,000,000	-	-
Junior subordinated debentures	16,496,000	6,186,000	10,310,000	-	-
Capital lease obligation	2,891,022	147,843	319,610	354,306	2,069,263
Other borrowings	4,026,885	763,067	1,130,186	1,090,878	1,042,754
Total long-term debt	153,988,907	62,671,910	56,759,796	16,445,184	18,112,017
Operating lease obligations	2,109,748	458,557	791,825	553,109	306,257
Total contractual obligations	$ 156,098,655	$ 63,130,468	$ 57,551,620	$ 16,998,293	$ 18,418,274

		Amount of Commitment Expiration - Per Period			
Commitments with off-balance sheet risk	Total	Less Than	1-3	4-5	After 5

		1 Year	Years	Years	Years
Commitments to extend credit (1)(3)	$ 18,991,000	$ 18,991,000	$ -	$ -	$ -
Commitments related to loans held for sale(2)	943,000	943,000	-	-	-
Unused lines of credit (3)(4)	44,915,000	18,400,000	2,681,000	3,445,000	20,389,000
Standby letters of credit (5)	1,113,000	1,113,000	-	-	-
	$ 65,962,000	$ 39,447,000	$ 2,681,000	$ 3,445,000	$ 20,389,000

(1) Represents commitments outstanding for residential real estate, commercial real estate, and commercial loans.
(2) Commitments of residential real estate loans that will be held for sale.
(3) Loan commitments and unused lines of credit for commercial and construction loans that expire or are subject to renewal in twelve months or less.
(4) Represents unused lines of credit from commercial, construction, and home equity loans.
(5) Standby letters of credit generally expiring in twelve months.

The Bank has written options limited to those residential real estate loans designated for sale in the secondary market and subject to a rate lock. These rate-locked loan commitments are used for trading activities, not as a hedge. The fair value of the outstanding written options at June 30, 2008 was a loss of $4,921.

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CAPITAL

At June 30, 2008 and 2007, stockholders' equity totaled $40,273,312 and $40,849,878, respectively, or 6.73% and 7.34% of total assets, respectively. In addition, we had on both June 30, 2008 and 2007, $16,496,000 of junior subordinated debentures which mature in 2034 and 2035 and qualify as Tier 1 Capital. See Note 18 to the Consolidated Financial Statements. The changes in stockholders' equity include net income for the year ended June 30, 2008 of $1,931,289, stock issued for $45,125 from the exercise of stock options, $2,661 from a stock grant and a decrease of $610,474 in the net unrealized losses on available-for-sale securities offset by dividend payments of $851,785, and stock repurchases of $2,314,330, representing 137,800 shares repurchased at an average cost of $16.79 per share. See Note 9 to the Consolidated Financial Statements for additional information on capital ratios.

The 2006 Stock Repurchase Plan was approved by the Board of Directors on December 15, 2006, replacing the 2004 Stock Repurchase Plan which was terminated on the same date. Although the Board of Directors may discontinue the repurchase program at any time, it is scheduled to terminate on December 31, 2008. Under the 2006 Stock Repurchase Plan, the Company may purchase up to 200,000 shares of its common stock from time to time in the open market at prevailing prices. Common stock repurchased pursuant to the plan is classified as authorized but unissued shares of common stock available for future issuance as determined by the Board of Directors. Total stock repurchases under the 2006 Plan in fiscal 2008 were 137,800 shares, for $2,314,330, at an average price of $16.79 per share. For fiscal 2007, the total stock repurchased was 3,800 shares, for $67,944, at an average price of $17.88 per share. The remaining repurchase capacity of the 2006 Plan is 58,400 shares. Since inception, total stock repurchases under the 2006 plan were 141,600 shares, for $2,382,274, through June 30, 2008. Management believes that these and future purchases have not and will not have a significant impact on the Company's liquidity.

Regulatory capital guidelines require the Bank to maintain certain capital ratios. The Bank's Tier 1 Capital was $40,302,000, or 7.06% of total average assets at June 30, 2008 compared to $46,780,000, or 8.60% of total average assets, at June 30, 2007. The decrease in the Bank's Tier 1 Capital ratio was due to the goodwill and other intangibles resulting from the three insurance agency acquisitions in fiscal 2008. We are also required to maintain risk-based capital ratios based on the level of certain assets, as adjusted to reflect their perceived level of risk. Our regulatory capital ratios currently exceed all applicable requirements. See Note 9 to the Consolidated Financial Statements.

IMPACT OF INFLATION

The consolidated financial statements and related notes have been presented in terms of historic dollars without considering changes in the relative purchasing power of money over time due to inflation. Unlike industrial companies, substantially all of the assets and virtually all of the liabilities of the Company are monetary in nature. As a result, interest rates have a more significant impact on the Company's performance than the general level of inflation. Over short periods of time, interest rates may not necessarily move in the same direction or in the same magnitude as inflation.

IMPACT OF NEW ACCOUNTING STANDARDS

Note 1 of the Consolidated Financial Statement includes the Financial Accounting Standards Board (FASB) and the SEC issued statements and interpretations affecting the Company.

EVENTS SUBSEQUENT TO JUNE 30, 2008

As of June 30, 2008, the Bank owned preferred stock of FNMA and FHLMC with book values of $25,000 and $100,000, respectively. The Company owned common and preferred stock of AIG with book values of $43,250 and $75,000, respectively. The actions by the Federal Government to take over FNMA and FHLMC on September 7, 2008 and its take over of AIG on September 16, 2008 will result in other than temporary impairment which will be recognized in the quarter ending September 30, 2008 based on their fair values as of September 30, 2008. An impairment expense of 100% of the book value of these securities would not impact the Company’s or Bank’s ability to maintain capital ratios above the well capitalized regulatory requirement, or the Company’s ability to pay its regular quarterly cash dividend to common shareholders. The anticipated write downs are not expected to have a material impact on financial condition or results of operations.

Item 7.a . Quantitative and Qualitative Disclosure about Market Risk

See Item 7 of our Form 10-K, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Risk Management" and accompanying table set forth therein for quantitative and qualitative disclosures about market risk.

Item 8. Financial Statements and Supplementary Data

a. Financial Statements Required by Regulation S-X

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To the Board of Directors
Northeast Bancorp
Lewiston, Maine

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We have audited the accompanying consolidated balance sheets of Northeast Bancorp and Subsidiary as of June 30, 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 Company'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 the standards of the Public Company Accounting Oversight Board (United States). 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. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. 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 position of Northeast Bancorp and Subsidiary as of June 30, 2008 and 2007, and the results of their operations and their cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

/s/ Shatswell, MacLeod & Company, P.C.
Shatswell, MacLeod & Company, P.C.

West Peabody, Massachusetts
September 18, 2008

NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
June 30, 2008 and 2007

ASSETS

	2008	2007
Cash and due from banks	$ 9,077,012	$ 9,065,330
Interest-bearing deposits	3,466,969	1,676,391
Total cash and cash equivalents	12,543,981	10,741,721
Available-for-sale securities, at fair value	134,482,977	86,348,070
Loans held-for-sale	485,580	1,636,485
Loans receivable	409,193,969	425,571,418
Less allowance for loan losses	5,656,000	5,756,000
Net loans	403,537,969	419,815,418
Premises and equipment - net	8,683,569	7,545,430
Acquired assets - net	678,350	-
Accrued interest receivable	2,291,314	2,586,720
Federal Home Loan Bank stock, at cost	4,889,400	4,825,700
Federal Reserve Bank stock, at cost	471,500	471,500
Goodwill	4,390,340	2,880,803
Intangible assets, net of accumulated amortization of $1,642,140 in 2008 and $1,031,483 in 2007	8,444,424	4,110,081
Bank owned life insurance (BOLI)	12,292,216	9,844,584
Other assets	5,082,030	5,994,468
Total assets	$ 598,273,650	$ 556,800,980

NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
June 30, 2008 and 2007

LIABILITIES AND STOCKHOLDERS' EQUITY

	2008	2007
Liabilities:		
Deposits		
Demand	$ 35,142,661	$ 36,332,604
NOW	47,977,659	53,405,241
Money market	22,160,816	8,053,552
Regular savings	19,905,507	21,145,567
Brokered time deposits	12,596,615	22,546,163
Certificates of deposit under $100,000	147,252,982	154,972,970
Certificates of deposit $100,000 or more	78,337,531	68,097,680
Total deposits	363,373,771	364,553,777
Federal Home Loan Bank advances	90,575,000	93,016,698
Structured repurchase agreements	40,000,000	-
Short-term borrowings	32,840,837	33,105,377

Junior subordinated debentures issued to affiliated trusts		16,496,000		16,496,000
Capital lease obligation		2,891,022		2,653,511
Other borrowings		4,026,885		2,292,163
Due to broker		4,934,931		-
Other liabilities		2,861,892		3,833,576
Total liabilities		558,000,338		515,951,102
Commitments and contingent liabilities				
Stockholders' equity				
Preferred stock, $1.00 par value, 1,000,000 shares authorized; none issued		-		-
Common stock, at stated value, 15,000,000 shares authorized; 2,315,182 and 2,448,832 shares outstanding at June 30, 2008 and 2007, respectively		2,315,182		2,448,832
Additional paid-in capital		2,582,270		4,715,164
Retained earnings		36,679,932		35,600,428
Accumulated other comprehensive loss		(1,304,072)		(1,914,546)
Total stockholders' equity		40,273,312		40,849,878
Total liabilities and stockholders' equity	$	598,273,650	$	556,800,980

The accompanying notes are an integral part of these consolidated financial statements.

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NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
Years Ended June 30, 2008, 2007 and 2006

	2008	2007	2006
Interest and dividend income:			
Interest and fees on loans	$ 29,271,770	$ 31,366,547	$ 31,643,003
Interest on Federal Home Loan Bank overnight deposits	36,012	152,805	93,017
Taxable interest on available-for-sale securities	5,106,019	3,154,072	2,947,224
Tax-exempt interest on available-for-sale securities	448,378	442,311	264,839
Dividends on available-for-sale securities	151,481	140,954	130,605
Dividends on Federal Home Loan Bank and Federal Reserve Bank stock	306,668	368,463	335,900
Other interest and dividend income	77,346	57,203	41,620
Total interest and dividend income	35,397,674	35,682,355	35,456,208
Interest expense:			
Deposits	13,089,876	13,490,173	11,152,306
Federal Home Loan Bank advances	3,747,221	3,819,550	3,482,655
Structured repurchase agreements	1,503,778	-	-
Short-term borrowings	1,244,442	1,504,936	927,688
Junior subordinated debentures issued to affiliated trusts	1,064,964	1,080,538	1,063,681
FRB borrower-in-custody	8,007	-	-
Obligation under capital lease agreements	149,453	136,726	130,583
Other borrowings	243,264	65,075	3,693
Total interest expense	21,051,005	20,096,998	16,760,606
Net interest and dividend income before provision for loan losses	14,346,669	15,585,357	18,695,602
Provision for loan losses	836,484	989,158	1,226,413
Net interest and dividend income after provision for loan losses	13,510,185	14,596,199	17,469,189
Noninterest income:			
Fees and service charges on loans	94,371	79,885	97,630
Fees for other services to customers	1,094,043	1,042,648	1,114,081
Net securities gains	293,101	42,349	17,335
Gain on sales of loans	555,707	869,255	308,777
Investment commissions	2,222,935	2,385,118	1,769,300
Insurance commissions	5,364,280	2,330,435	1,916,822
BOLI income	457,198	388,613	366,939
Other	721,589	806,524	1,003,997
Total noninterest income	10,803,224	7,944,827	6,594,881
Noninterest expense:			
Salaries and employee benefits	13,019,398	12,022,037	10,637,758
Occupancy expense	1,792,827	1,722,381	1,672,505
Equipment expense	1,587,297	1,531,276	1,440,238
Intangible assets amortization	610,657	314,584	241,028

Other	4,844,275	4,484,908	4,216,975
Total noninterest expense	21,854,454	20,075,186	18,208,504
Income before income taxes	2,458,955	2,465,840	5,855,566
Income tax expense	527,666	579,163	1,851,367
Net income	$ 1,931,289	$ 1,886,677	$ 4,004,199
Earnings per common share:			
Basic	$ 0.82	$ 0.77	$ 1.61
Diluted	$ 0.82	$ 0.76	$ 1.59

The accompanying notes are an integral part of these consolidated financial statements.

NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
Years Ended June 30, 2008, 2007 and 2006

	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance at June 30, 2005	$ -	$ 2,519,832	$ 6,530,836	$ 31,489,092	$ (670,187)	$ 39,869,573
Net income	-	-	-	4,004,199	-	4,004,199
Other comprehensive income net of tax:						
Net unrealized losses on investments available-for-sale, net of reclassification adjustment	-	-	-	-	(1,952,282)	(1,952,282)
Total comprehensive income	-	-	-	-	-	2,051,917
Purchase of 90,200 shares of Company stock	-	(90,200)	(2,052,050)	-	-	(2,142,250)
Stock options exercised	-	17,500	196,472	-	-	213,972
Dividends on common stock at $0.36 per share	-	-	-	(897,087)	-	(897,087)
Balance at June 30, 2006	-	2,447,132	4,675,258	34,596,204	(2,622,469)	39,096,125
Net income	-	-	-	1,886,677	-	1,886,677
Other comprehensive income net of tax:						
Net unrealized gain on investments available-for-sale, net of reclassification adjustment	-	-	-	-	707,923	707,923
Total comprehensive income	-	-	-	-	-	2,594,600
Purchase of 3,800 shares of Company stock	-	(3,800)	(64,144)	-	-	(67,944)
Stock options exercised	-	500	6,050	-	-	6,550
Common stock issued in	-	5,000	98,000	-	-	103,000

connection with the purchase of branch real estate						
Dividends on common stock at $0.36 per share	-	-	-	(882,453)	-	(882,453)
Balance at June 30, 2007	-	2,448,832	4,715,164	35,600,428	(1,914,546)	40,849,878
Net income	-	-	-	1,931,289	-	1,931,289
Other comprehensive income net of tax:						
Net unrealized gain on investments available-for-sale, net of reclassification adjustment	-	-	-	-	610,474	610,474
Total comprehensive income	-	-	-	-	-	2,541,763
Purchase of 137,800 shares of Company stock	-	(137,800)	(2,176,530)	-	-	(2,314,330)
Stock options exercised	-	4,000	41,125	-	-	45,125
Stock grant	-	150	2,511	-	-	2,661
Dividends on common stock at $0.36 per share	-	-	-	(851,785)	-	(851,785)
Balance at June 30, 2008	$ -	$ 2,315,182	$ 2,582,270	$ 36,679,932	$ (1,304,072)	$ 40,273,312

The accompanying notes are an integral part of these consolidated financial statements.

NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended June 30, 2008, 2007 and 2006

	2008	2007	2006
Cash flows from operating activities:			
Net income	$ 1,931,289	$ 1,886,677	$ 4,004,199
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	836,484	989,158	1,226,413
Provision for losses on acquired assets	-	6,384	2,500
Provision made for deferred compensation	132,111	276,539	399,845
Write-down of available-for-sale securities	147,247	50,442	38,394
Write-down of non-marketable securities	47,020	248,482	42,257
Deferred income tax expense (benefit)	218,579	(329,268)	(323,220)
BOLI income, net	(447,632)	(349,258)	(366,939)
Depreciation of premises and equipment	1,121,573	1,088,373	1,048,529
Amortization of intangible assets	610,657	314,584	241,028
Net gain on sale of available-for-sale securities	(293,101)	(42,349)	(17,335)
Net (gain) loss on disposals, writedowns and sale of fixed assets	-	(73,962)	128,363
Gain on sale of deposits	-	-	(500,845)
Net change of loans held-for-sale	1,150,905	(955,342)	(362,293)
Stock grant	2,661	-	-
Other	(29,611)	27,839	21,962
Change in other assets and liabilities:			
Interest receivable	295,406	91,838	(123,669)
Other assets and liabilities	(771,442)	49,756	106,976
Net cash provided by operating activities	4,952,146	3,279,893	5,566,165
Cash flows from investing activities:			
Federal Reserve Bank stock purchased	-	(12,000)	(54,000)
Federal Home Loan Bank stock purchased	(63,700)	-	-
Proceeds from redemption of Federal Home Loan Bank stock	-	672,600	1,146,200
Proceeds from the sales of available-for-sale securities	16,035,767	2,290,571	1,354,098
Purchases of available-for-sale securities	(78,435,328)	(14,720,181)	(25,311,089)
Proceeds from maturities and principal payments on available-for-sale securities	20,300,010	13,255,927	9,078,452
Loan originations and principal collections, net	14,762,615	9,361,953	24,729,918
Purchases of premises and equipment	(1,873,282)	(1,373,474)	(1,111,469)
Proceeds from sales of premises and equipment	-	246,610	-
Proceeds from sales of acquired assets	-	4,000	244,722
Purchase of BOLI	(2,000,000)	(600,000)	-
Cash paid in connection with acquisition of insurance agencies	(3,740,363)	(2,471,002)	-
Net cash (used) provided by investing activities	(35,014,281)	6,655,004	10,076,832
Cash flows from financing activities:			
Net (decrease) increase in deposits	(1,180,006)	(30,739,600)	7,267,169
Cash paid on sale of deposits	-	-	(7,691,669)

Advances from the Federal Home Loan Bank	22,000,000	43,000,000	105,000,000
Repayment of advances from the Federal Home Loan Bank	(39,056,698)	(36,831,900)	(115,309,004)
Net advances on Federal Home Loan Bank overnight advances	14,615,000	10,960,000	-
Structured repurchase agreement proceeds	40,000,000	-	-
Net (decrease) increase in short-term borrowings	(264,540)	3,467,951	(3,741,986)
Dividends paid	(851,785)	(882,453)	(897,087)
Company stock purchased	(2,314,330)	(67,944)	(2,142,250)
Issuance of common stock	45,125	6,550	213,972
Repayment on debt from insurance agencies acquisitions	(990,882)	(81,966)	-
Repayment on capital lease obligation	(137,489)	(127,535)	(111,656)
Net cash provided (used) by financing activities	31,864,395	(11,296,897)	(17,412,511)
Net increase (decrease) in cash and cash equivalents	1,802,260	(1,362,000)	(1,769,514)
Cash and cash equivalents, beginning of year	10,741,721	12,103,721	13,873,235
Cash and cash equivalents, end of year	$ 12,543,981	$ 10,741,721	$ 12,103,721
Supplemental schedule of cash flow information:			
Interest paid	$ 20,900,773	$ 20,120,234	$ 16,872,352
Income taxes paid	540,000	819,500	2,220,561
Supplemental schedule of noncash investing and financing activities:			
Transfer from loans to acquired assets and other real estate owned	$ 678,350	$ -	$ 173,800
Change in valuation allowance for unrealized gains (losses) on available-for-sale securities, net of tax	610,474	707,923	(1,952,282)
Net change in deferred taxes for unrealized (gains) losses on available-for-sale securities	(314,486)	(364,689)	1,005,701
Transfer from loan loss allowance to other liabilities for off balance sheet credit risk	-	-	204,086
Capital lease asset and related obligation	375,000	-	2,892,702
Stock issued in branch purchase	-	103,000	-
Other borrowings and goodwill reductions related to acquisition	98,332	-	-

The accompanying notes are an integral part of these consolidated financial statements.

NORTHEAST BANCORP AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Years Ended June 30, 2008, 2007 and 2006

1. Summary of Significant Accounting Policies

The accounting and reporting policies of Northeast Bancorp and Subsidiary (“Company”) conform to accounting principles generally accepted in the United States of America and general practice within the banking industry.

Business

The Company is a Maine corporation and a bank holding company registered with the Federal Reserve Bank of Boston (“FRB”) under the Bank Holding Company Act of 1956. The Company provides a full range of banking services to individual and corporate customers throughout south-central and western Maine through its wholly-owned subsidiary, Northeast Bank ("Bank"), a Maine state-chartered universal bank and a member of the Federal Reserve Bank of Boston. As a result, the Bank is subject to the joint regulatory oversight by the FRB and the State of Maine Bureau of Financial Institutions. The Bank is also subject to the regulations of the Federal Deposit Insurance Corporation ("FDIC"). The Bank faces competition from banks and other financial institutions.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Northeast Bancorp, and its wholly-owned subsidiary, Northeast Bank (including the Bank's wholly-owned subsidiary, Northeast Bank Insurance Group, Inc.). All significant intercompany transactions and balances have been eliminated in consolidation.

In fiscal 2004, pursuant to the criteria established by FIN 46R, the Company deconsolidated three trusts which the Company had formed for the purposes of issuing trust preferred securities to unaffiliated parties and investing the proceeds from the sale thereof and the common securities of the trusts in junior subordinated debentures issued by the Company. The affiliated trusts are NBN Capital Trust II, NBN Capital Trust III and NBN Capital Trust IV. The result of the deconsolidation and the accounting for these entities was to recognize investments in these entities of approximately $408,000 in the aggregate in other assets and to report the amount of junior subordinated debentures issued by the Company to such entities, rather than the related trust preferred securities, in the consolidated balance sheet which resulted in a $408,000 increase in this liability. The adoption of FIN 46R did not have any additional impact on the Company's financial condition, results of operations, earnings per share or cash flows.

NBN Capital Trust II, NBN Capital Trust III and NBN Capital Trust IV are considered affiliates. (See note 18).

Use of Estimates

The financial statements have been prepared in conformity with accounting principles generally accepted in the Unites States of America. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the statement of financial condition and income and expenses for the period. Actual results could differ significantly from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses and a determination as to whether declines in the fair values below cost of investments is other-than-temporary.

In connection with the determination of the allowance for loan losses, management obtains independent appraisals for significant properties. A substantial portion of the Company's loans are secured by real estate in the State of

Maine. Accordingly, the ultimate collectibility of a substantial portion of the Company's loan portfolio is susceptible to changes in market conditions in Maine.

In connection with the determination of whether fair value declines of investments are other-than-temporary, management investigates the underlying cause for the declines, the near term prospects for recovery and the Company's intent and ability to hold the investments.

Cash and Cash Equivalents

For purposes of presentation in the consolidated statements of cash flow, cash and cash equivalents consist of cash and due from banks, interest-bearing deposits and Federal Home Loan Bank overnight deposits. The Company is required to maintain a certain reserve balance in the form of cash or deposits with the Federal Reserve Bank. At June 30, 2008 and 2007, the reserve balance was approximately $224,000 and $250,000, respectively.

Available-for-sale Securities

Marketable equity securities and debt securities, which may be sold prior to maturity, are classified as available-for-sale and are carried at fair value. Fair value is determined based on bid prices published in financial newspapers or bid quotations received from securities dealers. Changes in fair value, net of applicable income taxes, are reported as a separate component of stockholders' equity. When a decline in fair value of a security is considered other-than-temporary, the loss is charged to other expense in the consolidated statements of income and is treated as a write-down of the security's cost. Realized gains and losses on the sale of securities are recognized on the trade date using the specific identification method. The Company has no marketable securities classified as held-to-maturity or trading. Debt securities are adjusted for amortization of premiums and accretion of discounts so as to approximate the interest method. Gains and losses on sales of investment securities are computed on a specific identification basis.

Federal Home Loan Bank and Federal Reserve Bank Stock

Federal Home Loan Bank stock and Federal Reserve Bank stock are carried at cost. Each is a restricted investment.

Loans held-for-sale and Mortgage Banking Activities

Loans originated for sale are specifically identified and carried at the lower of aggregate cost or fair value, estimated based on bid quotations from loan dealers. The carrying value of loans held-for-sale approximates the fair value at June 30, 2008 and 2007. Realized gains and losses on sales of loans are determined using the specific identification method and are reflected as gains on sale of loans in the consolidated statements of income.

The Company sells loans both on a servicing released and servicing retained basis. The Company recognizes as separate assets the rights to service mortgage loans for others, and performs an assessment of capitalized mortgage servicing rights for impairment based on the current fair value of those rights. The Company capitalizes mortgage servicing rights at their allocated cost (based on the relative fair values of the rights and the related loans) upon the sale of the related loans.

The Company's mortgage servicing rights asset at June 30, 2008 and 2007 was approximately $100,000 and $202,000, respectively, and is included in other assets in the consolidated statements of financial condition. The fair value of mortgage servicing rights exceeds their carrying value. Mortgage servicing rights are amortized over the estimated weighted average life of the loans. The Company's assumptions with respect to prepayments, which affect the estimated average life of the loans, are adjusted periodically to reflect current circumstances. The Company evaluates the estimated life and fair value of its servicing portfolio based on data that is disaggregated to reflect note rate, type and term on the underlying loans.

Loans

Loans are carried at the principal amounts outstanding plus net premiums paid and net deferred loan origination fees and costs. Loan origination fees and certain direct loan origination costs are deferred and recognized in interest income as an adjustment to the loan yield over the life of the related loans. Loan premiums paid to acquire loans are recognized as a reduction of interest income over the estimated life of the loans. Loans are generally placed on nonaccrual status when they are past due 90 days as to either principal or interest, or when in management's judgment the collectibility of interest or principal of the loan has been significantly impaired. When a loan has been placed on nonaccrual status, previously accrued and uncollected interest is reversed against interest on loans. A loan can be returned to accrual status when collectibility of principal is reasonably assured and the loan has performed for a period of time, generally six months. Loans are classified as impaired when it is probable that the Company will not be able to collect all amounts due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status and collateral value.

Allowance for Loan Losses

The allowance for loan losses is established through a provision for loan losses charged to operations. Loan losses are charged against the allowance when management believes that the collectibility of the loan principal is unlikely. Recoveries on loans previously charged off are credited to the allowance.

The allowance for loan losses represents management's estimate of probable losses inherent in the loan portfolio. This evaluation process is subject to numerous estimates and judgments. The frequency of default, risk ratings and the loss recovery rates, among other things, are considered in making this evaluation, as are the size and diversity of individual large credits. Larger balance, non-homogeneous loans representing significant individual credit exposures are evaluated based upon the borrower's overall financial condition, resources and payment record; the prospects for support from any financially responsible guarantors; and, if appropriate, the realizable value of any collateral. The allowance for loan losses attributed to these loans is established through a process that includes estimates of historical and projected default rates and loss severities; internal risk ratings; and geographic, industry, and other environmental factors. Management also considers overall portfolio indicators, including trends in internally risk-rated loans, classified loans, nonaccrual loans and historical and forecasted write-offs; and a review of industry, geographic, and portfolio concentrations, including current developments. In addition, management considers the current business strategy and credit process, including credit limit setting and compliance, credit approvals, loan underwriting criteria, and loan workout procedures. Each portfolio of smaller balance, homogeneous loans, including residential real estate and consumer loans, is collectively evaluated for impairment. The allowance for loan losses for these loans is established via a process that includes historical delinquency and credit loss experience, together with analyses that reflect current trends and conditions. Management also considers overall portfolio indicators including historical credit losses; delinquent, non-performing and classified loans; trends in volumes; terms of loans; an evaluation of overall credit quality and the credit process, including lending policies and procedures; and economic factors. Changes in these estimates could have a direct impact on the provision and could result in a change in the allowance.
Management believes that the allowance for loan losses is adequate. While management uses available information to recognize losses on loans, changing economic conditions and the economic prospects of the borrowers might necessitate future additions to the allowance. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed by the straight-line and accelerated methods over the estimated useful lives of the assets. Premises and equipment under capital leases are amortized over the estimated useful lives of the assets or the respective lease terms, whichever is shorter. Maintenance and repairs are charged to expense as incurred and the cost of major renewals and betterments are capitalized. Premises and equipment are evaluated periodically for impairment. An assessment of recoverability is performed prior to any write-down of the asset. If circumstances suggest that their value may be impaired, then an expense would be charged in the then current period.

Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that includes the enactment date.

Acquired Assets

Acquired assets are carried at the lower of cost or fair value of the collateral less estimated selling expenses.

Goodwill and Intangible Assets

Goodwill of $407,897 arising from the acquisition of a bank in prior years is deemed to have an indefinite useful life. The Company ceased amortization of goodwill on July 1, 2001, with the adoption of Statement of Financial Accounting Standard No. 142, Goodwill and Other Intangible Assets. Intangible assets include noncompete agreements and customer lists which are being amortized on a straight-line basis over the estimated lives of the asset ranging from seven to nineteen years. The weighted average amortization period for intangibles subject to amortization is 14.16 years (based on original balances and amortization period, 12.77 years based on remaining amortization period). Goodwill and intangible assets are reviewed annually for possible impairment, and if the assets are deemed impaired, an expense would be charged in the then current period.

The changes in the carrying amount of goodwill and other intangibles for the years ended June 30, 2008 and 2007 were as follows:

	Goodwill	Customer List Intangibles	Non-compete Intangibles	Total Identifiable Intangibles
Balance, June 30, 2006	$ 407,897	1,890,516	29,149	1,919,665
Recorded during the year	2,472,906	1,970,000	535,000	2,505,000
Amortization expense	-	(268,560)	(46,024)	(314,584)
Other adjustment of purchase accounting estimates	-	-	-	-
Balance, June 30, 2007	2,880,803	3,591,956	518,125	4,110,081
Recorded during the year	1,545,110	3,905,000	1,100,000	5,005,000
Amortization expense	-	(510,401)	(100,256)	(610,657)
Reclassification	60,000	(60,000)	-	(60,000)
Other adjustment of purchase accounting estimates	(95,573)	-	-	-
Balance, June 30, 2008	$ 4,390,340	6,926,555	1,517,869	8,444,424

Estimated Annual Amortization Expense, years ending June 30:	
2009	$ 717,524
2010	692,124
2011	692,124
2012	692,124
2013	692,124

The components of identifiable intangible assets follow:

	June 30, 2008		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Indentifiable intangible assets:			
Customer list intangibles	$ 8,201,564	1,275,009	6,926,555
Non-compete intangibles	1,885,000	367,131	1,517,869
Total	$ 10,086,564	1,642,140	8,444,424

	June 30, 2007		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Indentifiable intangible assets:			

Customer list intangibles	$ 4,356,564	764,608	3,591,956
Non-compete intangibles	785,000	266,875	518,125
Total	$ 5,141,564	1,031,483	4,110,081

Advertising Expense

Advertising costs are expensed as incurred. Advertising costs were approximately $504,000, $440,000 and $492,000 for the years ended June 30, 2008, 2007 and 2006, respectively.
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Stock-Based Compensation

The Company has stock-based employee compensation plans, which are described more fully in note 13. The Company adopted Statement of Financial Accounting Standard No. 123 (revised 2004), Shared-Based Payment ("SFAS 123-R"), effective for the fiscal year beginning July 1, 2005, superseding APB Opinion 25 and replacing FASB Statement No. 123. Prior to July 1, 2005, the Company utilized the intrinsic value methodology allowed by APB Opinion 25. SFAS 123-R requires companies to measure and record compensation expense for stock options and other share-based payments based on the instruments' fair value reduced by expected forfeitures. Under the modified prospective approach adopted by the Company, the Company recognizes expense for new options awarded and to awards modified, repurchased or canceled after the effective date. Since there were no new options granted (or modifications of existing options) during fiscal 2008 and 2007 and since all previously granted options were fully vested at the grant date, adoption of SFAS 123-R had no impact on the 2008 and 2007 financial statements.

There were no stock options granted in fiscal 2008, 2007 and 2006.

Bank-Owned Life Insurance

Bank-owned life insurance ("BOLI") represents life insurance on the lives of certain employees. Increases in the cash value of the policies, as well as insurance proceeds received, are recorded in other noninterest income, and are not subject to income taxes. The cash surrender value is included in assets. The Company reviews the financial strength of the insurance carriers prior to the purchase of BOLI and annually thereafter.

Comprehensive Income

Accumulated other comprehensive income or loss consists solely of unrealized gains or losses on investment securities available-for-sale, net of related income taxes.

Derivatives

The Company accounts for derivatives in accordance with Statement of Financial Accounting Standards ("SFAS") No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended, which requires the Company to recognize all derivatives on the statement of financial condition at fair value. Derivatives that are not hedges must be adjusted to fair value through income. If the derivative is a hedge, depending on the nature of the hedge, changes in the fair value of derivatives are either offset against the change in fair value of assets, liabilities or firm commitments through earnings or recognized in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of a derivative's change in fair value will be immediately recognized in earnings.

The Company uses derivative financial instruments for trading and hedging purposes. The derivative financial instruments used by the Company are covered call and put contracts on its equity securities portfolio, certain residential mortgage loan commitments for resale into the secondary market, and purchased interest rate caps and sold interest rate floors which were imbedded in the structured repurchase agreements. The total value of securities under call and put contracts and commitments to originate residential mortgage loans for resale at June 30, 2008, 2007 and 2006, which are not used as a hedge but are classified as trading, is immaterial to the Company's financial position, liquidity, and results of operations. See note 8 of the consolidated financial statements for additional information on interest rate caps and floors.

Trust Assets

Assets of the Company's trust department are not included in these consolidated financial statements because they are not assets of the Company. As of June 30, 2008, total assets held in trust for customers, for which the Company has fiduciary responsibility, amounted to approximately $96,429,000.

Treasury Stock

On July 1, 2003, the Maine Business Corporation Act became effective. This Act eliminated the concept of treasury stock, instead providing that shares of its stock acquired by the Company simply constitute authorized but unissued shares. Accordingly, all stock held by the Company as treasury stock has been reclassified as authorized but unissued stock in accordance with the Act.

Reclassifications

Certain reclassifications have been made to the prior year financial statements to conform to the current year presentation.

New Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles ("GAAP") and enhances disclosures about fair value measurements. SFAS 157 retains the exchange price notion and clarifies that the exchange price is the price that would be received for an asset or paid to transfer a liability (an exit price) in an orderly transaction between market participants on the measurement date. SFAS 157 is effective for the Company's consolidated financial statements for the year beginning on July 1, 2008, with earlier adoption permitted. The Company does not expect the adoption of SFAS 157 to have a material impact on its financial condition, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities including an amendment of FASB Statement No. 115 ("SFAS 159"). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This Statement also establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. The new standard is effective at the beginning of the Company's fiscal year beginning July 1, 2008, and early application may be elected in certain circumstances. The Company is currently evaluating and has not yet determined the impact the new standard is expected to have on its financial position, results of operations or cash flows.

In December 2007, the FASB issued SFAS No. 141 (Revised 2008), Business Combinations ("SFAS 141(R)"). SFAS 141(R) will significantly change the accounting for business combinations. Under SFAS 141(R), an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date fair value with limited exceptions. It also amends the accounting treatment for certain specific items including acquisition costs and non controlling minority interests and includes a substantial number of new disclosure requirements. SFAS 141(R) applies prospectively to business combinations for which the acquisition date is on or after January 1, 2009. The Company does not expect the adoption of this statement to have a material impact on its financial condition and results of operations.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities-an amendment of FASB Statement No. 133 ("SFAS 161"). SFAS 161 changes the disclosure requirements for derivative instruments and hedging activities. Entities are required to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under Statement 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. The guidance in SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. This statement encourages, but does not require, comparative disclosures for earlier periods at initial adoption. The Company does not expect the adoption of this statement to have a material impact on its financial condition and results of operations.

2. Available-for-sale securities

A summary of the cost and approximate fair values of available-for-sale securities at June 30, 2008 and 2007 follows:

	2008		2007	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Debt securities issued by U.S. Government-sponsored enterprises	$ 1,394,087	1,313,124	21,765,732	21,158,409
Mortgage-backed securities	120,695,852	119,600,353	53,987,824	52,138,732
Municipal bonds	11,274,516	11,112,247	11,067,197	10,709,069
Corporate bonds	500,000	481,768	500,000	484,625
Equity securities	2,594,389	1,975,485	1,928,144	1,857,235
	$ 136,458,844	134,482,977	89,248,897	86,348,070

The gross unrealized gains and unrealized losses on available-for-sale securities are as follows:

	2008	2007

	Gross Unrealized Gains	Gross Unrealized Losses	Gross Unrealized Gains	Gross Unrealized Losses
Debt securities issued by U. S. Government-sponsored enterprises	$ 6,239	87,202	-	607,323
Mortgage-backed securities	394,927	1,490,426	2,818	1,851,910
Municipal bonds	272	162,541	-	358,128
Corporate bonds	-	18,232	-	15,375
Equity securities	2,396	621,300	18,661	89,570
	$ 403,834	2,379,701	21,479	2,922,306

At June 30, 2008, mortgage-backed and U.S. Government-sponsored enterprise securities with a fair value of approximately $115,988,000 were pledged as collateral to secure outstanding repurchase agreements, FHLB advances and other purposes.

The following summarizes the Company's gross unrealized losses and fair values aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at June 30, 2008 and 2007:

	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
June 30, 2008:						
U.S. Government-sponsored enterprises	$ -	-	905,009	87,202	905,009	87,202
Mortgage-backed securities	79,631,910	1,444,686	965,826	45,740	80,597,736	1,490,426
Municipal bonds	10,709,579	162,541	-	-	10,709,579	162,541
Corporate bonds	481,768	18,232	-	-	481,768	18,232
Equity securities	1,348,236	340,571	550,093	280,729	1,898,329	621,300
	$ 92,171,493	1,966,030	2,420,928	413,671	94,592,421	2,379,701
June 30, 2007:						
U.S. Government-sponsored enterprises	$ 391,296	9,828	20,767,113	597,495	21,158,409	607,323
Mortgage-backed securities	22,180,625	463,353	27,327,140	1,388,557	49,507,765	1,851,910
Municipal bonds	7,945,475	262,497	2,763,594	95,631	10,709,069	358,128
Corporate bonds	-	-	484,625	15,375	484,625	15,375
Equity securities	839,368	49,720	630,039	39,850	1,469,407	89,570
	$ 31,356,764	785,398	51,972,511	2,136,908	83,329,275	2,922,306

Unrealized losses within U.S. Government-sponsored enterprises of $87,202 consist of one individual debt security issued by the FNMA which has had continuous loss for more than one year. Unrealized losses within the mortgage-backed securities category of $1,490,426 consist of thirty individual debt securities, of which two securities have had continuous losses for more than one year. Unrealized losses within the municipal bond category of $162,541 consist of thirty-two individual debt securities. The primary cause for unrealized losses within the above investment categories is the impact movements in market interest rates have had in comparison to the underlying yields on these securities, and illiquidity in the market. Unrealized losses within the equity security category of $621,300 consist of eighty-three individual equity securities, of which twenty-three have had continuous losses for more than one year.

Management of the Company, in addition to considering current trends and economic conditions that may affect the quality of individual securities within the Company's investment portfolio, also considers the Company's ability and intent to hold such securities to maturity or recovery of cost. Management does not believe any of the Company's available-for-sale securities are other-than-temporarily impaired at June 30, 2008, 2007 and 2006, except as discussed below.

Based on management's assessment of available-for-sale securities, there has been more than a temporary decline in market value of certain equity securities. During the years ended June 30, 2008, 2007 and 2006, write-downs of available-for-sale securities were $147,247, $50,442 and $38,394, respectively, and are included in other noninterest expense in the consolidated statements of income.

Included in accumulated other comprehensive loss, as an adjustment to stockholders’ equity is the following:

	2008	2007

Net unrealized losses	$ (1,975,867)	(2,900,827)
Deferred tax effect	671,795	986,281
Accumulated other comprehensive loss	$ (1,304,072)	(1,914,546)

The cost and market values of available-for-sale debt securities at June 30, 2008, by contractual maturity are shown below. Actual maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Cost	Fair Value
Due one year or less	$ -	-
Due after one year through five years	500,000	481,768
Due after five years through ten years	215,396	215,432
Due after ten years	12,453,207	12,209,939
	13,168,603	12,907,139
Mortgage-backed securities (consisting of securities with interest rates ranging from 4.00% to 6.375% maturing February 2013 to March 2037)	120,695,852	119,600,353
	$ 133,864,455	132,507,492

Realized gains and losses on sales of available-for-sale securities were $316,159 and $23,058, respectively, for the year ended June 30, 2008, $59,419 and $17,070, respectively, for the year ended June 30, 2007 and $21,073 and $3,738, respectively, for the year ended June 30, 2006. The tax provision applicable to these net realized gains amounted to $101,589, $14,678 and $6,008, respectively.

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3. Loans Receivable

The Company's lending activities are predominantly conducted in south-central and western Maine. However, the Company occasionally purchases residential mortgage loans in the open market out of this geographical area when management believes this is prudent. The Company grants single-family and multi-family residential loans, commercial real estate loans, commercial loans and a variety of consumer loans. In addition, the Company grants loans for the construction of residential homes, multi-family properties, commercial real estate properties and for land development. The majority of loans granted by the Company are collateralized by real estate. The ability and willingness of residential and commercial real estate, commercial and construction loan borrowers to honor their repayment commitments is generally dependent on the health of the real estate sector in the borrowers' geographic area and/or the general economy. In addition, the Company participates in indirect lending arrangements for automobile, mobile home and recreational vehicle loans. The Company's indirect lending activities are conducted throughout the State of Maine, but are concentrated in south-central and western Maine.

Loans consisted of the following as of June 30:

		2008	2007
Mortgage loans:			
Residential real estate	$	140,244,226	145,184,733
Commercial real estate		111,222,848	112,534,812
Construction		12,621,369	7,707,432
Total mortgage loans		264,088,443	265,426,977
Commercial loans		33,516,315	40,783,958
Consumer and other loans		117,046,759	118,880,723
		414,651,517	425,091,658
Undisbursed portion of construction loans		(8,084,395)	(2,256,606)
Net deferred loan origination costs		2,626,847	2,736,366
		409,193,969	425,571,418
Less allowance for loan losses		5,656,000	5,756,000
Net loans	$	403,537,969	419,815,418

Included in the loan portfolio are unamortized premiums on purchased loans of approximately $48,000 and $60,000 at June 30, 2008 and 2007, respectively.

In the ordinary course of business, the Company has loan transactions with its officers, directors and their associates and affiliated companies ("related parties") at substantially the same terms as those prevailing at the time for comparable transactions with others. Such loans amounted to $4,369,167 and $3,110,276 at June 30, 2008 and 2007, respectively. In 2008, new loans and advances granted to related parties totaled $3,850,333, and payments and reductions amounted to $2,591,442. In 2007, new loans and advances totaled $1,484,077 and payments and reductions amounted to $1,166,764.

Activity in the allowance for loan losses was as follows:

	Years Ended June 30,		
	2008	2007	2006
Balance at beginning of year	$ 5,756,000	5,496,000	5,104,000
Provision charged to operating expenses	836,484	989,158	1,226,413

Transferred to off balance sheet credit risk reserve included in other liabilities	-	-	(204,086)
Loans charged off	(1,123,406)	(854,631)	(793,653)
Recoveries on loans previously charged off	186,922	125,473	163,326
Net loans charged off	(936,484)	(729,158)	(630,327)
Balance at end of year	$ 5,656,000	5,756,000	5,496,000

As shown above, during fiscal 2006 the Company transferred $204,086, representing the portion of the allowance related to unfunded loans and commitments at the transfer date, to other liabilities.

Commercial and commercial real estate loans with balances greater than $25,000 are considered impaired when it is probable that the Company will not collect all amounts due in accordance with the contractual terms of the loan. Loans that are returned to accrual status are no longer considered to be impaired. Certain loans are exempt from individual impairment evaluation, including large groups of smaller-balance homogenous loans that are collectively evaluated for impairment, such as consumer and residential mortgage loans and commercial loans with balances less than $25,000.
The allowance for loan losses includes allowances related to loans that are identified as impaired, which are based on discounted cash flows using the loan's effective interest rate, the fair value of the collateral for collateral-dependent loans, or the observable market price of the impaired loan. When foreclosure is probable, impairment is measured based on the fair value of the collateral. Loans that experience insignificant payment delays (less than 60 days) or insignificant shortfalls in payment amounts (less than 10%) generally are not classified as impaired. Restructured loans are reported as impaired in the year of restructuring. Thereafter, such loans may be removed from the impaired loan disclosure if the loans were paying a market rate of interest at the time of restructuring and are performing in accordance with their renegotiated terms.

The Company recognizes interest on impaired loans on a cash basis when the ability to collect the principal balance is not in doubt; otherwise, cash received is applied to the principal balance of the loan.

The following table summarizes information about impaired loans at or for the years ended:

	2008	2007	2006
Impaired loans	$ 5,880,447	2,498,498	7,128,111
Impaired loans with related allowances	1,371,835	884,543	5,950,923
Allowances on impaired loans	400,430	322,402	1,290,960
Average balance of impaired loans during the year	5,243,419	2,269,862	4,584,621
Interest recognized on impaired loans	306,098	211,346	71,400

Impaired loans at June 30, 2008 include loans totaling $2,505,000, which were current as to both principal and interest payments at that date, but which were considered impaired based on current estimates of collateral valuation.

Loans on nonaccrual status, including certain impaired loans described above, at June 30, 2008 and 2007, totaled approximately $7,703,000 and $5,090,000, respectively. Interest income that would have been recorded under the original terms of such loans, net of interest income actually recognized for the years ended June 30, 2008, 2007 and 2006, totaled approximately $351,000, $211,000 and $158,000, respectively. The Company has no material outstanding commitments to lend additional funds to customers whose loans have been placed on nonaccrual status or the terms of which have been modified.

The Company was servicing, for others, loans of approximately $45,574,000 and $51,097,000 at June 30, 2008 and 2007, respectively.

4. Premises and Equipment

Premises and equipment at June 30, 2008 and 2007, are summarized as follows:

	2008	2007
Land	$ 1,560,331	1,327,621
Buildings	2,798,651	2,058,695
Assets recorded under capital lease	3,267,702	2,892,702
Leasehold and building improvements	2,049,692	1,888,618
Furniture, fixtures and equipment	6,414,077	5,663,105
	16,090,453	13,830,741
Less accumulated depreciation	7,406,884	6,285,311
Net premises and equipment	$ 8,683,569	7,545,430

Depreciation and amortization of premises and equipment included in occupancy, equipment expense, was $1,121,573, $1,088,373, and $1,048,529 for the years ended June 30, 2008, 2007 and 2006, respectively.

5. Acquired Assets

The following table summarizes the composition of acquired assets at June 30:

	2008	2007
Real estate properties acquired in settlement of loans and other acquired assets	$ 678,350	-
Less allowance for losses	-	-

$	678,350	-

Activity in the allowance for losses on acquired assets was as follows for the years ended June 30:

6. Acquisition of Insurance Agencies

Northeast Bank Insurance Group, Inc. acquired three insurance agencies in fiscal 2008 and four insurance agencies in fiscal 2007. Each acquisition was as a purchase of assets for cash and a note, except the Palmer Insurance Agency which was the purchase of stock, for cash and a note. The details of each purchase appear below including the acquisition date and the agencies location in Maine. Each agency will be operate at its existing location except Hartford which was relocated to our agency office in Auburn, Maine and Russell, which was relocated to our agency office in Anson, Maine. Spence & Mathews has an office in Rochester, NH.

All acquisitions were accounted for using the purchase method and resulted in increases in goodwill and customer list and non-compete intangibles on the consolidated balance sheet. All purchase and sale agreements except the Russell Insurance Agency and Hartford Insurance Agency call for a reduction in the purchase price should the stipulated minimum commission revenue levels not be attained over periods of one to three years from the purchase date. During the year ended June 30, 2008, other borrowings and goodwill related to the Southern Maine acquisition were reduced by $98,332 in accordance with this stipulation. The customer list intangibles and estimated useful lives are based on estimates from a third-party appraiser. The useful lives of these intangibles range from eleven to nineteen years. Non-compete intangible useful lives are amortized over a range of ten to fifteen years.

The debt incurred is due to the seller of each agency. Each bears an interest rate of 6.50% over terms as follows: Palmer debt is payable over a term of seven years; the Sturtevant debt is payable over a term of three years; the Southern Maine debt is payable over a term of four years; and the Russell debt is payable over a term of two years. Hartford, Spence & Mathews, and Hyler are payable over a term of seven years. Hartford, Spence & Mathews, and Hyler have debt of $100,000, $800,000, and $200,000, respectively, that bears no interest and has been recorded at its present value assuming a discount rate of 6.50%. Northeast Bank guaranteed the debt repayment to each seller.

Northeast Bank Insurance Group, Inc. leases the office locations for Sturtevant, Southern Maine, and Hyler, which are operating leases. We also lease both office locations for Spence & Mathews. The Berwick office is recorded as a capital lease. The Rochester, NH lease is an operating lease. Northeast Bank acquired Palmer's agency building and land in January, 2007.

The results of operations of all agencies have been included in the consolidated financial statements since their acquisition date. There is no pro-forma disclosure included because the agencies individually and in aggregate were not considered significant acquisitions.

2008 Acquisitions

Purchase price	Hartford	Spence & Mathews	Hyler	Totals
Cash paid	$ 425,250	3,043,000	233,000	3,701,250
Debt incurred	911,350	1,122,885	789,701	2,823,936
Acquisition costs	9,181	17,630	9,543	36,354
Total	$ 1,345,781	4,183,515	1,032,244	6,561,540
Allocation of purchase price:				
Goodwill	$ 275,781	1,090,265	179,064	1,545,110
Customer list intangible	970,000	2,285,000	650,000	3,905,000
Non-compete intangible	100,000	800,000	200,000	1,100,000
Fixed and other assets	-	8,250	3,180	11,430
Total	$ 1,345,781	4,183,515	1,032,244	6,561,540
Acquisition date	08/30/07	11/30/07	12/11/07	
Location in Maine	Auburn	Berwick	Thomaston	

2007 Acquisitions

Purchase price	Palmer	Sturtevant and Ham	Southern Maine	Russell	Totals
Cash paid	$ 800,000	475,000	900,000	275,000	2,450,000
Debt incurred	1,067,000	475,000	450,000	325,000	2,317,000
Acquisition costs	8,360	3,877	4,264	4,501	21,002
Total	$ 1,875,360	953,877	1,354,264	604,501	4,788,002
Allocation of purchase price:					
Goodwill	$ 1,174,274	324,367	754,764	219,501	2,472,906
Customer list intangible	600,000	550,000	520,000	300,000	1,970,000
Non-compete intangible	300,000	75,000	75,000	85,000	535,000
Fixed and other assets	5,086	4,510	4,500	-	14,096
Deferred income taxes	(204,000)	-	-	-	(204,000)
Total	$ 1,875,360	953,877	1,354,264	604,501	4,788,002
Acquisition date	11/28/06	12/01/06	03/30/07	06/28/07	
Location in Maine	Turner	Livermore	Scarborough	Madison	

$2,902,501 of the total goodwill acquired is expected to be deductible for tax purposes.

Northeast Bank Insurance Group, Inc. acquired Solon-Anson Insurance Agency, Inc. on September 29, 2004. This acquisition used purchase accounting and resulted in a customer list intangible asset of $2,081,500, which is being amortized over twelve years.

7. Deposits

Deposits at June 30 are summarized as follows:

	Weighted Average Rate at June 30, 2008	2008 Amount	2008 Percent	2007 Amount	2007 Percent
Demand	0.00%	$ 35,142,661	9.7%	36,332,604	10.0%
NOW	1.46%	47,977,659	13.2%	53,405,241	14.7%
Money market	2.50%	22,160,816	6.1%	8,053,552	2.2%
Regular savings	0.52%	19,905,507	5.5%	21,145,567	5.8%
Certificates of deposit and brokered time deposits:					
Less than 1.00%	0.50%	7,674	0.0%	151,674	0.0%
1.00 - 3.75%	3.09%	109,394,988	30.1%	9,973,634	2.7%
3.76 - 5.75%	4.80%	128,739,995	35.4%	235,151,508	64.5%
5.76 - 7.75%	6.90%	44,471	0.0%	339,997	0.1%
	3.00%	$ 363,373,771	100.0%	364,553,777	100.0%

The scheduled maturities of certificates of deposit and brokered time deposits for the twelve months ended June 30, respectively, are as follows:

	2009	2010	2011	2012	2013	Thereafter
Less than 1.00%	$ 7,674	-	-	-	-	-
1.00-3.75%	96,306,016	11,802,228	305,343	127,964	808,403	45,034
3.76-5.75%	105,694,785	14,402,647	3,487,255	1,986,400	2,946,335	222,573
5.76-7.75%	9,807	-	34,664	-	-	-
Total	$202,018,282	26,204,875	3,827,262	2,114,364	3,754,738	267,607

Interest expense on deposits for the years ended June 30, 2008, 2007 and 2006 is summarized as follows:

	2008	2007	2006
NOW	$ 1,019,644	1,234,207	1,065,675
Money market	419,733	221,118	246,283
Regular savings	160,518	194,258	227,830
Certificates of deposit and brokered time deposits	11,489,981	11,840,590	9,612,518
	$ 13,089,876	13,490,173	11,152,306

In the fourth quarter of fiscal year 2006, the Company sold the deposits of its Lisbon Falls, Maine branch and the branch was closed. The deposits sold totaled approximately $8,908,000. The Company recognized a gain on sale of deposits of $500,845 from this transaction, which is included in other income in the 2006 consolidated statement of income.

8. Borrowings

Federal Home Loan Bank

A summary of advances from the Federal Home Loan Bank of Boston are as follows:

	June 30, 2008	
Principal Amounts	Interest Rates	Maturity Dates
$55,575,000	2.50% - 5.21%	2009
2,000,000	4.31%	2010
3,000,000	4.99%	2011
15,000,000	2.55% - 3.99%	2013
10,000,000	4.26%	2017
5,000,000	4.29%	2018
$90,575,000		

	June 30, 2007	
Principal Amounts	Interest Rates	Maturity Dates
$50,016,698	2.68% - 5.69%	2008
30,000,000	4.86% - 5.21%	2009
3,000,000	4.99%	2011
10,000,000	4.26%	2017
$93,016,698		

At June 30, 2008, FHLB advances of $33,000,000 are subject to call provisions and may be called prior to the stated maturity.

Certain mortgage loans, free of liens, pledges and encumbrances and certain investment securities maintained at the FHLB not otherwise pledged have been pledged under a blanket agreement to secure these advances. The Company is required to own stock of the Federal Home Loan Bank of Boston in order to borrow from the Federal Home Loan Bank.

As of June 30, 2008 the Company had a $2,103,000 line of credit arrangement with the FHLB which was fully available. Also at June 30, 2008, the Company had approximately $25,008,000 of additional capacity to borrow from the FHLB for long-term advances.

Structured Repurchase Agreements

In a leveraging strategy for the year ended June 30, 2008, the Company borrowed $40,000,000 in two transactions.

On August 28, 2007, the Company borrowed funds of $30,000,000. The proceeds were used to purchase $24,816,734 of mortgage-backed securities which were combined with $7,335,665 of available mortgage-backed securities for total collateral of $32,152,399. The balance of the proceeds was used to pay down overnight advances from the Fed Discount Window Borrower-in-Custody program. This funding had imbedded purchased interest rate caps and sold interest rate floors, as summarized below. The interest rate caps reduced the balance sheet risk to rising interest rates. Interest is payable quarterly, and the interest rates are fixed for the first two years during which the issuer of the debt may not terminate the transaction. Following the two year period ending August 28, 2009, the interest rates will reset quarterly based on three month LIBOR and the debt issuer can terminate the transaction on any quarterly payment date.

On December 13, 2007, the Company borrowed funds of $10,000,000. Along with available funds, the proceeds were used to acquire $12,000,000 of mortgage-backed securities as collateral. The funding had imbedded purchased interest rate caps as summarized below. Interest is payable quarterly. The interest rate is fixed for three years during which the debt issuer may not terminate the transaction. After December 13, 2010, the interest rate will reset quarterly based on three month LIBOR and the transaction can be terminated by the debt issuer on any quarterly payment date.

Amount	Interest Rate	Cap/Floor	Notional Amount	Strike Rate	Maturity
$20,000,000	4.68%	Purchased Caps	$40,000,000	5.50%	August 28, 2012
10,000,000	3.98%	Sold Floors	$20,000,000	4.86%	August 28, 2012
10,000,000	4.18%	Purchased Caps	$10,000,000	4.88%	December 13, 2012
$40,000,000					

Payments would be received on the interest rate caps when three month LIBOR exceeded the strike rate on the quarterly reset date. Payments would be made on the sold interest rate floors when three month LIBOR was below the strike rate on the quarterly reset date. The amount of the payment would be equal to the difference between the strike rate and three month LIBOR multiplied by the notional amount of the cap or floor and be made 90 days after the reset date. The total of the repurchase agreement interest payment due and amount due, if any, on the sold interest rate floor is capped at 7.96% interest rate based on the repurchase agreement amount.

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Other borrowings

Other borrowings consist of non-negotiable promissory notes payable to former shareholders of acquired insurance companies.
Maturities of notes payable for the years ending after June 30, 2008 are summarized as follows:

June 30, 2008 Principal Amounts	Interest Rates	Maturity Dates
$ 763,067	6.50%	2009
634,157	6.50%	2010
496,029	6.50%	2011
528,270	6.50%	2012
562,608	6.50%	2013
599,178	6.50%	2014
443,576	6.50%	2015
$ 4,026,885		

Maturities of notes payable for the years ending after June 30, 2007 are summarized as follows:

June 30, 2007 Principal Amounts	Interest Rates	Maturity Dates
$ 534,522	6.50%	2008
569,471	6.50%	2009
428,194	6.50%	2010
244,721	6.50%	2011
161,056	6.50%	2012
171,525	6.50%	2013
182,674	6.50%	2014
$ 2,292,163		

Capital Lease Obligations

In fiscal 2008, the Company recognized a capital lease obligation for the building occupied by the Spence & Mathews Insurance Agency located at 4 Sullivan Square, Berwick, Maine which was acquired by Northeast Bank Insurance Group, Inc. on November 30, 2008. The present value of the annual lease payments of $38,880 over the remaining twenty-one year term exceeded 90% of the fair value of this building. The Spence & Mathews Insurance Agency occupies the entire building. In fiscal 2006, the Company recognized a capital lease obligation for its new headquarters known as the Southern Gateway building located at 500 Canal Street in Lewiston, Maine. The present value of the lease payments over fifteen years ($264,262 per year for each of the initial ten years of the lease term and $305,987 per year for each of the last five years) exceeded 90% of the fair value of the Southern Gateway building. Northeast Bank's commercial lending and underwriting, consumer loan underwriting, loan servicing, deposit operations, accounting, human resources, risk management, and executive administration departments occupy the approximately 27,000 square feet of space.

The future minimum lease payments over the remaining terms of the leases and the outstanding capital lease obligations at June 30, 2008 are as follows:

2009	$ 303,142
2010	303,142
2011	303,142
2012	303,142
2013	303,142
2014 and thereafter	2,684,381
Total minimum lease payments	4,200,091
Less imputed interest	1,309,069
Capital lease obligation	$ 2,891,022

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Fed Discount Window Borrower-in-Custody Program

The Bank also has a secured line of credit of $25,029,000 through the Fed Discount Window Borrower-in-Custody program. The Bank pledged $31,287,000 of its indirect auto loan portfolio as collateral for this line of credit. If used, interest is based upon the current federal funds rate plus 0.25%. There were no outstanding balances under this line of credit at June 30, 2008.

Short-Term Borrowings

Short-term borrowings consist of securities sold under agreements to repurchase and other sweep accounts. The weighted average interest rate on short-term borrowings was 2.50% and 4.28% at June 30, 2008 and 2007, respectively. Securities sold under agreement to repurchase, which were scheduled to mature the next business day, were collateralized by mortgage-backed and U.S. Government-sponsored enterprise securities with a fair value of $28,551,000 and amortized cost of $29,016,000, respectively, at June 30, 2008 and a fair value of $31,530,000 and amortized cost of $30,348,000, respectively at June 30, 2007. Sweep accounts had excess insurance coverage of $7,630,000 at June 30, 2008. The average balance of short-term borrowings was $34,449,000 and $36,145,000 during the years ended June 30, 2008 and 2007, respectively. The maximum amount outstanding at any month-end during 2008 and 2007 was $40,076,000 and $44,164,000, respectively. Securities sold under these agreements were under the control of the Company throughout 2008 and 2007.

9. Capital and Regulatory Matters

The Company and the Bank are 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 Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The Company and the Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

The prompt corrective action regulations define specific capital categories based on an institution's capital ratios. The capital categories, in declining order, are "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized" and "critically undercapitalized."

As of June 30, 2008 and 2007, the most recent notification from the Company’s and the Bank's regulator categorized the Company and the Bank as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized," the Company and the Bank must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratio as set forth in the table below. There are no conditions or events since that notification that management believes have changed the institution's category.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios as set forth in the table below. At June 30, 2008 and 2007, the Company and the Bank ratios exceeded the regulatory requirements. Management believes that the Company and the Bank met all capital adequacy requirements to which it was subject as of June 30, 2008 and 2007.

The following tables illustrate the actual and required amounts and ratios for the Company at the dates indicated.

Actual	For Capital	To Be "Well Capitalized" Under Prompt Corrective

			Adequacy Purposes		Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
	(Dollars in Thousands)					
As of June 30, 2008:						
Northeast Bancorp:						
Total capital to risk weighted assets	$ 50,245	11.91%	>33,744	>8.0%	>42,180	>10.0%
Tier 1 capital to risk weighted assets	$ 41,919	9.94%	>16,872	>4.0%	>25,308	> 6.0%
Tier 1 capital to total average assets	$ 41,919	7.31%	>22,943	>4.0%	>28,679	> 5.0%
As of June 30, 2007:						
Northeast Bancorp:						
Total capital to risk weighted assets	$ 57,302	13.97%	>32,804	>8.0%	>41,005	>10.0%
Tier 1 capital to risk weighted assets	$ 49,295	12.02%	>16,402	>4.0%	>24,603	> 6.0%
Tier 1 capital to total average assets	$ 49,295	9.07%	>21,845	>4.0%	>27,306	> 5.0%

The following tables illustrate the actual and required amounts and ratios for the Bank at the dates indicated.

	Actual		For Capital Adequacy Purposes		To Be "Well Capitalized" Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in Thousands)			
As of June 30, 2008:						
Northeast Bank:						
Total capital to risk weighted assets	$ 45,555	10.85%	>33,581	>8.0%	>41,976	>10.0%
Tier 1 capital to risk weighted assets	$ 40,302	9.60%	>16,791	>4.0%	>25,186	> 6.0%
Tier 1 capital to total average assets	$ 40,302	7.06%	>22,847	>4.0%	>28,559	> 5.0%
As of June 30, 2007:						
Northeast Bank:						
Total capital to risk weighted assets	$ 51,892	12.71%	>32,668	>8.0%	>40,835	>10.0%
Tier 1 capital to risk weighted assets	$ 46,780	11.46%	>16,334	>4.0%	>24,501	> 6.0%
Tier 1 capital to total average assets	$ 46,780	8.60%	>21,748	>4.0%	>27,185	> 5.0%

The Bank may not declare or pay a cash dividend on, or repurchase, any of its capital stock from the Parent if the effect thereof would cause the capital of the Bank to be reduced below the capital requirements imposed by the regulatory authorities or if such amount exceeds the otherwise allowable amount under FRB rules (approximately $2,998,000 is available at June 30, 2008).

The Board of Directors extended the 2006 Stock Repurchase Plan to December 31, 2008. Under the 2006 Stock Repurchase Plan, the Company may purchase up to 200,000 shares of its common stock from time to time in the open market at prevailing prices. Common stock repurchased pursuant to the Plan will be classified as authorized but un-issued shares of common stock available for future issuance as determined by the Board of Directors, from time to time. Total stock repurchases under the 2006 Plan were 137,800 shares for $2,314,330 during the year ended June 30, 2008 and 3,800 shares for $67,944 during the year ended June 30, 2007. The Board of Directors may discontinue the repurchase program at any time. Total stock repurchases in fiscal 2008 were 137,800 shares for $2,314,330 at an average price of $16.79 and in fiscal 2007 were 3,800 shares for $67,944 at an average price of $17.88 per share. The remaining repurchase capacity of the 2006 Plan is 58,400 shares. Management believes that these and future purchases have not and will not have a significant impact on the Company's liquidity. The repurchases had a positive effect on earnings per share during 2008 and 2007, by reducing the number of common stock shares outstanding.

10. Earnings Per Common Share

Basic earnings per share (EPS) are computed by dividing net income available to common stockholders by the weighted average number of shares outstanding. The following table shows the weighted average number of shares outstanding for each of the last three years. Shares issuable relative to stock options granted have been reflected as an increase in the shares outstanding used to calculate diluted EPS, after applying the treasury stock method. The number of shares outstanding for basic and diluted EPS is presented as follows:

	2008	2007	2006
Average shares outstanding, used in computing Basic EPS	2,352,484	2,451,610	2,493,560
Effect of Dilutive Securities:			
Stock and options outstanding	12,357	18,905	23,456
Options exercised or canceled	1,499	47	9,079
Average equivalent shares outstanding, used in computing Diluted EPS	2,366,340	2,470,562	2,526,095

11. Other Expenses

Other expenses include the following for the years ended June 30, 2008, 2007 and 2006:

	2008	2007	2006
Professional fees	$ 674,100	639,821	620,914
Advertising expense	504,234	440,222	491,920
Write-down of non-marketable securities	47,020	248,482	42,257
Computer services and processing costs	615,402	616,173	580,995
Loan expense	308,317	402,936	342,586
Write-down of available-for-sale securities	147,247	50,442	38,394
Other	2,547,955	2,086,832	2,099,909
	$ 4,844,275	4,484,908	4,216,975

12. Income Taxes

The current and deferred components of income tax expense (benefit) were as follows for the years ended June 30, 2008, 2007 and 2006:

	2008	2007	2006
Federal:			
Current	$ 242,115	845,509	2,089,538
Deferred	218,579	(329,268)	(323,220)
	460,694	516,241	1,766,318
State and local - current	66,972	62,922	85,049
	$ 527,666	579,163	1,851,367

Total income tax expense is different from the amounts computed by applying the U.S. federal income tax rates in effect to income before income taxes. The reasons for these differences are as follows for the years ended June 30, 2008, 2007 and 2006:

	2008		2007		2006	
	Amount	% of Pretax Income	Amount	% of Pretax Income	Amount	% of Pretax Income
Expected income tax expense at federal tax rate	$ 836,044	34.0%	838,386	34.0%	1,990,892	34.0%
State tax, net of federal tax benefit	44,100	1.8	41,529	1.7	56,132	1.0
Dividend received deduction	(34,991)	(1.4)	(33,547)	(1.4)	(30,634)	(0.5)
Non-taxable interest income	(171,749)	(7.0)	(143,938)	(5.8)	-	-
Non-taxable BOLI income	(158,777)	(6.5)	(118,748)	(4.8)	(112,829)	(1.9)
Other	13,039	0.6	(4,519)	(0.2)	(52,194)	(0.9)
	$ 527,666	21.5%	579,163	23.5%	1,851,367	31.7%

The tax effect of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at June 30, 2008 and 2007, are presented below:

	2008	2007
Deferred tax assets:		
Loans, principally due to allowance for loan losses	$ 1,929,000	2,018,000
Interest on nonperforming loans	138,000	72,000
Difference in tax and financial statement basis of investments	829,000	1,125,000
Deferred compensation	45,000	263,000
Other	86,000	110,000
Total deferred tax assets	3,027,000	3,588,000
Deferred tax liabilities:		
Difference in tax and financial statement amortization of goodwill and other intangible assets	(348,000)	(324,000)
Mortgage servicing rights	(36,000)	(69,000)
Premises and equipment	(182,000)	(193,000)
Prepaid expenses	(151,000)	(159,000)
Total deferred tax liabilities	(717,000)	(745,000)
Net deferred tax asset, included in other assets	$ 2,310,000	2,843,000

The Company has sufficient refundable taxes paid in available carryback years to fully realize its recorded deferred tax assets. Accordingly, no valuation allowance has been recorded.

In prior years, the Bank utilized the percentage of income bad debt deduction to calculate its bad debt expense for tax purposes as was then permitted by the Internal Revenue Code. Subsequent tax legislation required the Company to recapture a portion of its tax bad debt reserves. Except as stated below, the unrecaptured base year reserves will not be subject to recapture as long as the Bank continues to carry on the business of banking. However, the balance of the tax bad debt reserves is subject to provisions of present law that require recapture in the case of certain excess distributions to stockholders. For federal income tax purposes, the Company has designated approximately $1,967,000 of net worth as a reserve for tax basis bad debts on loans. No deferred taxes have been provided for base year reserve recapture as management plans to avoid the events that would cause such recapture.

13. Employee Benefit Plans

401(k) Plan

The Company offers a contributory 401(k) plan which is available to all full-time salaried and hourly-paid employees who have attained age 18, and completed 90 days of employment. Employees may contribute up to 100% of their base compensation, subject to IRS limitations. The Company will match 50% up to the first 6% contributed. For the years ended June 30, 2008, 2007 and 2006, the Company contributed $253,236, $220,649 and $202,664, respectively.

The Company also has a profit sharing plan which covers substantially all full-time employees. Contributions and costs are determined as a percent of each covered employee's salary and are at the Board of Directors' discretion. There were no discretionary contributions in 2008, 2007 or 2006.

Stock Option Plans

The Company has adopted Stock Option Plans. Both "incentive stock options" and "nonqualified stock options" may be granted pursuant to the Stock Option Plans. Under the Stock Option Plans, incentive stock options may only be granted to employees of the Company and nonqualified stock options may be granted to employees and directors. All options granted under the Stock Option Plans will be required to have an exercise price per share equal to at least the fair market value per share of common stock on the date the option is granted. Options immediately vest upon being granted. The options are exercisable for a maximum of ten years after the options are granted in the case of all incentive stock options and as determined by the Board of Directors for nonqualified stock options.

In accordance with the Stock Option Plans, a total of 363,250 shares of unissued common stock were reserved for grants. At June 30, 2008, a total of 189,500 shares remained available to be granted.

A summary of the qualified and nonqualified stock option activity for the years ended June 30 follows:

	2008		2007		2006	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at beginning of year	52,000	$ 12.12	52,500	$ 12.13	71,500	$ 12.31
Granted	-		-	-	-	-
Exercised	(4,000)	11.28	(500)	13.10	(17,500)	12.23
Expired	(12,000)	18.50	-	-	(1,500)	14.90
Outstanding and exercisable	36,000	$ 10.09	52,000	$ 12.12	52,500	$ 12.13

at end of year

The following table summarizes information about stock options outstanding at June 30, 2008:

	Options Outstanding and Exercisable		
Range of Exercise Prices	Number Outstanding at June 30, 2008	Weighted-Average Remaining Contractual Life (Years)	Weighted-Average Exercise Price
$8.00 to $8.88	23,500	1.6	$ 8.48
$13.10	12,500	3.1	13.10
$8.00 to $13.10	36,000	2.1	$ 10.09

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14. Commitments, Contingent Liabilities and Other Off-Balance Sheet Risks

The Company 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 and to reduce its own exposure to fluctuations in interest rates. 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 balance sheets. The contract amounts of those instruments reflect the extent of involvement the Company has in particular classes of financial instruments.

The Company'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 contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Financial instruments with contract amounts which represent credit risk are as follows as of June 30:

	2008	2007
Commitments to originate loans:		
Residential real estate mortgages	$ 4,050,000	5,936,000
Residential real estate mortgages held for sale	943,000	2,557,000
Construction loans	2,702,000	-
Commercial real estate mortgages, including multi-family residential real estate	11,729,000	395,000
Commercial business loans	510,000	3,672,000
	$ 19,934,000	12,560,000
Unused lines of credit	$ 36,831,000	42,745,000
Standby letters of credit	1,113,000	696,000
Unadvanced portions of construction loans	8,084,000	2,257,000

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 Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the counter party. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment, and income-producing commercial properties. As discussed in note 3, the Company has recorded an allowance for possible losses on commitments and unfunded loans totaling $16,070 and $178,818 at June 30, 2008 and 2007, respectively.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those guarantees are issued to support private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. As of June 30, 2008 and 2007, the maximum potential amount of the Company’s obligation was $1,113,000 and $696,000, respectively, for financial and standby letters of credit. The Company’s outstanding letters of credit generally have a term of less than one year. If a letter of credit is drawn upon, the Company may seek recourse through the customer’s underlying line of credit. If the customer’s line of credit is also in default, the Company may take possession of the collateral, if any, securing the line of credit.

Lease Obligations

The Company leases certain properties and equipment used in operations under terms of operating leases which include renewal options. Rental expense under leases approximated $592,000, $589,000 and $662,000 for the years ended June 30, 2008, 2007 and 2006, respectively.

Approximate future minimum lease payments over the remaining terms of leases at June 30, 2008 are as follows:

2009	$ 458,557
2010	430,225
2011	361,600
2012	361,076
2013	192,033
2014 and thereafter	306,257
	$ 2,109,748

Legal Proceedings

The Company and its subsidiary are parties to litigation and claims arising in the normal course of business. Management believes that the liabilities, if any, arising from such litigation and claims will not be material to the Company's consolidated financial position or results of operations.

15. Condensed Parent Information

Condensed balance sheets for Northeast Bancorp at June 30, 2008 and 2007, and statements of income and cash flows for each of the years in the three year period ended June 30, 2008, are presented below.

Balance Sheets	June 30,	
Assets	2008	2007
Cash	$ 417,838	1,339,286
Available-for-sale securities	953,617	565,516
Investment in banking subsidiary	51,582,074	51,464,689
Investment in common securities of affiliated trusts	496,000	496,000
Goodwill, net	407,897	407,897
Other assets	2,987,843	3,213,580
Total assets	$ 56,845,269	57,486,968
Liabilities and Stockholders' Equity		
Junior Subordinated Debentures issued to affiliated trusts	$ 16,496,000	16,496,000
Other liabilities	75,957	141,090
	16,571,957	16,637,090
Stockholders' equity	40,273,312	40,849,878
Total liabilities and stockholders' equity	$ 56,845,269	57,486,968

Statements of Income

	Years Ended June 30,		
	2008	2007	2006
Income:			
Dividends from banking subsidiary	$ 3,300,000	2,500,000	1,250,000
Other income	265,516	233,814	147,233
Total income	3,565,516	2,733,814	1,397,233
Expenses:			
Interest on Junior Subordinated Debentures paid to affiliated trusts	1,064,964	1,080,538	1,063,681
General and administrative expenses	338,694	372,513	151,421
Total expenses	1,403,658	1,453,051	1,215,102
Income (loss) before income tax benefit and equity in undistributed net income of subsidiary	2,161,858	1,280,763	182,131
Income tax benefit	402,919	427,997	367,542
Income before equity in undistributed net (loss) income of subsidiary	2,564,777	1,708,760	549,673

Equity in undistributed net (loss) income of subsidiary	(633,488)	177,917	3,454,526
Net income	$ 1,931,289	1,886,677	4,004,199

Statements of Cash Flows	Years Ended June 30, 2008	2007	2006
Cash flows from operating activities:			
Net income	$ 1,931,289	1,886,677	4,004,199
Adjustments to reconcile net income to net cash provided by operating activities:			
Amortization	24,000	24,000	24,000
Stock grant	2,661	-	-
Undistributed loss (earnings) of subsidiary	633,488	(177,917)	(3,454,526)
Write down on available-for-sale securities	147,247	50,442	33,404
Net gain on available-for-sale securities	(78,789)	(43,513)	(17,693)
Write down of non-marketable investments	47,020	248,482	42,257
Decrease (increase) in other assets	227,045	(366,431)	(272,411)
(Decrease) increase in other liabilities	(65,133)	56,876	9,934
Net cash provided by operating activities	2,868,828	1,678,616	369,164
Cash flows from investing activities:			
Increase in investment of bank subsidiary	-	(400,000)	-
Purchases of available-for-sale securities	(1,653,242)	(1,964,213)	(1,063,076)
Proceeds from sales of available-for-sale securities	983,956	2,249,946	855,635
Net cash used by investing activities	(669,286)	(114,267)	(207,441)