NORTHEAST BANCORP /ME/
Form 10-K
September 27, 2007

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, 2007

[ ] 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 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 29, 2006, was approximately $46,845,271 based on the last reported sales price of the Company's common shares on the American Stock 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 2,391,332 common shares of the registrant outstanding as of September 20, 2007.
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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 2007 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 eleven 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 as 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, 2007, the Company, on a consolidated basis, had total assets of approximately $557 million, total deposits of approximately $365 million, and stockholders' equity of approximately $41 million. Unless the context otherwise requires, references herein to the Company include the Company and its subsidiaries 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. 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 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.

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With the goal of providing a full range of banking and other financial related 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, Bethel, Jackman, Livermore Falls, Mexico, Rangeley, Scarborough, South Paris and Turner, Maine from where the Bank's insurance division offers personal and commercial casualty and property insurance products. The Company's market area, which covers western and south central regions of the State of Maine, is characterized by a diverse economy that has experienced moderate 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 and interest rates and services, 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. 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 will procure mortgagee's title insurance to protect against defects in its lien on the property that may 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 matters, 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, 2007 was $2,597,020, 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 15 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 collateralized by short-term assets whereas term loans are primarily collateralized by long-term assets.

As a result, 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 86 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 FNMA 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, 2007, was approximately $6.4 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 $100,000 and all new collateralized loans of more than $750,000 require pre-approval by the Bank's loan committee, which is currently comprised of five directors of the Bank and meets on such basis as is deemed necessary to promptly service loan demand. 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, 2007, investment in and loans to this subsidiary constituted 0.80% of the Company's total assets.

Employees

As of June 30, 2007, the Company, the Bank and its subsidiary together employed 200 full-time and 24 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 will 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, 2007, under dividend restrictions imposed under federal and state laws, Northeast Bank could declare, without obtaining governmental approvals, aggregate dividends to the Company of approximately $3,632,000.

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 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, 2007, the Company's consolidated Tier 1 Capital ratio was 9.07% and its Total Capital ratio was 13.97%.

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, 2007, was 12.02%.

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, 2007, 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, 2007, 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 semiannual 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. Those rules are intended to allow shareholders to more easily and efficiently monitor the performance of companies and directors.

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, 2008 (i.e., fiscal year 2009). 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 Exchange Act of 1934, 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 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 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.

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.

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 Northeast Bancorp's financial performance. When analyzing an investment in Northeast Bancorp (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 rates 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, 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

The Company regularly purchases U.S. Government-sponsored enterprise debt securities, U.S. Government agency 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.

Competition

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.

Government Regulation and Supervision

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.

Internal Controls and Procedures

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.

Litigation

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

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 were relocated to 500 Canal Street, Lewiston, Maine ("Headquarters Building") from 158 Court Street, Auburn, Maine in August, 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 and completed the relocation of the above offices and departments in August 2005.

In addition to the branch office located in our Headquarters Building, we have 11 additional banking branches located in the State of Maine, 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	Lease (5)
350 Minot Avenue, Auburn*	Lease (5)
235 Western Avenue, Augusta*	Fee Simple

11 Main Street, Bethel*	Fee Simple
346 Main Street, Jackman	Lease (5)
28 Main Street, Livermore Falls	Lease (7)
89 Main Street, Mexico	Lease (5)
2568 Main Street, Rangeley	Lease (5)
423 U. S. Route 1, Scarborough	Lease (6)
235 Main Street, South Paris*	Fee Simple
10 Snell Hill Road, Turner	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 one year and automatically renews in September each year.
(6) Lease term is three years and expires July 31, 2010.
(7) Lease term is eight months and expires December 31, 2007.

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.

On September 1, 2006, the Company purchased its South Paris, Maine branch, previously leased from a member of our Board of Directors. The $400,000 purchase price was based upon an independent appraisal. The consideration paid was 5,000 shares of Company common stock and $297,000 in cash. The common stock issued was based on the market price on the day prior to the closing. This acquisition was not material to the balance sheet or the results of operations for the Company.

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 securities-holders during the fourth quarter of the fiscal year ended June 30, 2007.

Executive Officers of the Registrant

Pursuant to the Instructions of Form 10-K and Item 401(b) of Regulation S-K, 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	56	President and Chief Executive Officer (1)
Philip C. Jackson	63	Senior Vice President of Bank Trust Operations
Pender J. Lazenby	57	Chief Risk Officer
Marcel Blais	48	Chief Operating Officer
Robert S. Johnson	55	Chief Financial Officer (1)
Suzanne Carney	40	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.

Philip C. Jackson has been a director of the Company and the Bank since 1987. Mr. Jackson also has served as the Senior Vice President of the Bank's Trust Operations since 1997. From 1991 to 1994, Mr. Jackson served as President of Bethel Savings Bank, the predecessor to the Bank.

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 20, 2007, there were approximately 2,391,332 shares of common stock outstanding held by approximately 446 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.

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

2005 – 2006	High	Low	Div Pd
Jul 1- Sep 30	22.50	19.85	.090
Oct 1 - Dec 31	24.00	21.66	.090
Jan 1 - Mar 31	24.50	20.80	.090
Apr 1 - Jun 30	22.10	20.76	.090

On September 20, 2007, the last reported sale price of the Company's Common stock as quoted on NASDAQ was $17.75. 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, 2007 totaled 3,800 shares at an average price per share of $17.88.

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	-	-	-	200,000
May 1 – May 31	-	-	-	200,000
Jun. 1 – Jun. 30	3,800	17.88	3,800	196,200

(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, 2007, unless extended.

Item 6. Selected Financial Data

	At or for the Year Ended June 30,				
	2007	2006	2005	2004	2003
	(Dollars in thousands except for Per Share Data)				
Selected operations data:					
Interest income	$ 35,682	$ 35,456	$ 32,674	$ 28,124	$ 29,026
Interest expense	20,097	16,761	13,967	12,079	13,769
Net interest income	15,585	18,695	18,707	16,045	15,257
Provision for loan losses	989	1,226	1,302	962	1,091
Other operating income (1)	7,903	6,578	5,083	4,670	4,174
Net securities gains	42	17	68	201	922
Other operating expenses (2)	20,075	18,209	16,684	14,799	13,530
Income before income taxes	2,466	5,855	5,872	5,155	5,732
Income tax expense	579	1,851	1,853	1,643	1,877
Net income	$ 1,887	$ 4,004	$ 4,019	$ 3,512	$ 3,855
Consolidated per share data:					
Net income:					
Basic	$ 0.77	$ 1.61	$ 1.60	$ 1.38	$ 1.46
Diluted	$ 0.76	$ 1.59	$ 1.57	$ 1.35	$ 1.44
Cash dividends	$ 0.36	$ 0.36	$ 0.36	$ 0.35	$ 0.32
Selected balance sheet data:					
Total assets	$ 556,801	$ 562,918	$ 575,900	$ 538,754	$ 467,684
Loans receivable	425,571	435,663	461,052	432,594	378,987
Deposits	364,554	395,293	396,219	377,820	318,743

Borrowings	147,564	124,860	136,293	121,443	109,871
Total stockholders' equity	40,850	39,096	39,870	36,453	36,499
Other ratios:					
Return on average assets	0.34%	0.70%	0.71%	0.71%	0.86%
Return on average equity	4.59%	9.95%	10.39%	9.50%	10.58%
Average equity to average total assets	7.37%	7.07%	6.86%	7.51%	8.11%
Common dividend payout ratio	46.77%	22.40%	22.65%	25.93%	22.22%

(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, 2007, 2006 and 2005. 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 2007 have been reclassified to conform to the 2007 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, 2007, from 12 banking offices and 11 insurance agency offices all located in western and south-central Maine. At June 30, 2007, we had consolidated assets of $556.8 million and consolidated stockholders' equity of $40.8 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 eight 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 2007 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, 2007, we acquired four insurance agencies. On August 30, 2007, we acquired the Hartford Agency in Lewiston, Maine, our fifth purchase, for $1,358,000 in cash and debt.

The Company's profitability is affected by the Bank's 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. It 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 modest economic growth and a slowing of real estate appreciation from 2006 through 2007. 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 2007 to fiscal 2006:

- Four insurance agencies were acquired in twelve months ended June 30, 2007.
- Revenues from our investment brokerage, insurance, and trust and wealth management divisions increased by 28%.
- Commercial real estate loans were sold to the secondary market, increasing gain on sale income by $428,000.
- Net interest margins decreased to 299 basis points compared to 349 basis points in fiscal 2006 and, combined with a decrease in total interest earning assets, resulted in a decrease in net interest income.
- Though net income decreased in fiscal 2007, our financial condition and liquidity remain strong.
- The Company and the Bank are “well capitalized” under regulatory definitions.
- The allowance for loan losses increased by $260,000 in fiscal 2007, to $5,756,000, and, as a percentage of total loans, increased in fiscal 2007 to 1.35% compared to 1.26% in fiscal 2006.
- Net income decreased to $1,886,677 for fiscal 2007 compared to $4,004,199 for fiscal 2006.

On September 1, 2006, the Bank purchased the real estate located at 235 Main Street, South Paris, Maine, (our South Paris branch) from a director for a purchase price of $400,000. The price was determined through an independent, third party appraisal. We paid $297,000 in cash and 5,000 shares of Northeast Bancorp common stock (based on the $20.60 per share closing price on August 31, 2006). Management believes that the transaction reflected arms-length, negotiated terms.

RESULTS OF OPERATIONS

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 $4.7 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	$ 131,490	$ 375,714	$ 507,204
Loans, net	(1,075,851)	799,395	(276,456)
FHLB deposits & other	33,336	42,035	75,371
Total interest-earning assets	(911,025)	1,217,144	306,119
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	$ (670,514)	$ (2,359,759)	$ (3,030,273)

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 $197,674 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 nonperforming 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 nonperforming 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 nonperforming loans, to $5,090,000, primarily due to nonperforming commercial real estate loans. Of total non-performing loans at June 30, 2007, $2,038,000 million was current with principal and interest payments. Nonperforming 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.

Comparison of Fiscal Years Ended June 30, 2006 and 2005

For fiscal 2006, we reported net income of $4,004,199, or $1.59 per diluted share, as compared to $4,018,634, or $1.57 per diluted share, for the fiscal year ended June 30, 2005 ("fiscal 2005"), a decrease of $14,435, or less than 1%. This decrease was attributable to increased noninterest expense which slightly exceeded the increase in noninterest income. The return on average assets was 0.70% in fiscal 2006 compared to 0.71 % in fiscal 2005. The return on average assets changed due to total average assets increasing by $5.8 million, or 1%, compared to fiscal 2005. The return on average equity was 9.95% in fiscal 2006 and 10.39% in fiscal 2005. The decrease in our return on average equity was due to decreased net income for those periods and an increase in average equity of 4%.

Net interest income decreased by less than 1% during fiscal 2006. This decrease was primarily due to a decrease in our net interest margin of 1 basis point. Average interest earning assets increased approximately $5.4 million as compared to the average interest earning assets in fiscal 2005. Of the increase in average interest earning assets, average investment securities increased $10.6 million and average loans decreased $4.8 million. Net interest margin, the ratio of net interest income to average interest earning assets, decreased to 3.49% in fiscal 2006 from 3.50% in fiscal 2005. Net interest spread, the difference between the yield on interest earning assets and the cost of funds, decreased by 8 basis points to 3.15% in fiscal 2006 from 3.23% in fiscal 2005. The Bank balance sheet moved during fiscal 2006 from an asset sensitive profile, where the yields on assets reprice faster that the cost of funds, to a slightly liability sensitive profile, where cost of funds reprice faster than the yields on assets. Noninterest income increased 28% during fiscal 2006 primarily from increased investment brokerage and insurance commission revenue, loan servicing fees, gains on the sale of residential real estate loans, and the gain on sale of deposits. This increase was partially offset by lower net securities gains. The provision for loan losses decreased 6%, primarily resulting from a decrease in loans. Noninterest expense increased 9% during fiscal 2006, which was primarily due to increases in salaries and employee benefits expense, occupancy and equipment expense associated with the consolidation of the Bank's operations and administration functions into a new Gateway headquarters in Lewiston and the full year impact of the Solon-Anson Insurance Agency acquisition (September, 2004), partially offset by a decrease in other expense. Other expense in fiscal 2005 included a loss from the write-off of deferred issuance costs related to trust preferred securities redeemed on December 31, 2004.

Net Interest Income

Net interest income decreased by $11,484, or less than 1%, during fiscal 2006 primarily resulting from a decrease in the net interest margin. Average interest earning assets increased $5.4 million during fiscal 2006, comprised of a $10.6 million increase in average investment securities, partially offset by a $4.8 million decrease in average loans and a $0.5 million decrease in interest-bearing deposits (primarily with the Federal Home Loan Bank). The increase in average investment securities was due to increases in mortgage-backed securities, pledged as eligible collateral for FHLB advances and securities sold under agreements to repurchase and municipal securities. The decrease in average loans resulted from a decrease in construction loans, commercial loans and commercial real estate loans of $18.8 million, partially offset by increases in residential real estate loans and consumer loans of $3.0 million and $11.0 million, respectively. Origination of commercial loans and commercial real estate loans decreased by $60 million in fiscal 2006 compared to fiscal 2005. Average interest-bearing deposits increased by $0.6 million, or 0.1%, during fiscal 2006, with the increase primarily consisting of time deposits. Average certificates of deposit increased by $43.7 million. All other interest-bearing deposits decreased including average brokered time deposits, which decreased by $31.7 million, or 36%, reflecting a reduction in our use of wholesale funding. Average repurchase agreements increased during fiscal 2006 by $0.9 million, or 3%. Average borrowings increased primarily due to a new obligation under a capital lease. The yield on average interest earning assets increased 48 basis points to 6.60% in fiscal 2006. The cost of funds increased 56 basis points, to 3.45%, due to an increase in the cost of interest-bearing deposits, partially (offset by) a decrease in the costs of advances from the FHLB and junior subordinated debentures (refinanced in fiscal 2005). 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 2005 to 2006 in net interest income by category due to changes in rate and volume.

Rate/Volume Analysis for the Year Ended
June 30, 2006 versus June 30, 2005

	Difference Due to		
	Volume	Rate	Total
Investments	$ 437,837	$ 378,420	$ 816,257
Loans, net	(314,444)	2,338,463	2,024,019
FHLB deposits & other	(8,398)	68,098	59,700
Total interest-earning assets	114,995	2,784,981	2,899,976
Deposits	14,332	2,513,176	2,527,508
Repurchase agreements	11,589	512,560	524,149
Borrowings	42,541	(300,440)	(257,899)
Total interest-bearing liabilities	68,462	2,725,296	2,793,758
Net interest income	$ 46,533	$ 59,685	$ 106,218

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 lease, and junior subordinated debentures. The adjustments to interest income and yield to a fully tax equivalent basis were $117,702 and $0 for the twelve months ended June 30, 2006 and 2005, respectively.

Provision for Loan Losses

The provision for loan losses in fiscal 2006 was $1,226,413, a decrease of $75,187, or 6%, compared to fiscal 2005. This decrease in the provision for loan losses reflects the significant overall decrease in loans of approximately $25.4 million and a decrease in net loan charge-offs. Although we experienced higher loan delinquency, higher nonperforming loans, and higher classified and criticized loans for fiscal 2006, the level of expected loan defaults and the level of loss did not increase. Net charge-offs were $630,300 in fiscal 2006 compared to $774,600 in fiscal 2005. This $144,300 decrease was in residential real estate, commercial real estate loans and consumer loans. Net charge-offs to average loans outstanding was 0.14% in fiscal 2006 compared to 0.17% in fiscal 2005.

The allowance for loan losses at June 30, 2006 was $5,496,000 as compared to $5,104,000 at June 30, 2005, an increase of $392,000, or 8%. This increase was net of $204,000 reclassified from the allowance for loan losses to a separate reserve account for off-balance credit risk (unadvanced lines of credit and loan commitments) included in other liabilities. This off-balance credit risk had been included in the allowance for loan loss in prior years. The ratio of the allowance to total loans was 1.26% at June 30, 2006 compared to 1.11% at June 30, 2005. The ratio of the allowance for loan losses to nonperforming loans was 106% at June 30, 2006 and 301% at June 30, 2005, reflecting an increase of $3.5 million in nonperforming loans, to $5.2 million, primarily from nonperforming commercial real estate and commercial loans. Of total non-performing loans at June 30, 2006, $1.9 million was current with principal and interest payments. Nonperforming loans were 1.19% of total loans at June 30, 2006 as compared to 0.37% at June 30, 2005, also due to the increase in nonperforming loans at June 30, 2006 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, 2006 and 2005 was $6,594,881 and $5,151,179, respectively, an increase of $1,443,702, or 28%, in fiscal 2006. Most of this increase was due to the increase in investment brokerage and insurance commission revenue and a gain from the sale of the deposits and certain loans of the Lisbon Falls branch.

Fees for other services to customers of $1,114,081 increased $46,965, or 4%, during fiscal 2006. This increase was due to higher transaction service fees, overdraft fees, and ATM and debit card fee revenue as compared to fiscal 2005.

Net securities gains of $17,335 decreased $50,605, or 74%, during fiscal 2006. The volume of securities sold in fiscal 2006 decreased from fiscal 2005. 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. Other-than-temporary write-downs on equity securities of $38,394 and $27,849 during fiscal 2006 and 2005, respectively, were included in noninterest expense.

Gains on the sales of loans of $308,777 increased $75,750, or 33%, during fiscal 2006. This increase was primarily due to a higher sales volume of residential real estate loans, which increased by $4 million, to $15 million, in fiscal 2006 compared to $11 million in fiscal 2005. Sold loan volume was impacted by 30 year fixed rate residential real estate loan origination volume, which is subject to changing interest rates, and a shift in the demand for loans with fixed or adjustable interest rates. The Bank continues to hold in portfolio all new 15 year fixed rate loans and all adjustable rate loans. Residential real estate loans were sold to reduce our exposure to interest rate risk.

Investment commission revenue of $1,769,300 increased $314,437, or 22%, during fiscal 2006. This increase was primarily due to adding investment brokers and increased production from existing investment brokers.

Insurance commissions of $1,916,822 increased $512,787, or 37%, during the fiscal year 2006 due to the full year impact of the acquisition of the Solon Anson Insurance Agency (September 2004) and increased contingency payments from insurance carriers based on loss experience.

BOLI income of $366,939 increased $36,239, or 11%, during fiscal 2006. This increase was due to an increase in the average interest yield to 4.21% in fiscal 2006 from 4.15% in fiscal 2005. 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 income of $1,003,997 increased $511,273, or 104%, during fiscal 2006. This increase was primarily due to the deposit premium received of $500,845 from the sale of the deposits and certain loans of the Lisbon Falls branch to Androscoggin Bank. Trust fee revenue also increased by $109,266. The deposit premium and increased trust fees were partially offset by change in loss on the disposal of fixed assets of $188,082. The latter represents costs written off for a new branch site which was abandoned in fiscal 2006. A $59,719 gain was realized in fiscal 2005 from the sale of our former Richmond branch building.

Noninterest Expense

Noninterest expense for fiscal years ended June 30, 2006 and 2005 was $18,208,504 and $16,684,174, respectively, an increase of $1,524,330, or 9%. The increase in fiscal 2006 was primarily the result of an increase in salaries and employee benefits and occupancy and equipment expenses. Our efficiency ratio increased to 72.0% during fiscal 2006 from 69.9% in fiscal 2005 due to increased noninterest expense.

Salaries and employee benefits expense of $10,637,758 increased $1,083,441, or 11%, during the fiscal year 2006. This increase includes the salary and benefits for new positions in commercial lending, investment brokerage, insurance agency, trust, and risk management divisions. Total full-time equivalent employees were 201 compared to 193 at June 30, 2006 and 2005, respectively. Deferred compensation expense related to the Solon-Anson Insurance acquisition was $399,845, an increase of $301,769 compared to fiscal 2005.

Occupancy expense of $1,672,505 increased $253,809, or 18%, during the fiscal year 2006. This increase was primarily due to the relocation of our commercial, administration and operations to the new Southern Gateway building in Lewiston, completed in August 2005. Expenses contributing to this increase were amortization of capital lease asset, depreciation of leasehold improvements and real estate taxes. Repairs to the Mechanic Falls branch for mold remediation increased building repairs by $25,305. Higher heating fuel oil costs increased utilities expense by $55,611.

Equipment expense of $1,440,238 increased $330,130, or 30%, during the fiscal year 2006. As with occupancy expense, moving expense and increased depreciation expense from new furniture and equipment for the new Southern Gateway building accounted for most of this increase. Additional licensing fees for our core operating system for new customer relationships also contributed to this increase.

Other expense of $4,216,975 decreased $134,377, or 3%, during fiscal year 2006. This decrease was due in part to the $396,425 loss recognized in fiscal 2005 from the write-off of unamortized deferred issuance costs related to the redemption of the 9.60% trust preferred stock. Also contributing to this decrease was other-than-temporary write downs on equity and non-marketable securities of $38,394 and $42,257, respectively, for fiscal 2006 compared to $27,849 and $96,931, respectively, in fiscal 2005, an aggregate decrease of $44,129. 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 this decrease was an increase of $155,719 in advertising expense resulting from increased use of television advertising, and an increase of $108,841 in computer services expenses resulting from higher investment brokerage transaction costs, increased processing fees from higher trust activity, increased internet banking costs from higher customer enrollment and conversion costs and core system users in the insurance agency.

Taxes

The Company's effective tax rate was 31.7% and 31.5% for the fiscal years ended June 30, 2006 and 2005, respectively. See Note 12 in the Consolidated Financial Statements for additional information.

Comprehensive Income

The Company's comprehensive income was $2,051,917 and $4,745,415 during 2006 and 2005, respectively. Comprehensive income differed from our net income in 2006 and 2005 due to the change in the fair value of available-for-sale securities, net of income tax. In fiscal 2006, there was a net decrease in fair value of $1,952,282 due to a net unrealized loss on investments available-for-sale, net of income tax. There was a net increase in fair value in fiscal 2005 of $726,781. See the Consolidated Statements of Changes in Stockholders' Equity and Note 16 in the Consolidated Financial Statements for additional information.

FINANCIAL CONDITION

The Company's total assets decreased $6,116,822, or 1%, to $556,800,980 at June 30, 2007 compared to $562,917,802 at June 30, 2006. This decrease was primarily due to a $10,091,111 decrease in total loans, primarily construction, commercial real estate and commercial loans, partially offset by an $4,663,322 increase in goodwill and intangibles created from the acquisition of four insurance agencies. The cash flow from the decrease in loans was utilized to repay brokered time deposits at maturity. Also, advances from the FHLB increased $17,128,100 to replace the funding of brokered time deposits. Stockholders' equity totaled $40,849,878 and $39,096,125 at June 30, 2007 and 2006, respectively, an increase of $1,753,753. Stockholders' equity was increased by net income of $1,886,677, a decrease in net unrealized losses on available-for-sale securities of $707,923, proceeds from the exercise of previously granted stock options of $6,550 and stock issued of $103,000 in connection with the purchase of branch real estate. These increases were offset by share repurchases and retirements of $67,944 and payment of cash dividends of $882,453.

Cash and Cash Equivalents

Average cash and cash equivalents (cash and due from bank and short-term investments) decreased $1,258,962, to $11,174,060, in fiscal 2007 as compared to $12,433,022 in fiscal 2006. This decrease was due to the transfer of our clearing activity to Banker’s Bank Northeast, reducing reserves balances maintained at the Federal Reserve Bank of

Boston.

Investments Securities and Other Interest-earning Assets

The average balance of the available-for-sale securities portfolio was $84,705,459 and $80,050,271 for fiscal 2007 and fiscal 2006, respectively. This increase of $4,655,188, or 6%, provided additional collateral for FHLB advances and securities sold under agreements to repurchase. 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.

All of the Company's securities are classified as available-for-sale and were carried at fair value of $86,348,070 and $86,137,707 as of June 30, 2007 and 2006, respectively. These securities had net unrealized losses after taxes of $1,914,546 at June 30, 2007 and $2,622,469 at June 30, 2006. 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 $433,576,281 in fiscal 2007, compared to $448,610,511 in fiscal 2006. This decrease of $15,034,230, or 3%, in our average balance for loans at June 30, 2007, 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 $147,432,431 in fiscal 2007, as compared to $149,940,456 in fiscal 2006. This decrease of $2,508,025, 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, 2007 and 2006, respectively. Of residential real estate loans at June 30, 2007, approximately 37% were variable rate products, compared to 43% at June 30, 2006. 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 2007. The decrease reflects the Bank’s tightening of credit underwriting standards as delinquencies and classified and criticized 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 $116,384,948 in fiscal 2007 and $121,279,403 in fiscal 2006. This decrease of $4,894,455, or 4%, 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 26% of the total loan portfolio at both June 30, 2007 and 2006, respectively. Approximately 94% 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 96% of this portfolio at June 30, 2006.

Construction loans averaged $7,009,832 in fiscal 2007 and $8,840,891 in fiscal 2006. This decrease of $1,831,059, or 21%, was primarily in commercial construction loans. Construction loans were 1% of the total loan portfolio at June 30, 2007 and 2006, 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 and verified by inspection. Approximately 60% of the construction loans were variable rate product at June 30, 2007, compared to approximately 30% at June 30, 2006.

Commercial loans averaged $44,762,107 in fiscal 2007 and $58,416,018 in fiscal 2006. This decrease of $13,653,911, or 23%, reflects the above factors and reduced warehouse lines of credit. Commercial loans were 10% and 12% of total loans at June 30, 2007 and 2006, respectively. Variable rate products comprised 58% and 56% of this loan portfolio at June 30, 2007 and 2006, 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 $115,314,393 in fiscal 2007 and $107,591,979 in fiscal 2006. This increase of $7,722,414, or 7%, was attributable to new recreational vehicle loans. Consumer and other loans comprised 29% and 26% of total loans at June 30, 2007 and 2006, respectively. Consumer, including indirect auto and recreational vehicle, and other loans are mostly fixed rate products. At June 30, 2007 and 2006, we held $36,808,246 and $39,075,798 of indirect auto loans, respectively. Indirect auto, indirect RV and indirect mobile home loans together comprised approximately 95% of total consumer and other loans, a slight decrease from 96% in 2006. The detail of consumer loans at June 30, 2007 and 2006 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 to 1.78% from 1.45%, and an increase in the net charge-off of consumer loans to $443,000 from $286,000 for the fiscal years ended June 30, 2007 and 2006, respectively.

	Consumer Loans			
	June 30, 2007	% of Total	June 30, 2006	% of Total
Indirect Auto	$ 36,808,246	31%	$ 39,075,798	35%
Indirect RV	51,611,223	43%	41,111,060	36%
Indirect Mobile Home	24,961,562	21%	28,212,411	25%
Subtotal Indirect	113,381,031	95%	108,399,269	96%
Other	5,499,692	5%	4,793,128	4%
Total Consumer Loans	$ 118,880,723	100%	$ 113,192,397	100%

BOLI averaged $9,082,562 in fiscal 2007 and $8,717,180 in fiscal 2006. One new general account policy was purchased in fiscal 2007 for $600,000. BOLI assets were invested in the general account of three insurance companies and separate accounts in a third quality 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, 2007. 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 21.12% of capital plus the allowance for loan losses at June 30, 2007.

Goodwill and intangible average assets were $1,404,753 and $3,015,589, respectively, for fiscal 2007, and $407,897 and $2,048,461, respectively, for fiscal 2006. These increases resulted from the acquisition of four insurance agencies during fiscal 2007. The allocation of the purchase price paid for the four insurance agency acquisitions in excess of tangible assets acquired added $2,472,906 to goodwill and $2,505,000 to intangibles in the form of customer lists and non-compete agreements. These intangibles are being amortized over lives from 5 to 18 years, with an average of 12.55 years. Goodwill and intangibles are subject to impairment testing annually. No impairment expense was recognized in fiscal 2007.

Deposits

Average demand deposit accounts were $35,420,046 for the year ended June 30, 2007 as compared to $39,161,547 in fiscal 2006. The increase of $3,741,501, or 10%, was related to the loss of commercial real estate and commercial loans during fiscal 2007.

Average interest-bearing deposits decreased by $13,513,511, or 4%, during fiscal 2007 to $342,601,166. This decrease was primarily due to decreased brokered time deposits and non-maturing, interest-bearing deposits. Average certificates of deposit balances increased $19,445,872, to $218,915,654, primarily from the promotion of time deposits as interest rates remained high during fiscal 2007. This increase allowed the Bank to decrease brokered time deposits as they matured. Average brokered time deposit balances decreased $18,777,144, or 33%, to $37,352,470 in fiscal 2007 from $56,129,614 in fiscal 2006. All other non-maturing interest-bearing deposits decreased during fiscal 2007. NOW, money market, and savings balances declined as customers moved balances to higher yielding time deposits. Average NOW accounts decreased $5,301,826, or 9%, during fiscal 2007 to $54,666,850. The average interest rate paid on NOW accounts increased from 1.93% in fiscal 2006 to 2.26% in fiscal 2007. Average money market accounts decreased $3,735,870, or 29%, to $9,357,336 in fiscal 2007. The average interest rate paid on money market accounts increased from 1.88% in fiscal 2006 to 2.36% in fiscal 2007. Average savings accounts decreased $5,144,543, or 19%, to $22,308,856 during fiscal 2007. The average interest rate paid on savings accounts increased from 0.83% in fiscal 2006 to 0.87% in fiscal 2007. The average interest rate paid on certificates of deposit increased from 3.72% in fiscal 2006 to 4.62% 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 yearand have interest rates equal to or slightly above comparable FHLB advances. At June 30, 2007, outstanding brokered time deposits of $22,546,163 as a percentage of total assets was 4.05%, compared to 9.21% at

June 30, 2006. The average interest rate paid on brokered time deposits increased from 3.58% in fiscal 2006 to 4.69% in fiscal 2007. 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 2007.

Other Funding Sources

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

Average short-term borrowings during fiscal 2007 were $36,144,925, compared to $31,427,133 during fiscal 2006. The increase of $4,717,792, or 15%, was due to one existing customer. This liability was collateralized by U.S. government-sponsored enterprise and federal agency mortgage-backed securities. See Note 8 to the Consolidated Financial Statements.

Average FHLB advances for fiscal 2007 were $79,209,913, compared to $79,648,575 in fiscal 2006. This decrease was $438,662, or 1%. These advances had an average cost of 4.84% during fiscal 2007 compared to 4.40% during fiscal 2006. At June 30, 2007 and 2006, FHLB advances were $93,016,698 and $75,888,598, respectively. The Company had unused advance capacity with the FHLB of $19,576,000 at June 30, 2007. Management intends to increase available FHLB advance capacity by continuing to add qualifying securities. See Note 8 to the Consolidated Financial Statements.

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 1.00%. At June 30, 2007, the credit availability under the Borrower in Custody program was $28,690,000. There were no borrowings outstanding under this credit line at June 30, 2007.

The following is a summary of the unused borrowing capacity of the Bank at June 30, 2007 and available to meet our short-term funding needs:

Brokered time deposits	$ 116,654,000	Subject to policy limitation of 25% of total assets
Federal Home Loan Bank of Boston	$ 19,576,000	Unused advance capacity subject to eligible and qualified collateral
Fed Discount Window Borrower-in-Custody	$ 28,690,000	Unused credit line subject to the pledge of indirect auto loans
Total Unused Borrowing Capacity	$ 164,920,000	

We had outstanding $16,496,000 at June 30, 2007 and 2006, respectively, of junior subordinated debentures issued by us to affiliated trusts. See "Capital" for more information on junior subordinated debentures and affiliated trusts.

ASSET QUALITY

We monitor our asset quality with 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, 2007 and 2006, the allowance for loan losses was $5,756,000 and $5,496,000, respectively. The increase in the allowance for loan losses was attributed to the increasing mix of consumer indirect loans with a higher risk profile in the Bank's loan portfolio, the increase in loan delinquencies and an increase in internally classified and criticized loans.

The allowance for loan losses as a percentage of total loans was 1.35% and 1.26% at June 30, 2007 and 2006, respectively. This increase of 9 basis points was attributable to a decline in loans in fiscal 2007 compared to fiscal 2006.

Classified loans, exclusive of non-performing loans, that could potentially become non-performing due to delinquencies or marginal cash flows were $2,542,000 and $3,349,000 at June 30, 2007 and 2006, respectively. Significant credit losses are not expected.

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:

06/30/07	06/30/06	06/30/05	06/30/04
2.90%	2.09%	1.09%	1.13%

The delinquency for the years prior to June 30, 2006 have been restated because we changed the method of measuring past due loans to the number of days lapsed from the date of last payment from the number of payments past due. For the years ended June 30, 2005 and 2004, the previously reported delinquency and current non-accrual loans were 0.96% and 0.66%, respectively.

Non-performing Assets

Total non-performing loans were $5,090,000 and $5,195,000 at June 30, 2007 and 2006, respectively. This decrease of $105,000, or 2%, was attributable primarily to commercial real estate and commercial loans. Of non-performing commercial real estate and commercial loans, $627,000 and $1,411,000, 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, 2007. The following table represents the non-performing loans as of June 30, 2007 and 2006.

Description	June 30, 2007	June 30, 2006
Residential real estate	$ 477,000	$ 521,000
Commercial real estate	2,033,000	2,980,000
Commercial loans	2,104,000	1,553,000
Consumer and other	476,000	141,000
Total non-performing	$ 5,090,000	$ 5,195,000

Non-performing loans as a percentage of total loans were 1.20% and 1.19% at June 30, 2007 and 2006, respectively. The allowance for loan losses was equal to 113% and 106% of total non-performing loans at June 30, 2007 and 2006, respectively. At June 30, 2007, non-performing loans included $2,038,000 of loans that are current and paying as agreed, but which the Bank maintains as non-performing until the borrower has 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 2.42% and 1.66% for June 30, 2007 and 2006, 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 $729,000 during 2007, compared to $630,000 in 2006. Net charge-offs as a percentage of average loans outstanding were 0.17% and 0.14% in 2007 and 2006, respectively. The increase of $99,000 was due to higher gross charge-offs in indirect consumer loans and commercial 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 $15,011,000 and $12,228,000 at June 30, 2007 and 2006, 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 and also reflects a tightening of our credit standards. 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, 2007, $3,935,000 of this amount was non-performing commercial real estate and commercial loans. The remaining $11,076,000 of commercial real estate and commercial loans classified as substandard at June 30, 2007 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 and, when appropriate, to charge-off loans against the allowance for loan losses, provide 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 2007 examination.

At June 30, 2007, the Company had no acquired assets, compared to $10,384 at June 30, 2006. The decrease of $10,384 was due to a change in accounting for repossessed vehicles and no in substance foreclosures at June 30, 2007. 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, 2007 and included in consumer loans were $199,000. See Note 5 of the Consolidated Financial Statements for additional 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, 2006, this account balance was $204,086, compared to $178,818 at June 30, 2007. The adequacy of this balance is subject to the similar analysis as the allowance for loan losses by taking into consideration the unadvanced lines of credit for commercial and home equity loans, letters of credit and commitments to make loans.

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, 2007, we estimate that our net interest income in the following 12 months would decrease by 1.80% if rates went up 200 basis points and increase by 4.60% if rates went down 200 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 the repricing of our interest-bearing assets. In a falling rate environment, the interest-bearing liabilities reprice downward more quickly than the repricing of our interest-bearing assets. Also shown in the table are the results assuming a 200 basis increase and decrease in interest rates starting June 30, 2006.

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

	Up 200 Basis Points	Down 200 Basis Points
June 30, 2006	-0.17%	2.33%

LIQUIDITY

On a parent Company only basis, our commitments and debt service requirements at June 30, 2007 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 8.16% at June 30, 2007. 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, 2006, the annual aggregate payments to meet the debt service of the junior subordinated debentures is approximately $1,060,000.

Affiliated Trusts	Trust Preferred	Junior Subordinated	Interest Rate	Maturity Date

	Securities	Common Securities	Debentures		
NBN Capital Trust II	$ 3,000,000	$ 93,000	$ 3,093,000	8.16%	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	6.42%	

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 danger 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, 2007, our banking subsidiary had $165 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 30% 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, 2007 follows:

			Payments Due by Period		
Contractual Obligations	Total	Less Than 1 Year	1-3 Years	4-5 Years	After 5 Years
FHLB advances	$ 93,016,698	$ 50,016,698	$ 33,000,000	$ 10,000,000	$ -
Junior subordinated debentures	16,496,000	-	16,496,000	-	-
Capital lease obligation	2,653,511	134,087	289,193	319,668	1,910,563
Other borrowings	2,292,163	534,522	997,665	405,777	354,199
Total long-term debt	114,458,372	50,685,307	50,782,858	10,725,445	2,264,762
Operating lease obligations	1,926,575	379,059	622,833	466,344	458,339
Total contractual obligations	$ 116,384,947	$ 51,064,366	$ 51,405,691	$ 11,191,789	$ 2,723,101

		Amount of Commitment Expiration - Per Period			
Commitments with off-balance sheet risk	Total	Less Than 1 Year	1-3 Years	4-5 Years	After 5 Years
Commitments to extend credit (1)(3)	$ 10,003,000	$ 10,003,000	$ -	$ -	$ -
Commitments related to loans held for sale(2)	2,557,000	2,557,000	-	-	-

Unused lines of credit (3)(4)	45,002,000	21,189,000	3,099,000	2,288,000	18,426,000
Standby letters of credit (5)	696,000	696,000	-	-	-
	$ 58,258,000	$ 34,445,000	$ 3,099,000	$ 2,288,000	$ 18,426,000

(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, 2007 was a loss of $10,248.

CAPITAL

At June 30, 2007 and 2006, stockholders' equity totaled $40,849,878 and $39,096,125, respectively, or 7.34% and 6.95% of total assets, respectively. In addition, we had on both June 30, 2007 and 2006, $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, 2007 of $1,886,677, stock issued for $6,550 from the exercise of stock options and $103,000 in connection with the purchase of branch real estate and a decrease of $707,923 in the net unrealized losses on available-for-sale securities offset by dividend payments of $882,453, and stock repurchases of $67,944, representing 3,800 shares repurchased at an average cost of $17.88 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 Company may discontinue the repurchase program at any time, it is scheduled to terminate on December 31, 2007. 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 2007 were 3,800 shares, for $67,944, at an average price of $17.88 per share. For fiscal 2006, the total stock repurchased was 90,200 shares, for $2,142,250, at an average price of $23.75 per share. The remaining repurchase capacity of the 2006 Plan is 196,200 shares. Since inception, total stock repurchases under the 2004 plan were 145,500 shares, for $3,204,902, through December 15, 2006. 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 $46,780,000, or 8.60% of total average assets at June 30, 2007 compared to $50,864,000, or 9.07% of total average assets, at June 30, 2006. 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.

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**

To the Board of Directors
Northeast Bancorp and Subsidiary
Lewiston, Maine

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We have audited the accompanying consolidated balance sheet of Northeast Bancorp and Subsidiary as of June 30, 2007 and the related consolidated statements of income, changes in stockholders' equity and cash flows for the year ended June 30, 2007. 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 audit. The consolidated financial statements of Northeast Bancorp and Subsidiary as of June 30, 2006 were audited by other auditors whose report dated August 11, 2006 expressed an unqualified opinion on those statements.

We conducted our audit 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 audit provides a reasonable basis for our opinion.

In our opinion, the 2007 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, 2007, and the results of their operations and their cash flows for the year ended June 30, 2007, in conformity with U.S. generally accepted accounting principles.

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

West Peabody, Massachusetts
September 6, 2007

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors
Northeast Bancorp and Subsidiaries

We have audited the consolidated statement of financial condition of Northeast Bancorp and Subsidiaries (the Company) as of June 30, 2006, and the related consolidated statements of income, changes in stockholders' equity and cash flows for each of the two years in the period ended June 30, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Northeast Bancorp and Subsidiaries as of June 30, 2006, and the results of their operations and their cash flows for each of the two years in the period ended June 30, 2006, in conformity with U.S. generally accepted accounting principles.

	/s/ Baker Newman & Noyes
Portland, Maine	Baker Newman & Noyes
August 11, 2006	Limited Liability Company

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NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
June 30, 2007 and 2006

ASSETS

	2007	2006
Cash and due from banks	$ 9,065,330	$ 9,573,908
Interest-bearing deposits	1,676,391	1,099,813
Federal Home Loan Bank overnight deposits	-	1,430,000
Total cash and cash equivalents	10,741,721	12,103,721
Available-for-sale securities, at fair value	86,348,070	86,137,707
Loans held-for-sale	1,636,485	681,143
Loans receivable	425,571,418	435,662,529
Less allowance for loan losses	5,756,000	5,496,000
Net loans	419,815,418	430,166,529
Premises and equipment - net	7,545,430	7,315,881
Acquired assets - net	-	10,384
Accrued interest receivable	2,586,720	2,678,558
Federal Home Loan Bank stock, at cost	4,825,700	5,498,300
Federal Reserve Bank stock, at cost	471,500	459,500
Goodwill	2,880,803	407,897
Intangible assets, net of accumulated amortization of $2,681,148 in 2007 and $2,366,564 in 2006	4,110,081	1,919,665
Bank owned life insurance (BOLI)	9,844,584	8,895,326
Other assets	5,994,468	6,643,191
Total assets	$ 556,800,980	$ 562,917,802

NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
June 30, 2007 and 2006

LIABILITIES AND STOCKHOLDERS' EQUITY

	2007	2006
Liabilities:		
Deposits		
Demand	$ 36,332,604	$ 38,137,357
NOW	53,405,241	54,432,157
Money market	8,053,552	9,430,378
Regular savings	21,145,567	24,247,324
Brokered time deposits	22,546,163	51,859,091
Certificates of deposit under $100,000	154,972,970	152,681,352
Certificates of deposit $100,000 or more	68,097,680	64,505,718
Total deposits	364,553,777	395,293,377
Federal Home Loan Bank advances	93,016,698	75,888,598
Short-term borrowings	33,105,377	29,637,426
Junior subordinated debentures issued to affiliated trusts	16,496,000	16,496,000
Capital lease obligation	2,653,511	2,781,046
Other borrowings	2,292,163	57,129
Other liabilities	3,833,576	3,668,101
Total liabilities	515,951,102	523,821,677
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; 2,448,832 and 2,447,132 shares outstanding at June 30, 2007 and 2006, respectively	2,448,832	2,447,132
Additional paid-in capital	4,715,164	4,675,258
Retained earnings	35,600,428	34,596,204
Accumulated other comprehensive loss	(1,914,546)	(2,622,469)
Total stockholders' equity	40,849,878	39,096,125
Total liabilities and stockholders' equity	$ 556,800,980	$ 562,917,802

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

NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
Years Ended June 30, 2007, 2006 and 2005

	2007	2006	2005
Interest and dividend income:			
Interest and fees on loans	$ 31,366,547	$ 31,643,003	$ 29,618,984
Interest on Federal Home Loan Bank overnight deposits	152,805	93,017	52,912
Taxable interest on available-for-sale securities	3,154,072	2,947,224	2,568,558
Tax-exempt interest on available-for-sale securities	442,311	264,839	-
Dividends on available-for-sale securities	140,954	130,605	146,678
Dividends on Federal Home Loan Bank and Federal Reserve Bank stock	368,463	335,900	264,777
Other interest and dividend income	57,203	41,620	22,025
Total interest and dividend income	35,682,355	35,456,208	32,673,934
Interest expense:			
Deposits	13,490,173	11,152,306	8,624,798
Federal Home Loan Bank advances	3,819,550	3,482,655	3,850,815
Short-term borrowings	1,504,936	927,688	403,539
Junior subordinated debentures issued to affiliated trusts	1,080,538	1,063,681	1,087,696
Obligation under capital lease agreements	136,726	130,583	-
Other borrowings	65,075	3,693	-
Total interest expense	20,096,998	16,760,606	13,966,848
Net interest and dividend income before provision for loan losses	15,585,357	18,695,602	18,707,086
Provision for loan losses	989,158	1,226,413	1,301,600
Net interest and dividend income after provision for loan losses	14,596,199	17,469,189	17,405,486
Noninterest income:			
Fees and service charges on loans	79,885	97,630	100,858
Fees for other services to customers	1,042,648	1,114,081	1,067,116
Net securities gains	42,349	17,335	67,940
Loss on trading activities	-	-	(83)
Gain on sales of loans	869,255	308,777	233,027
Investment and insurance commissions	4,715,553	3,686,122	2,858,897
BOLI income	388,613	366,939	330,700
Other	806,524	1,003,997	492,724
Total noninterest income	7,944,827	6,594,881	5,151,179
Noninterest expense:			
Salaries and employee benefits	12,022,037	10,637,758	9,554,317
Occupancy expense	1,722,381	1,672,505	1,418,696
Equipment expense	1,531,276	1,440,238	1,110,108
Intangible assets amortization	314,584	241,028	249,701
Other	4,484,908	4,216,975	4,351,352

Total noninterest expense	20,075,186	18,208,504	16,684,174
Income before income taxes	2,465,840	5,855,566	5,872,491
Income tax expense	579,163	1,851,367	1,853,857
Net income	$ 1,886,677	$ 4,004,199	$ 4,018,634
Earnings per common share:			
Basic	$ 0.77	$ 1.61	$ 1.60
Diluted	$ 0.76	$ 1.59	$ 1.57

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

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NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
Years Ended June 30, 2007, 2006 and 2005

	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance at June 30, 2004	$ -	$ 2,525,416	$ 6,943,894	$ 28,380,678	$ (1,396,968)	$ 36,453,020
Net income	-	-	-	4,018,634	-	4,018,634
Other comprehensive income net of tax:						
Net unrealized losses on investments						
available-for-sale, net of reclassification						
adjustment	-	-	-	-	726,781	726,781
Total comprehensive income	-	-	-			4,745,415
Purchase of 43,609 shares of Company stock	-	(43,609)	(799,893)	-	-	(843,502)
Stock options exercised	-	37,875	385,410	-	-	423,285
Stock grant	-	150	1,425	-	-	1,575
Dividends on common stock at $0.36 per share	-	-	-	(910,220)	-	(910,220)
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 losses 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 connection with the purchase of branch real estate	-	5,000	98,000	-	-	103,000
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

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

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NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended June 30, 2007, 2006 and 2005

	2007	2006	2005
Cash flows from operating activities:			
Net income	$ 1,886,677	$ 4,004,199	$ 4,018,634
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	989,158	1,226,413	1,301,600
Provision for losses on acquired assets	6,384	2,500	20,000
Provision made for deferred compensation	276,539	399,845	98,000
Write-down of available-for-sale securities	50,442	38,394	27,849
Write-down of non-marketable securities	248,482	42,257	96,931
Deferred income tax benefit	(329,268)	(323,220)	(197,522)
BOLI income, net	(349,258)	(366,939)	(274,347)
Depreciation of premises and equipment	1,088,373	1,048,529	711,339
Amortization of intangible assets	314,584	241,028	249,701
Net gain on sale of available-for-sale securities	(42,349)	(17,335)	(67,940)
Net (gain) loss on disposals, writedowns and sale of fixed assets	(73,962)	128,363	(59,719)
Gain on sale of deposits	-	(500,845)	-
Net change of loans held-for-sale	(955,342)	(362,293)	226,872
Other	27,839	21,962	(350,028)
Change in other assets and liabilities:			
Interest receivable	91,838	(123,669)	(361,720)
Other assets and liabilities	28,754	106,976	631,272
Net cash provided by operating activities	3,258,891	5,566,165	6,070,922
Cash flows from investing activities:			
Federal Reserve Bank stock purchased	(12,000)	(54,000)	(405,500)
Proceeds from redemption of Federal Home Loan Bank stock	672,600	1,146,200	-
Proceeds from the sales of available-for-sale securities	2,290,571	1,354,098	1,126,131
Purchases of available-for-sale securities	(14,720,181)	(25,311,089)	(22,862,781)
Proceeds from maturities and principal payments on available-for-sale securities	13,255,927	9,078,452	15,859,638
Net decrease (increase) in loans	9,361,953	24,729,918	(29,502,226)
Purchases of premises and equipment	(1,373,474)	(1,111,469)	(1,241,683)
Proceeds from sales of premises and equipment	246,610	-	481,794
Proceeds from sales of acquired assets	4,000	244,722	497,507
Other	-	-	(75,492)
Purchase of retirement annuity	-	-	(900,000)
Purchase of BOLI	(600,000)	-	(529,184)
Cash paid in connection with acquisition of insurance agencies	(2,450,000)	-	(993,469)
Net cash provided (used) by investing activities	6,676,006	10,076,832	(38,545,265)
Cash flows from financing activities:			
Net (decrease) increase in deposits	(30,739,600)	7,267,169	18,398,993
Cash paid on sale of deposits	-	(7,691,669)	-

Advances from the Federal Home Loan Bank	43,000,000	105,000,000	33,000,000
Repayment of advances from the Federal Home Loan Bank	(36,831,900)	(115,309,004)	(24,403,032)
Net advances (repayments) on Federal Home Loan Bank overnight advances	10,960,000	-	(5,377,000)
Net increase (decrease) in short-term borrowings	3,467,951	(3,741,986)	8,494,543
Dividends paid	(882,453)	(897,087)	(910,220)
Company stock purchased	(67,944)	(2,142,250)	(698,812)
Issuance of common stock	6,550	213,972	280,170
Proceeds from issuance of junior subordinated debentures	-	-	10,310,000
Repayment of junior subordinated debentures	-	-	(7,394,849)
Repayment on debt from insurance agencies acquisitions	(81,966)	-	-
Repayment on capital lease obligation	(127,535)	(111,656)	-
Net cash (used) provided by financing activities	(11,296,897)	(17,412,511)	31,699,793
Net decrease in cash and cash equivalents	(1,362,000)	(1,769,514)	(774,550)
Cash and cash equivalents, beginning of year	12,103,721	13,873,235	14,647,785
Cash and cash equivalents, end of year	$ 10,741,721	$ 12,103,721	$ 13,873,235
Supplemental schedule of cash flow information:			
Interest paid	$ 20,120,234	$ 16,872,352	$ 13,214,688
Income taxes paid	819,500	2,220,561	2,017,222
Supplemental schedule of noncash investing and financing activities:			
Transfer from loans to acquired assets	$ -	$ 173,800	$ 570,339
Stock tendered in cashless stock option exercise	-	-	144,690
Change in valuation allowance for unrealized losses (gains) on available-for-sale securities, net of tax	707,923	1,952,282	(726,781)
Net change in deferred taxes for unrealized losses (gains) on available-for-sale securities	364,689	1,005,701	(374,404)
Transfer from loan loss allowance to other liabilities for off balance sheet credit risk	-	204,086	-
Capital lease asset and related obligation	-	2,892,702	-
Stock issued in branch purchase	103,000	-	-

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, 2007, 2006 and 2005

1. Summary of Significant Accounting Policies

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

Business

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 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 (the Bank), a Maine state-chartered universal bank. Effective August, 2004, the Bank converted its charter to a state bank from a charter as a federal savings and loan association and became 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 vigorous 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 December 2003, the Financial Accounting Standards Board (FASB) issued a revised FASB Interpretation No. 46, *Consolidation of Variable Interest Entities* ("FIN 46R") which, in part, specifically addresses limited purpose trusts formed to issue trust preferred securities. FIN 46R establishes the criteria used to identify variable interest entities and to determine whether or not to consolidate a variable interest entity. 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, NBN Capital Trust II and NBN Capital Trust III. 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 statement of financial condition 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, NBN Capital Trust II and NBN Capital Trust III 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, 2007 and 2006, the reserve balance was approximately $250,000 and $230,000, 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.

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, 2007 and 2006. 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, 2007 and 2006 was approximately $202,000 and $303,000, 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 which 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 five to eighteen years. The weighted average amortization period for intangibles subject to amortization is 12.55 years. 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 estimated aggregate amortization expense for each of the five succeeding fiscal years is as follows: 2008 - $389,287; 2009 - $352,943; 2010 - $345,703; 2011 - $345,703 and 2012 - $345,703.

Advertising Expense

Advertising costs are expensed as incurred. Advertising costs were approximately $440,000, $492,000 and $336,000 for the years ended June 30, 2007, 2006 and 2005, respectively.

Stock-Based Compensation

The Company has stock-based employee compensation plans, which are described more fully in note 14. 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 2007 and 2006 and since all previously granted options were fully vested at the grant date, adoption of SFAS 123-R had no impact on the 2007 and 2006 financial statements.

The following table illustrates the effect on net income and earnings per share as if the Company had applied the fair value recognition provisions of SFAS 123-R to stock-based employee compensation.

	Years Ended June 30, 2007	2006	2005
Net income, as reported	$ 1,886,677	$ 4,004,199	$ 4,018,634
Deduct: total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	-	-	1,513
Pro forma net income	$ 1,886,677	$ 4,004,199	$ 4,017,121
Earnings per share:			
Basic - as reported	$ .77	$ 1.61	$ 1.60
Basic - pro forma	$ .77	$ 1.61	$ 1.59
Diluted - as reported	$ .76	$ 1.59	$ 1.57
Diluted - pro forma	$ .76	$ 1.59	$ 1.57

The following table presents the weighted average fair value and related assumptions using the Black-Scholes option-pricing model for all stock options granted during the periods indicated. There were no stock options granted in fiscal 2007 and 2006.

	2007	2006	2005
Weighted average fair value	$ -	$ -	$ 1,513
Dividend yield	-	-	2.8%
Expected volatility	-	-	24.3%
Risk-free interest rates	-	-	4.5%
Expected lives	-	-	8 years

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 has only limited involvement with derivative financial instruments and they are used for trading and hedging purposes. The derivative financial instruments used by the Company are covered call and put contracts on its equity securities portfolio and certain residential mortgage loan commitments for resale into the secondary market. The total value of securities under call and put contracts and commitments to originate residential mortgage loans for resale at June 30, 2007, 2006 and 2005, 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.

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, 2007, total assets held in trust for customers, for which the Company has fiduciary responsibility, amounted to approximately $97,329,000.

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 February 2006, the FASB issued SFAS No. 155, *Accounting for Certain Hybrid Instruments* (SFAS 155), which permits, but does not require, fair value accounting for any hybrid financial instrument that contains an embedded derivative that would otherwise require bifurcation in accordance with SFAS 133. The statement also subjects beneficial interests issued by securitization vehicles to the requirements of SFAS No. 133. The statement is effective as of July 1, 2007. The adoption of SFAS 155 is not expected to have a material impact on the Company’s financial condition and results of operations.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets - an amendment of FASB Statement No. 140* (SFAS 156). SFAS 156 requires an entity to recognize a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in specific situations. Additionally, the servicing asset or servicing liability shall be initially measured at fair value; however, an entity may elect the "amortization method" or "fair value method" for subsequent balance sheet reporting periods. SFAS 156 is effective as of an entity's first fiscal year beginning after September 15, 2006. Early adoption is permitted as of the beginning of an entity's fiscal year, provided the entity has not yet issued financial statements, including interim financial statements, for any period of that fiscal year. The Company does not expect the adoption of this statement to have a material impact on its financial condition, results of operations or cash flows.

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.

2. Available-for-sale securities

A summary of the cost and approximate fair values of available-for-sale securities at June 30, 2007 and 2006 follows:

	2007		2006	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Debt securities issued by U.S. Government-sponsored enterprises	$ 21,765,732	$ 21,158,409	$ 25,766,682	$ 24,694,409
Mortgage-backed securities	53,987,824	52,138,732	50,618,118	48,126,031
Municipal bonds	11,067,197	10,709,069	11,075,274	10,770,167
Corporate bonds	500,000	484,625	500,000	477,520
Equity securities	1,928,144	1,857,235	2,151,072	2,069,580
	$ 89,248,897	$ 86,348,070	$ 90,111,146	$ 86,137,707

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

	2007		2006	
	Gross Unrealized Gains	Gross Unrealized Losses	Gross Unrealized Gains	Gross Unrealized Losses
Debt securities issued by U. S. Government-sponsored enterprises	$ -	$ 607,323	$ -	$ 1,072,273
Mortgage-backed securities	2,818	1,851,910	2,289	2,494,376
Municipal bonds	-	358,128	-	305,107
Corporate bonds	-	15,375	-	22,480
Equity securities	18,661	89,570	22,809	104,301
	$ 21,479	$ 2,922,306	$ 25,098	$ 3,998,537

At June 30, 2007, mortgage-backed and U.S. Government-sponsored enterprise securities with a fair value of approximately $70,934,000 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, 2007.

Less than 12 Months	More than 12 Months	Total

	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
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			