AMERICAN RIVER BANKSHARES
Form 10-K
March 06, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2007

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

For the transition period from __________________________ to _____________________

Commission File No. **0-31525**

AMERICAN RIVER BANKSHARES

(Exact name of registrant as specified in its charter)

California	**68-0352144**
State or other jurisdiction of incorporation or organization	(IRS Employer Identification Number)

3100 Zinfandel Drive, Rancho Cordova, California	**95670**
(Address of principal executive offices)	(Zip code)

Registrant s telephone number, including area code **916-851-0123**

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

Title of Each Class	Name of Each Exchange On Which Registered
Common Stock, no par value	NASDAQ Global Select Market

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 o 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 o 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 o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of the 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, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer o	Accelerated filer x
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant s most recently completed second fiscal quarter. $117,645,000.

Indicate the number of shares outstanding of each of the registrant s classes of common stock, as of the latest practicable date.

As of March 5, 2008, the registrant s no par value Common Stock totaled 5,540,002 shares outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

The following documents are incorporated by reference into this Form 10-K: Part III, Items 10 through 14 from Registrant s definitive proxy statement for the 2008 annual meeting of shareholders.

AMERICAN RIVER BANKSHARES

INDEX TO
ANNUAL REPORT ON FORM 10-K
FOR YEAR ENDED DECEMBER 31, 2007

PART I

Item 1. Business.

Cautionary Statements Regarding Forward-Looking Statements

Certain matters discussed or incorporated by reference in this Annual Report on Form 10-K including, but not limited to, matters described in Item 7 - Management s Discussion and Analysis of Financial Condition and Results of Operations, are forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, Section 27A of the Securities Act of 1933, as amended, and subject to the safe-harbor provisions of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements may contain words related to future projections including, but not limited to, words such as believe, expect, anticipate, intend, may, will, should, would, and variations of those words and similar words that are subject to risks, uncertainties and other factors that could cause actual results to differ materially from those projected. Factors that could cause or contribute to such differences include, but are not limited to, the following: (1) variances in the actual versus projected growth in assets; (2) return on assets; (3) loan and lease losses; (4) expenses; (5) changes in the interest rate environment including interest rates charged on loans, earned on securities investments and paid on deposits; (6) competition effects; (7) fee and other noninterest income earned; (8) general economic conditions nationally, regionally, and in the operating market areas of the Company and its subsidiaries; (9) changes in the regulatory environment; (10) changes in business conditions and inflation; (11) changes in securities markets; (12) data processing problems; (13) a decline in real estate values in the Company s operating market areas; (14) the effects of terrorism, the threat of terrorism or the impact of the current military conflicts in Afghanistan and Iraq and the conduct of the war on terrorism by the United States and its allies, as well as other factors. The factors set forth under Item 1A - Risk Factors in this report and other cautionary statements and information set forth in this report should be carefully considered and understood as being applicable to all related forward-looking statements contained in this report, when evaluating the business prospects of the Company and its subsidiaries.

Forward-looking statements are not guarantees of performance. By their nature, they involve risks, uncertainties and assumptions. The future results and shareholder values may differ significantly from those expressed in these forward-looking statements. You are cautioned not to put undue reliance on any forward-looking statement. Any such statement speaks only as of the date of this report, and in the case of any documents that may be incorporated by reference, as of the date of those documents. We do not undertake any obligation to update or release any revisions to any forward-looking statements, to report any new information, future event or other circumstances after the date of this report or to reflect the occurrence of unanticipated events, except as required by law. However, your attention is directed to any further disclosures made on related subjects in our subsequent reports filed with the Securities and Exchange Commission (the SEC) on Forms 10-K, 10-Q and 8-K.

Introduction

American River Bankshares (the Company) is a bank holding company registered under the Bank Holding Company Act of 1956, as amended. The Company was incorporated under the laws of the State of California in 1995. As a bank holding company, the Company is authorized to engage in the activities permitted under the Bank Holding Company Act of 1956, as amended, and regulations thereunder. Its principal office is located at 3100 Zinfandel Drive, Suite 450, Rancho Cordova, California 95670 and its telephone number is (916) 851-0123.

The Company owns 100% of the issued and outstanding common shares of its banking subsidiary, American River Bank, and American River Financial, a California corporation which has been inactive since its incorporation in 2003.

American River Bank was incorporated and commenced business in Fair Oaks, California, in 1983 and thereafter moved its headquarters to Sacramento, California in 1985. American River Bank operates five full service offices and one convenience office in Sacramento and Placer Counties including the main office located at 1545 River Park Drive, Suite 107, Sacramento and branch offices located at 520 Capitol Mall, Suite 100, Sacramento; 9750 Business Park Drive, Sacramento; 10123 Fair Oaks Boulevard, Fair Oaks and 2240 Douglas Boulevard, Roseville. The convenience office (limited service office) is located at 3100 Zinfandel Drive, Suite 450, Rancho Cordova. American River Bank also operatesthree full service offices in Sonoma County located at 412 Center Street, Healdsburg; 8733 Lakewood Drive, Windsor and 50 Santa Rosa Avenue, Suite 100, Santa Rosa, operated under the name North Coast Bank, a division of American River Bank. North Coast Bank was incorporated and commenced business in 1990 as Windsor Oaks National Bank in Windsor, California. In 1997, the name was changed to North Coast Bank. In 2000, North Coast Bank was acquired by the Company as a separate bank subsidiary. Effective December 31, 2003, North Coast Bank was merged with and into American River Bank.

On December 3, 2004, the Company acquired Bank of Amador located in Jackson, California. Bank of Amador was merged with and into American River Bank and now operates three full service banking offices as Bank of Amador, a division of American River Bank within its primary service area of Amador County, in the cities of Jackson, Pioneer and Ione.

American River Bank s deposits are insured by the Federal Deposit Insurance Corporation (FDIC) up to applicable legal limits. American River Bank does not offer trust services or international banking services and does not plan to do so in the near future. American River Bank s primary business is serving the commercial banking needs of small to mid-sized businesses within those counties listed above. American River Bank accepts checking and savings deposits, offers money market deposit accounts and certificates of deposit, makes secured and unsecured commercial, secured real estate, and other installment and term loans and offers other customary banking services. American River Bank also conducts lease financing for most types of business equipment, from computer software to heavy earth-moving equipment.

American River Bank owns 100% of two inactive companies, ARBCO and American River Mortgage. ARBCO was formed in 1984 to conduct real estate development and has been inactive since 1995. American River Mortgage has been inactive since its formation in 1994.

During 2007, the Company conducted no significant activities other than holding the shares of its subsidiaries. However, it is authorized, with the prior approval of the Board of Governors of the Federal Reserve System (the Board of Governors), the Company s principal regulator, to engage in a variety of activities which are deemed closely related to the business of banking.

The common stock of the Company is registered under the Securities Exchange Act of 1934, as amended, and is listed and traded on the Nasdaq Global Select Market under the symbol AMRB.

At December 31, 2007, the Company had consolidated assets of $574 million, deposits of $456 million and shareholders equity of $60 million.

General

The Company is a community-oriented bank holding company headquartered in Sacramento, California. The principal communities served are located in Sacramento, Placer, Yolo, El Dorado, Sonoma, and Amador counties. The Company generates most of its revenue by providing a wide range of products and services to small and middle-market businesses and individuals. The Company s principal source of revenue comes from interest income. Interest income is derived from: (i) interest and fees on loans and leases; (ii) interest on investments (principally government securities); and (iii) interest on Federal funds sold (funds loaned on a short-term basis to other banks). For the year ended December 31, 2007, these sources comprised 84.1%, 15.8%, and 0.1%, respectively, of the Company s interest income.

American River Bank s deposits are not received from a single depositor or group of affiliated depositors, the loss of any one of which would have a materially adverse effect on the business of the Company. A material portion of American River Bank s deposits are not concentrated within a single industry or group of related industries.

As of December 31, 2007 and December 31, 2006, American River Bank held $21,500,000 and $16,500,000, respectively, in certificates of deposit for the State of California. In connection with these deposits, American River Bank is generally required to pledge securities to secure such deposits, except for the first $100,000, which are insured by the FDIC.

American River Bank competes with approximately 41 other banking or savings institutions in Sacramento County and 35 in Placer County. American River Bank s market share of FDIC insured deposits in the service areas of Sacramento County and Placer County was approximately 1.3% in each year (based upon the most recent information made available by the FDIC through June 30, 2007). North Coast Bank, a division of American River Bank, competes with approximately 23 other banking or savings institutions in its service areas and its market share of FDIC insured deposits in the service area of Sonoma County was approximately ..7% (based upon the most recent information made available by the FDIC through June 30, 2007). Bank of Amador, a division of American River Bank competes with approximately 7 other banking or savings institutions in its service areas and its market share of FDIC insured deposits in the service area of Amador County was approximately 15.7% (based upon the most recent information made available by the FDIC through June 30, 2007).

Employees

At December 31, 2007, the Company and its subsidiaries employed 124 persons on a full-time equivalent basis. The Company believes its employee relations are good.

Website Access

The Company maintains a website where certain information about the Company is posted. Through the website, its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments thereto, as well as Section 16 Reports and amendments thereto, are available as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC. These reports are free of charge and can be accessed through the address www.amrb.com by selecting the *SEC Filings* link located at that address. Once you have selected the *SEC Filings* link you will have the option to access the Section 16 Reports or the reports filed on Forms 10-K, 10-Q and 8-K by the Company by selecting the appropriate link.

Supervision and Regulation

General

The common stock of the Company is subject to the registration requirements of the Securities Act of 1933, as amended, and the qualification requirements of the California Corporate Securities Law of 1968, as amended. The Company is also subject to the periodic reporting requirements of Section 13 of the Securities Exchange Act of 1934, as amended, which include, but are not limited to, annual, quarterly and other current reports with the SEC.

American River Bank is licensed by the California Commissioner of Financial Institutions (the Commissioner), its deposits are insured by the FDIC up to the applicable legal limits, and it has chosen not to become a member of the Federal Reserve System. Consequently, American River Bank is subject to the supervision of, and is regularly examined by, the Commissioner and the FDIC. The supervision and regulation includes comprehensive reviews of all major aspects of American River Bank s business and condition, including its capital ratios, allowance for possible loan and lease losses and other factors. However, no inference should be drawn that such authorities have approved any such factors. American River Bankshares and American River Bank are required to file reports with the Board of Governors, the Commissioner, and the FDIC and provide the additional information that the Board of Governors, the Commissioner, and the FDIC may require.

American River Bankshares is a bank holding company within the meaning of the Bank Holding Company Act of 1956, as amended (the Bank Holding Company Act), and is registered as such with, and subject to the supervision of, the Board of Governors. The Company is required to obtain the approval of the Board of Governors before it may acquire all or substantially all of the assets of any bank, or ownership or control of the voting shares of any bank if, after giving effect to such acquisition of shares, the Company would own or control more than 5% of the voting shares of such bank. The Bank Holding Company Act prohibits the Company from acquiring any voting shares of, or interest in, all or substantially all of the assets of, a bank located outside the State of California unless such an acquisition is specifically authorized by the laws of the state in which such bank is located. Any such interstate acquisition is also subject to the California law implementing certain provisions of prior federal law.

The Company, and any subsidiaries which it may acquire or organize, are deemed to be affiliates within the meaning of that term as defined in the Federal Reserve Act. This means, for example, that there are limitations (a) on loans by American River Bank to affiliates, and (b) on investments by American River Bank in affiliates stock as collateral for loans to any borrower. The Company and its subsidiaries are also subject to certain restrictions with respect to engaging in the underwriting, public sale and distribution of securities.

In addition, regulations of the Board of Governors under the Federal Reserve Act require that reserves be maintained by American River Bank in conjunction with any liability of the Company under any obligation (promissory note, acknowledgement of advance, banker s acceptance or similar obligation) with a weighted average maturity of less than seven (7) years to the extent that the proceeds of such obligations are used for the purpose of supplying funds to American River Bank for use in its banking business, or to maintain the availability of such funds.

Capital Standards

The Board of Governors and the FDIC have adopted risk-based capital guidelines for evaluating the capital adequacy of bank holding companies and banks. The guidelines are designed to make capital requirements sensitive to differences in risk profiles among banking organizations, to take into account off-balance sheet exposures and to aid in making the definition of bank capital uniform internationally. Under the guidelines, American River Bankshares and American River Bank are required to maintain capital equal to at least 8.0% of its assets and commitments to extend credit, weighted by risk, of which at least 4.0% must consist primarily of common equity (including retained earnings) and the remainder may consist of subordinated debt, cumulative preferred stock, or a limited amount of loan and lease loss reserves.

Assets, commitments to extend credit, and off-balance sheet items are categorized according to risk and certain assets considered to present less risk than others permit maintenance of capital at less than the 8% ratio. For example, most home mortgage loans are placed in a 50% risk category and therefore require maintenance of capital equal to 4% of those loans, while commercial loans are placed in a 100% risk category and therefore require maintenance of capital equal to 8% of those loans.

Under the risk-based capital guidelines, assets reported on an institution s balance sheet and certain off-balance sheet items are assigned to risk categories, each of which has an assigned risk weight. Capital ratios are calculated by dividing the institution s qualifying capital by its period-end risk-weighted assets. The guidelines establish two categories of qualifying capital: Tier 1 capital (defined to include common shareholders equity and noncumulative perpetual preferred stock) and Tier 2 capital which includes, among other items, limited life (and in the case of banks, cumulative) preferred stock, mandatory convertible securities, subordinated debt and a limited amount of reserve for credit losses. Tier 2 capital may also include up to 45% of the pretax net unrealized gains on certain available-for-sale equity securities having readily determinable fair values (i.e., the excess, if any, of fair market value over the book value or historical cost of the investment security). The federal regulatory agencies reserve the right to exclude all or a portion of the unrealized gains upon a determination that the equity securities are not prudently valued. Unrealized gains and losses on other types of assets, such as bank premises and available-for-sale debt securities, are not included in Tier 2 capital, but may be taken into account in the evaluation of overall capital adequacy and net unrealized losses on available-for-sale equity securities will continue to be deducted from Tier 1 capital as a cushion against risk. Each institution is required to maintain a minimum risk-based capital ratio (including Tier 1 and Tier 2 capital) of 8%, of which at least half must be Tier 1 capital.

A leverage capital standard was adopted as a supplement to the risk-weighted capital guidelines. Under the leverage capital standard, an institution is required to maintain a minimum ratio of Tier 1 capital to the sum of its quarterly average total assets and quarterly average reserve for loan losses, less intangible assets not included in Tier 1 capital. Period-end assets may be used in place of quarterly average total assets on a case-by-case basis. The Board of Governors and the FDIC have also adopted a minimum leverage ratio for bank holding companies as a supplement to the risk-weighted capital guidelines. The leverage ratio establishes a minimum Tier 1 ratio of 3% (Tier 1 capital to total assets) for the highest rated bank holding companies or those that have implemented the risk-based capital market risk measure. All other bank holding companies must maintain a minimum Tier 1 leverage ratio of 4% with higher leverage capital ratios required for bank holding companies that have significant financial and/or operational weakness, a high risk profile, or are undergoing or anticipating rapid growth.

At December 31, 2007, American River Bankshares and American River Bank were in compliance with the risk-weighted capital and leverage ratio guidelines.

Prompt Corrective Action

The Board of Governors and the FDIC have adopted regulations implementing a system of prompt corrective action pursuant to Section 38 of the Federal Deposit Insurance Act and Section 131 of the FDIC Improvement Act of 1991 (FDICIA). The regulations establish five capital categories with the following characteristics: (1) Well capitalized - consisting of institutions with a total risk-based capital ratio of 10% or greater, a Tier 1 risk-based capital ratio of 6% or greater and a leverage ratio of 5% or greater, and the institution is not subject to an order, written agreement, capital directive or prompt corrective action directive; (2) Adequately capitalized - consisting of institutions with a total risk-based capital ratio of 8% or greater, a Tier 1 risk-based capital ratio of 4% or greater and a leverage ratio of 4% or greater, and the institution does not meet the definition of a well capitalized institution; (3) Undercapitalized - consisting of institutions with a total risk-based capital ratio less than 8%, a Tier 1 risk-based capital ratio of less than 4%, or a leverage ratio of less than 4%; (4) Significantly undercapitalized - consisting of institutions with a total risk-based capital ratio of less than 6%, a Tier 1 risk-based capital ratio of less than 3%, or a leverage ratio of less than 3%; (5) Critically undercapitalized - consisting of an institution with a ratio of tangible equity to total assets that is equal to or less than 2%.

The regulations established procedures for classification of financial institutions within the capital categories, filing and reviewing capital restoration plans required under the regulations and procedures for issuance of directives by the appropriate regulatory agency, among other matters. The regulations impose restrictions upon all institutions to refrain from certain actions which would cause an institution to be classified within any one of the three undercapitalized categories, such as declaration of dividends or other capital distributions or payment of management fees, if following the distribution or payment the institution would be classified within one of the undercapitalized categories. In addition, institutions which are classified in one of the three undercapitalized categories are subject to certain mandatory and discretionary supervisory actions. Mandatory supervisory actions include (1) increased monitoring and review by the appropriate federal banking agency; (2) implementation of a capital restoration plan; (3) total asset growth restrictions; and (4) limitations upon acquisitions, branch expansion, and new business activities without prior approval of the appropriate federal banking agency. Discretionary supervisory actions may include (1) requirements to augment capital; (2) restrictions upon affiliate transactions; (3) restrictions upon deposit gathering activities and interest rates paid; (4) replacement of senior executive officers and directors; (5) restrictions upon activities of the institution and its affiliates; (6) requiring divestiture or sale of the institution; and (7) any other supervisory action that the appropriate federal banking agency determines is necessary to further the purposes of the regulations. Further, the federal banking agencies may not accept a capital restoration plan without determining, among other things, that the plan is based on realistic assumptions and is likely to succeed in restoring the depository institution s capital. In addition, for a capital restoration plan to be acceptable, the depository institution s parent holding company must guarantee that the institution will comply with such capital restoration plan. The aggregate liability of the parent holding company under the guaranty is limited to the lesser of (i) an amount equal to 5 percent of the depository institution s total assets at the time it became undercapitalized, and (ii) the amount that is necessary (or would have been necessary) to bring the institution into compliance with all capital standards applicable with respect to such institution as of the time it fails to comply with the plan. If a depository institution fails to submit an acceptable plan, it is treated as if it were significantly undercapitalized. FDICIA also restricts the solicitation and acceptance of and interest rates payable on brokered deposits by insured depository institutions that are not well capitalized. An undercapitalized institution is not allowed to solicit deposits by offering rates of interest that are significantly higher than the prevailing rates of interest on insured deposits in the particular institution s normal market areas or in the market areas in which such deposits would otherwise be accepted.

Any financial institution which is classified as critically undercapitalized must be placed in conservatorship or receivership within 90 days of such determination unless it is also determined that some other course of action would better serve the purposes of the regulations. Critically undercapitalized institutions are also prohibited from making (but not accruing) any payment of principal or interest on subordinated debt without prior regulatory approval and regulators must prohibit a critically undercapitalized institution from taking certain other actions without prior approval, including (1) entering into any material transaction other than in the usual course of business, including investment expansion, acquisition, sale of assets or other similar actions; (2) extending credit for any highly leveraged transaction; (3) amending articles or bylaws unless required to do so to comply with any law, regulation or order; (4) making any material change in accounting methods; (5) engaging in certain affiliate transactions; (6) paying excessive compensation or bonuses; and (7) paying interest on new or renewed liabilities at rates which would increase the weighted average costs of funds beyond prevailing rates in the institution s normal market areas.

Additional Regulations

Under the FDICIA, the federal financial institution agencies have adopted regulations which require institutions to establish and maintain comprehensive written real estate policies which address certain lending considerations, including loan-to-value limits, loan administrative policies, portfolio diversification standards, and documentation, approval and reporting requirements. The FDICIA further generally prohibits an insured state bank from engaging as a principal in any activity that is impermissible for a national bank, absent FDIC determination that the activity would not pose a significant risk to the Bank Insurance Fund, and that the bank is, and will continue to be, within applicable capital standards.

The Federal Financial Institution Examination Counsel (FFIEC) utilizes the Uniform Financial Institutions Rating System (UFIRS) commonly referred to as CAMELS to classify and evaluate the soundness of financial institutions. Bank examiners use the CAMELS measurements to evaluate capital adequacy, asset quality, management, earnings, liquidity and sensitivity to market risk. Effective January 1, 2005, bank holding companies such as the Company, were subject to evaluation and examination under a revised bank holding company rating system. The so-called BOPEC rating system implemented in 1979 was primarily focused on financial condition, consolidated capital and consolidated earnings. The rating system reflects the change toward analysis of risk management (as reflected in bank examination under the CAMELS measurements), in addition to financial factors and the potential impact of nondepository subsidiaries upon depository institution subsidiaries.

The federal financial institution agencies have established bases for analysis and standards for assessing a financial institution s capital adequacy in conjunction with the risk-based capital guidelines including analysis of interest rate risk, concentrations of credit risk, risk posed by non-traditional activities, and factors affecting overall safety and soundness. The safety and soundness standards for insured financial institutions include analysis of (1) internal controls, information systems and internal audit systems; (2) loan documentation; (3) credit underwriting; (4) interest rate exposure; (5) asset growth; (6) compensation, fees and benefits; and (7) excessive compensation for executive officers, directors or principal shareholders which could lead to material financial loss. If an agency determines that an institution fails to meet any standard, the agency may require the financial institution to submit to the agency an acceptable plan to achieve compliance with the standard. If the agency requires submission of a compliance plan and the institution fails to timely submit an acceptable plan or to implement an accepted plan, the agency must require the institution to correct the deficiency. The agencies may elect to initiate enforcement action in certain cases rather than rely on an existing plan particularly where failure to meet one or more of the standards could threaten the safe and sound operation of the institution.

Community Reinvestment Act (CRA) regulations evaluate banks lending to low and moderate income individuals and businesses across a four-point scale from outstanding to substantial noncompliance, and are a factor in regulatory review of applications to merge, establish new branches or form bank holding companies. In addition, any bank rated in substantial noncompliance with the CRA regulations may be subject to enforcement proceedings. In its most recent exam for CRA compliance, American River Bank has a rating of satisfactory.

Limitations on Dividends

The Company s ability to pay cash dividends is subject to restrictions set forth in the California General Corporation Law. Funds for payment of any cash dividends by the Company would be obtained from its investments as well as dividends and/or management fees from its subsidiaries. The payment of cash dividends and/or management fees by American River Bank is subject to restrictions set forth in the California Financial Code, as well as restrictions established by the FDIC. See Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities for more information regarding cash dividends.

Competition

Competitive Data

American River Bank. At June 30, 2007, based on the most recent Data Book Summary of Deposits in FDIC Insured Commercial and Savings Banks report at that date, the competing commercial and savings banks had 190 offices in the cities of Fair Oaks, Rancho Cordova, Roseville and Sacramento, California, where American River Bank has its 6 Sacramento area offices, 64 offices in the cities of Healdsburg, Santa Rosa and Windsor, California, where American River Bank has its 3 Sonoma County offices, and 4 offices in the cities of Jackson, Pioneer and Ione, California, where American River Bank has its 3 Amador County offices. Additionally, American River Bank competes with thrifts and, to a lesser extent, credit unions, finance companies and other financial service providers for deposit and loan customers.

Larger banks may have a competitive advantage because of higher lending limits and major advertising and marketing campaigns. They also perform services, such as trust services, international banking, discount brokerage and insurance services, which American River Bank is not authorized nor prepared to offer currently. American River Bank has made arrangements with its correspondent banks and with others to provide some of these services for its customers. For borrowers requiring loans in excess of American River Bank s legal lending limits, American River Bank has offered, and intends to offer in the future, such loans on a participating basis with its correspondent banks and with other community banks, retaining the portion of such loans which is within its lending limits. As of December 31, 2007, American River Bank s aggregate legal lending limits to a single borrower and such borrower s related parties were $9,932,000 on an unsecured basis and $16,554,000 on a fully secured basis based on capital and allowable reserves of $66,214,000.

American River Bank s business is concentrated in its service area, which primarily encompasses Sacramento County, South Western Placer County, Sonoma County, and Amador County. The economy of American River Bank s service area is dependent upon government, manufacturing, tourism, retail sales, agriculture, population growth and smaller service oriented businesses.

Based upon the most recent Data Book Summary of Deposits in FDIC Insured Commercial and Savings Banks report dated June 30, 2007, there were 232 operating commercial and savings bank offices in Sacramento County with total deposits of $18,295,666,000. This was a decrease of $455,513,000 over the June 30, 2006 balances. American River Bank held a total of $240,855,000 in deposits, representing approximately 1.3% of total commercial and savings banks deposits in Sacramento County as of June 30, 2007.

Based upon the most recent Data Book Summary of Deposits in FDIC Insured Commercial and Savings Banks report dated June 30, 2007, there were 117 operating commercial and savings bank offices in Placer County with total deposits of $5,719,602,000. This was an increase of $357,972,000 over the June 30, 2006 balances. American River Bank held a total of $72,726,000 in deposits, representing approximately 1.3% of total commercial and savings banks deposits in Placer County as of June 30, 2007.

Based upon the most recent Data Book Summary of Deposits in FDIC Insured Commercial and Savings Banks report dated June 30, 2007, there were 131 operating commercial and savings bank offices in Sonoma County with total deposits of $9,461,232,000. This was an increase of $442,037,000 over the June 30, 2006 balances. American River Bank held a total of $68,870,000 in deposits, representing approximately 0.7% of total commercial and savings banks deposits in Sonoma County as of June 30, 2007.

Based upon the most recent Data Book Summary of Deposits in FDIC Insured Commercial and Savings Banks report dated June 30, 2007, there were 13 operating commercial and savings bank offices in Amador County with total deposits of $636,995,000. This was an increase of $6,468,000 over the June 30, 2006 balances. American River Bank held a total of $99,677,000 in deposits, representing approximately 15.7% of total commercial and savings banks deposits in Amador County as of June 30, 2007.

In 1996, pursuant to Congressional mandate, the FDIC reduced bank deposit insurance assessment rates to a range from $0 to $0.27 per $100 of deposits, dependent upon a bank s risk. In 2005, Congress adopted the Federal Deposit Insurance Reform Act of 2005 (the Reform Act), which had the effect of merging the Bank Insurance Fund and the Savings Association Insurance Fund into a new Deposit Insurance Fund (DIF). The FDIC released final regulations under the Reform Act on November 2, 2006 that established a revised risk-based deposit insurance assessment rate system for members of the DIF to insure, among other matters, that there will be sufficient assessment income for repayment of DIF obligations and to further refine the differentiation of risk profiles among institutions as a basis for assessments. Under the new assessment rate system, the FDIC set the assessment rates that became effective January 1, 2007 for most institutions from $0.05 to $0.07 per $100 of insured deposits and established a Designated Reserve Ratio (DRR) for the DIF during 2007 of 1.25% of insured deposits.

The new assessment rate system consolidates the nine categories of the prior assessment system into four categories (Risk Categories I, II, III and IV) and three Supervisory Groups (A, B and C) based upon institution s capital levels and supervisory ratings. Risk Category I includes all well capitalized institutions with the highest supervisory ratings. Risk Category II includes adequately capitalized institutions that are assigned to Supervisory Groups A and B. Risk Category III includes all undercapitalized institutions that are assigned to Supervisory Groups A and B and institutions assigned to Supervisory Group C that are not undercapitalized but have a low supervisory rating. Risk Category IV includes all undercapitalized institutions that are assigned to Supervisory Group C.

Based upon the current risk-based assessment rate schedule, American River Bank s current capital ratios and levels of deposits, American River Bank does not anticipate a significant increase in operating expenses due to the assessment rate applicable to it during 2008 compared to 2007.

General Competitive Factors

In order to compete with the major financial institutions in their primary service areas, American River Bank uses to the fullest extent possible the flexibility which is accorded by their community banks status. This includes an emphasis on specialized services, local promotional activity, and personal contacts by their respective officers, directors and employees. They also seek to provide special services and programs for individuals in their primary service area who are employed in the agricultural, professional and business fields, such as loans for equipment, furniture, tools of the trade or expansion of practices or businesses. In the event there are customers whose loan demands exceed their respective lending limits, they seek to arrange for such loans on a participation basis with other financial institutions. They also assist those customers requiring services not offered by either bank to obtain such services from correspondent banks.

Commercial banks compete with savings and loan associations, credit unions, other financial institutions and other entities for funds. For instance, yields on corporate and government debt securities and other commercial paper affect the ability of commercial banks to attract and hold deposits. Commercial banks also compete for loans with savings and loan associations, credit unions, consumer finance companies, mortgage companies and other lending institutions.

Banking is a business that depends on interest rate differentials. In general, the difference between the interest rate paid by a bank to obtain their deposits and other borrowings and the interest rate received by a bank on loans extended to customers and on securities held in a bank s portfolio comprise the major portion of a bank s revenues.

The interest rate differentials of a bank, and therefore their revenues, are affected not only by general economic conditions, both domestic and foreign, but also by the monetary and fiscal policies of the United States as set by statutes and as implemented by federal agencies, particularly the Federal Reserve Board. The Federal Reserve Board can and does implement national monetary policy, such as seeking to curb inflation and combat recession, by its open market operations in United States government securities, adjustments in the amount of interest free reserves that banks and other financial institutions are required to maintain, and adjustments to the discount rates applicable to borrowing by banks from the Federal Reserve Board. These activities influence the growth of bank loans, investments and deposits and also affect interest rates charged on loans and paid on deposits. The nature and timing of any future changes in monetary policies and their impact on American River Bank is not predictable.

Impact of Legislative and Regulatory Proposals

Since 1996, California law implementing certain provisions of prior federal law has (1) permitted interstate merger transactions; (2) prohibited interstate branching through the acquisition of a branch business unit located in California without acquisition of the whole business unit of the California bank; and (3) prohibited interstate branching through de novo establishment of California branch offices. Initial entry into California by an out-of-state institution must be accomplished by acquisition of or merger with an existing whole bank which has been in existence for at least five years.

The federal financial institution agencies, especially the Board of Governors, have taken steps to increase the types of activities in which bank holding companies can engage, and to make it easier to engage in such activities.

In 1999, the Gramm-Leach-Bliley Act (the GLB Act) was signed into law. The GLB Act eliminates most of the remaining depression-era firewalls between banks, securities firms and insurance companies which was established by The Banking Act of 1933, also known as the Glass-Steagall Act (Glass-Steagall). Glass-Steagall sought to insulate banks as depository institutions from the perceived risks of securities dealing and underwriting, and related activities. The GLB Act repealed Section 20 of Glass-Steagall which prohibited banks from affiliating with securities firms. Bank holding companies that can qualify as financial holding companies can now acquire securities firms or create them as subsidiaries, and securities firms can now acquire banks or start banking activities through a financial holding company. The GLB Act includes provisions which permit national banks to conduct financial activities through a subsidiary that are permissible for a national bank to engage in directly, as well as certain activities authorized by statute, or that are financial in nature or incidental to financial activities to the same extent as permitted to a financial holding company or its affiliates. This liberalization of United States banking and financial services regulation applies both to domestic institutions and foreign institutions conducting business in the United States. Consequently, the common ownership of banks, securities firms and insurance firms is now possible, as is the conduct of commercial banking, merchant banking, investment management, securities underwriting and insurance within a single financial institution using a financial holding company structure authorized by the GLB Act.

Prior to the GLB Act, significant restrictions existed on the affiliation of banks with securities firms and on the direct conduct by banks of securities dealing and underwriting and related securities activities. Banks were also (with minor exceptions) prohibited from engaging in insurance activities or affiliating with insurers. The GLB Act removed these restrictions and substantially eliminated the prohibitions under the Bank Holding Company Act on affiliations between banks and insurance companies. Bank holding companies which qualify as financial holding companies can now insure, guarantee, or indemnify against loss, harm, damage, illness, disability, or death; issue annuities; and act as a principal, agent, or broker regarding such insurance services.

In order for a commercial bank to affiliate with a securities firm or an insurance company pursuant to the GLB Act, its bank holding company must qualify as a financial holding company. A bank holding company will qualify if (i) its banking subsidiaries are well capitalized and well managed and (ii) it files with the Board of Governors a certification to such effect and a declaration that it elects to become a financial holding company. The amendment of the Bank Holding Company Act now permits financial holding companies to engage in activities, and acquire companies engaged in activities, that are financial in nature or incidental to such financial activities. Financial holding companies are also permitted to engage in activities that are complementary to financial activities if the Board of Governors determines that the activity does not pose a substantial risk to the safety or soundness of depository institutions or the financial system in general. These standards expand upon the list of activities closely related to banking which have to date defined the permissible activities of bank holding companies under the Bank Holding Company Act.

One further effect of the GLB Act is to require that federal financial institution and securities regulatory agencies prescribe regulations to implement the policy that financial institutions must respect the privacy of their customers and protect the security and confidentiality of customers non-public personal information. These regulations require, in general, that financial institutions (1) may not disclose non-public personal information of customers to non-affiliated third parties without notice to their customers, who must have the opportunity to direct that such information not be disclosed; (2) may not disclose customer account numbers except to consumer reporting agencies; and (3) must give prior disclosure of their privacy policies before establishing new customer relationships.

Neither American River Bankshares or American River Bank have determined whether or when they may seek to acquire and exercise powers or activities under the GLB Act, and the extent to which competition will change among financial institutions affected by the GLB Act has not yet become clear.

On October 26, 2001, President Bush signed the USA Patriot Act (the Patriot Act), which includes provisions pertaining to domestic security, surveillance procedures, border protection, and terrorism laws to be administered by the Secretary of the Treasury. Title III of the Patriot Act entitled, International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001 includes amendments to the Bank Secrecy Act which expand the responsibilities of financial institutions in regard to anti-money laundering activities with particular emphasis upon international money laundering and terrorism financing activities through designated correspondent and private banking accounts.

Effective December 25, 2001, Section 313(a) of the Patriot Act prohibits any insured financial institution such as American River Bank, from providing correspondent accounts to foreign banks which do not have a physical presence in any country (designated as shell banks), subject to certain exceptions for regulated affiliates of foreign banks. Section 313(a) also requires financial institutions to take reasonable steps to ensure that foreign bank correspondent accounts are not being used to indirectly provide banking services to foreign shell banks, and Section 319(b) requires financial institutions to maintain records of the owners and agent for service of process of any such foreign banks with whom correspondent accounts have been established.

Effective July 23, 2002, Section 312 of the Patriot Act created a requirement for special due diligence for correspondent accounts and private banking accounts. Under Section 312, each financial institution that establishes, maintains, administers, or manages a private banking account or a correspondent account in the United States for a non-United States person, including a foreign individual visiting the United States, or a representative of a non-United States person shall establish appropriate, specific, and, where necessary, enhanced, due diligence policies, procedures, and controls that are reasonably designed to detect and record instances of money laundering through those accounts.

The Patriot Act contains various provisions in addition to Sections 313(a) and 312 that affect the operations of financial institutions by encouraging cooperation among financial institutions, regulatory authorities and law enforcement authorities with respect to individuals, entities and organizations engaged in, or reasonably suspected of engaging in, terrorist acts or money laundering activities. The Company and American River Bank are not currently aware of any account relationships between American River Bank and any foreign bank or other person or entity as described above under Sections 313(a) or 312 of the Patriot Act.

Certain surveillance provisions of the Patriot Act were scheduled to expire on December 31, 2005, and actions to restrict the use of the Patriot Act surveillance provisions were filed by the ACLU and other organizations. On March 9, 2006, after temporary extensions of the Patriot Act, President Bush signed the USA Patriot Improvement and Reauthorization Act of 2005 and the USA Patriot Act Additional Reauthorizing Amendments Act of 2006, which reauthorized all expiring provisions of the Patriot Act by making permanent 14 of the 16 provisions and imposed a four-year expiration date on December 31, 2009 on the other two provisions related to roving surveillance and production of business records.

The effects which the Patriot Act and any additional legislation enacted by Congress may have upon financial institutions is uncertain; however, such legislation could increase compliance costs and thereby potentially may have an adverse effect upon the Company s results of operations.

On July 30, 2002, President George W. Bush signed into law the Sarbanes-Oxley Act of 2002 (the Act) which responds to recent issues in corporate governance and accountability. Among other matters, key provisions of the Act and rules promulgated by the SEC pursuant to the Act include the following:

- Expanded oversight of the accounting profession by creating a new independent public company oversight board to be monitored by the SEC.
- Revised rules on auditor independence to restrict the nature of non-audit services provided to audit clients and to require such services to be pre-approved by the audit committee.
- Improved corporate responsibility through mandatory listing standards relating to audit committees, certifications of periodic reports by the CEO and CFO and making issuer interference with an audit a crime.
- Enhanced financial disclosures, including periodic reviews for largest issuers and real time disclosure of material company information.
- Enhanced criminal penalties for a broad array of white collar crimes and increases in the statute of limitations for securities fraud lawsuits.
- Disclosure of whether a company has adopted a code of ethics that applies to the company s principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions, and disclosure of any amendments or waivers to such code of ethics.
- Disclosure of whether a company s audit committee of its board of directors has a member of the audit committee who qualifies as an audit committee financial expert.
- A prohibition on insider trading during pension plan black-out periods.
- Disclosure of off-balance sheet transactions.
- A prohibition on personal loans to directors and officers.
- Conditions on the use of non-GAAP (generally accepted accounting principles) financial measures.

Standards on professional conduct for attorneys requiring attorneys having an attorney-client relationship with a company, among other matters, to report up the ladder to the audit committee, another board committee or the entire board of directors certain material violations.

Expedited filing requirements for Form 4 reports of changes in beneficial ownership of securities reducing the filing deadline to within 2 business days of the date a transaction triggers an obligation to report.

Accelerated filing requirements for Forms 10-K and 10-Q by public companies which qualify as accelerated filers to a phased-in reduction of the filing deadline for Form 10-K reports and Form 10-Q reports.

Disclosure concerning website access to reports on Forms 10-K, 10-Q and 8-K, and any amendments to those reports, by accelerated filers as soon as reasonably practicable after such reports and material are filed with or furnished to the SEC.

Rules requiring national securities exchanges and national securities associations to prohibit the listing of any security whose issuer does not meet audit committee standards established pursuant to the Act.

The Company s securities are listed on the Nasdaq Global Select Market. Consequently, in addition to the rules promulgated by the SEC pursuant to the Act, the Company must also comply with the listing standards applicable to Nasdaq listed companies. The Nasdaq listing standards applicable to the Company include standards related to (i) director independence, (ii) executive session meetings of the board, (iii) requirements for audit, nominating and compensation committee charters, membership qualifications and procedures, (iv) shareholder approval of equity compensation arrangements, and (v) code of conduct requirements that comply with the code of ethics under the Act.

The effect of the Act upon the Company is uncertain; however, the Company has incurred and it is anticipated that it will continue to incur increased costs to comply with the Act and the rules and regulations promulgated pursuant to the Act by the SEC, Nasdaq and other regulatory agencies having jurisdiction over the Company or the issuance and listing of its securities. The Company does not currently anticipate, however, that compliance with the Act and such rules and regulations will have a material adverse effect upon its financial position or results of its operations or its cash flows.

Effective January 1, 2003, the California Corporate Disclosure Act (the CCD Act) required publicly traded corporations incorporated or qualified to do business in California to disclose information about their past history, auditors, directors and officers. Effective September 28, 2004, the CCD Act, as currently in effect and codified at California Corporations Code Section 1502.1, requires the Company to file with the California Secretary of State and disclose within 150 days after the end of its fiscal year certain information including the following:

The name of the a company s independent auditor and a description of services, if any, performed for a company during the previous two fiscal years and the period from the end of the most recent fiscal year to the date of filing;

The annual compensation paid to each director and the five most highly compensated non-director executive officers (including the CEO) during the most recent fiscal year, including all plan and non-plan compensation for all services rendered to a company as specified in Item 402 of Regulation S-K such as grants, awards or issuance of stock, stock options and similar equity-based compensation;

A description of any loans made to a director at a preferential loan rate during the company s two most recent fiscal years, including the amount and terms of the loans;

Whether any bankruptcy was filed by a company or any of its directors or executive officers within the previous 10 years;

Whether any director or executive officer of a company has been convicted of fraud during the previous 10 years; and

A description of any material pending legal proceedings other than ordinary routine litigation as specified in Item 103 of Regulation S-K and a description of such litigation where the company was found legally liable by a final judgment or order.

The Company does not currently anticipate that compliance with the CCD Act will have a material adverse effect upon its financial position or results of its operations or its cash flows.

The Check Clearing for the 21st Century Act (commonly referred to as Check 21) was signed into law in 2003 and became effective on October 28, 2004. The law facilitates check truncation by creating a new negotiable instrument called a substitute check which permits banks to truncate original checks, to process check information electronically and to deliver substitute checks to banks that want to continue receiving paper checks. Check 21 is intended to reduce the dependence of the check payment system on physical transportation networks (which can be disrupted by terrorist attacks of the type which occurred on September 11, 2001) and to streamline the collection and return process. The law does not require banks to accept checks in electronic form nor does it require banks to use the new authority granted by the Act to create substitute checks. The Company does not currently anticipate that compliance with the Act will have a material effect upon its financial position or results of its operations or its cash flows.

The Board of Governors, the FDIC, the other federal financial institution regulatory agencies, and the Federal Trade Commission issued a joint press release on October 31, 2007 and final rules and guidelines effective January 1, 2008, subject to mandatory compliance as of November 1, 2008, implementing sections 114 and 315 of the Fair and Accurate Credit Transactions Act of 2003 to require financial institutions and other creditors to develop and implement a written identity theft prevention program. The program must include reasonable policies and procedures for detecting, preventing, and mitigating identity theft in connection with certain new and existing covered accounts. Covered accounts are defined as (i) an account primarily for personal, family, or household purposes (i.e., consumer accounts), or (ii) any other account for which there is a reasonably foreseeable risk to customers or the safety and soundness of the financial institution or creditor from identity theft. The program must be appropriate to the size and complexity of the financial institution or creditor and the nature and scope of its activities and should be designed to:

identify relevant patterns, practices, and specific forms of activity that are red flags of possible identity theft and incorporate those red flags into the program;

detect the occurrence of red flags incorporated into the program;

respond appropriately to any red flags that are detected to prevent and mitigate identity theft; and

ensure that the program is updated periodically to reflect changes in risks to customers or to the safety and soundness of the financial institution or creditor from identity theft.

The regulations include guidelines that each financial institution must consider and, to the extent appropriate, include in its program and steps that must be taken to administer the program including (i) obtaining approval of the program by the board of directors or a committee of the board, (ii) ensuring oversight of the development, implementation and administration of the program, (iii) training staff, and (iv) overseeing service provider arrangements. The guidelines contemplate that existing fraud prevention procedures may be incorporated into the program.

In addition to legislative changes, the various Federal and state financial institution regulatory agencies frequently propose rules and regulations to implement and enforce already existing legislation. It cannot be predicted whether or in what form any such rules or regulations will be enacted or the effect that such regulations may have on American River Bankshares or American River Bank.

Item 1A. Risk Factors.

The Company and its subsidiary, American River Bank, conduct business in an environment that includes certain risks described below which could have a material adverse effect on the Company s business, results of operations, financial condition, future prospects and stock price. You are also referred to the matters described under the heading Cautionary Statements Regarding Forward-Looking Statements, in Part I, Item 1 and Part II, Item 7 of this report on Form 10-K for additional information regarding factors that may affect the Company s business.

American River Bankshares business is subject to interest rate risk, and variations in interest rates may negatively affect its financial performance.

Changes in the interest rate environment may reduce the Company s net interest income. It is expected that the Company will continue to realize income from the differential or spread between the interest earned on loans, securities and other interest-earning assets, and interest paid on deposits, borrowings and other interest-bearing liabilities. Net interest spreads are affected by the difference between the maturities and repricing characteristics of interest-earning assets and interest-bearing liabilities. In addition, loan volume and yields are affected by market interest rates on loans, and rising interest rates generally are associated with a lower volume of loan originations. We cannot assure you that we can minimize the Company s interest rate risk. In addition, an increase in the general level of interest rates may adversely affect the ability of certain borrowers to pay the interest on and principal of their obligations. Accordingly, changes in levels of market interest rates could materially and adversely affect the Company s net interest spread, asset quality, loan origination volume and overall profitability.

Governmental monetary policies affect American River Bankshares business and are beyond the control of the Company.

The business of banking is affected significantly by the fiscal and monetary policies of the federal government and its agencies. Such policies are beyond the control of the Company. The Company is particularly affected by the policies established by the Board of Governors in relation to the supply of money and credit in the United States. The instruments of monetary policy available to the Board of Governors can be used in varying degrees and combinations to directly affect the availability of bank loans and deposits, as well as the interest rates charged on loans and paid on deposits, and this can and does have a material effect on the Company s business, results of operations and financial condition.

American River Bankshares subsidiary, American River Bank, faces strong competition from banks, financial service companies and other companies that offer banking services, which can hurt American River Bankshares business.

Increased competition in the market of the Company s subsidiary, American River Bank, may result in reduced loans and deposits. Ultimately, it may not be able to compete successfully against current and future competitors. Many competitors offer the banking services that are offered by American River Bank in its service area. These competitors include national and super-regional banks, finance companies, investment banking and brokerage firms, credit unions, government-assisted farm credit programs, other community banks and technology-oriented financial institutions offering online services. In particular, American River Bank s competitors include several major financial companies whose greater resources may afford them a marketplace advantage by enabling them to maintain numerous banking locations and mount extensive promotional and advertising campaigns. Additionally, banks and other financial institutions with larger capitalization and financial intermediaries not subject to bank regulatory restrictions have larger lending limits and are thereby able to serve the credit needs of larger customers. Areas of competition include interest rates for loans and deposits, efforts to obtain deposits, and range and quality of products and services provided, including new technology-driven products and services. Technological innovation continues to contribute to greater competition in domestic and international financial services markets as technological advances, such as Internet-based banking services that cross traditional geographic bounds, enable more companies to provide financial services. If American River Bank is unable to attract and retain banking customers, it may be unable to continue its loan growth and level of deposits, which may adversely affect its and the Company s results of operations, financial condition and future prospects.

Worsening economic conditions in Northern California could adversely affect American River Bankshares business.

The Company s subsidiary, American River Bank, conducts banking operations principally in Northern California. As a result, the Company s financial condition, results of operations and cash flows are subject to changes in the economic conditions in Northern California. The Company s business results are dependent in large part upon the business activity, population, income levels, deposits and real estate activity in Northern California, and adverse economic conditions could have adverse effects upon the Company. The State of California is currently experiencing significant budgetary and fiscal difficulties. The Company can provide no assurance that conditions in the California economy will not deteriorate or that such deterioration will not adversely affect the Company. A deterioration in economic conditions locally, regionally or nationally, including the economic impact of terrorist activities within and outside California could result in an economic downturn in Northern California and trigger the following consequences, any of which could adversely affect the Company s business:

- loan delinquencies and defaults may increase;
- problem assets and foreclosures may increase;

demand for the Company s products and services may decline;

low cost or non-interest bearing deposits may decrease; and

collateral for loans may decline in value, in turn reducing customers borrowing power, and reducing the value of assets and collateral as sources of repayment of existing loans.

American River Bankshares has a concentration risk in real estate related loans.

At December 31, 2007, approximately 68.0% of the Company s loan and lease portfolio consisted of real estate related loans. Substantially all of the Company s real property collateral is located in its operating markets in Northern California. A substantial decline in real estate values in the Company s primary market areas could occur as a result of worsening economic conditions, or other events including natural disasters such as earthquakes, fires, and floods. Such a decline in values could have an adverse impact on the Company by limiting repayment of defaulted loans through sale of the real estate collateral and by likely increasing the number of defaulted loans to the extent that the financial condition of its borrowers is adversely affected by such a decline in values. At December 31, 2007, residential construction loans, including land acquisition and development, totaled $48.8 million or 12.2% of the Company s total loan portfolio. This was comprised of 38.0% owner-occupied and 62.0% speculative construction and land loans. Construction, land acquisition and development lending involve additional risks because funds are advanced on the security of the project, which is of uncertain value prior to its completion. Because of the uncertainties inherent in estimating construction costs, as well as the market value of the completed project and the effects of governmental regulation on real property, it is relatively difficult to evaluate accurately the total funds required to complete a project and the related loan-to-value ratio. As a result, speculative construction loans often involve the disbursement of substantial funds with repayment dependent, in part, on the completion of the project and the ability of the borrower to sell the property, rather than the ability of the borrower or the guarantor to repay the principal and interest. If our appraisal of the value of the completed project proves to be overstated, we may have inadequate security for the repayment of the loan upon completion of construction of the project. If we are forced to foreclose on a project prior to or at completion due to a default, there can be no assurance that we will be able to recover all of the unpaid balance of, and accrued interest on, the loan, a well as related foreclosure and holding costs. In addition, we may be required to fund additional amounts to complete the project and may have to hold the property for an unspecified period of time. The adverse effects of the foregoing matters upon the Company s real estate portfolio could necessitate a material increase in the provision for loan and lease losses which could adversely affect the Company s results of operations, financial condition, and future prospects.

American River Bankshares is subject to extensive regulation, which could adversely affect its business.

The Company s operations are subject to extensive regulation by state and local governmental authorities and are subject to various laws and judicial and administrative decisions imposing requirements and restrictions on part or all of its operations. The Company believes that it is in substantial compliance in all material respects with laws, rules and regulations applicable to the conduct of its business. Because the Company s business is highly regulated, the laws, rules and regulations applicable to it are subject to regular modification and change. There can be no assurance that these laws, rules and regulations, or any other laws, rules or regulations, will not be adopted in the future, which could make compliance much more difficult or expensive, restrict the Company s ability to originate, broker or sell loans, further limit or restrict the amount of commissions, interest or other charges earned on loans originated or sold by the Company, or otherwise adversely affect the Company s results of operations, financial condition, or future prospects.

American River Bank s allowance for loan and lease losses may not be adequate to cover actual losses.

Like all financial institutions, American River Bank maintains an allowance for loan and lease losses to provide for loan defaults and non-performance, but its allowance for loan and lease losses may not be adequate to cover actual loan and lease losses. In addition, future provisions for loan and lease losses could materially and adversely affect American River Bank s and therefore the Company s operating results. American River Bank s allowance for loan and lease losses is based on prior experience, as well as an evaluation of the risks in the current portfolio. The amount of future losses is susceptible to changes in economic, operating and other conditions, including changes in the local and California real estate market and interest rates that may be beyond American River Bank s control, and these losses may exceed current estimates. Federal regulatory agencies, as an integral part of their examination process, review American River Bank s loans and leases and allowance for loan and lease losses. Although we believe that American River Bank s allowance for loan and lease losses is adequate to cover current losses, we cannot assure you that it will not further increase the allowance for loan and lease losses or that regulators will not require it to increase this allowance. Either of these occurrences could materially and adversely affect the Company s earnings.

American River Bankshares and American River Bank s operations are dependent upon key personnel.

The future prospects of the Company will be highly dependent on its directors, executive officers and other key personnel. The success of the Company will, to some extent, depend on the continued service of its directors and continued employment of the executive officers, in addition to the Company s ability to attract and retain experienced banking professionals to serve the Company and the Bank in other key positions. The unexpected loss of the services of any of these individuals could have a detrimental effect on the Company and American River Bank.

Technology implementation problems or computer system failures could adversely affect American River Bankshares and American River Bank.

The Company s future prospects will be highly dependent on the ability of American River Bank to implement changes in technology that affect the delivery of banking services such as the increased demand for computer access to bank accounts and the availability to perform banking transactions electronically. The Bank s ability to compete will depend upon it ability to continue to adapt technology on a timely and cost-effective basis to meet such demands. In addition, the business and operations of the Company and the Bank will be susceptible to adverse effects from computer failures, communication and energy disruption, and the activities of unethical individuals with the technological ability to cause disruptions or failures of the Bank s data processing system.

Information security breach or other technology difficulties could adversely affect American River Bankshares and American River Bank.

The Company and the Bank cannot be certain that implementation of safeguards will eliminate the risk of vulnerability to technological difficulties or failures or ensure the absence of a breach of information security. The Bank will rely on the services of various vendors who provide data processing and communication services to the banking industry. Nonetheless, if information security is compromised or other technology difficulties or failures occur, information may be lost or misappropriated, services and operations may be interrupted and the Company and Bank could be exposed to claims from its customers as a result. The occurrence of any of these events could adversely affect the Company s results of operations, financial condition, prospects, and stock price.

Item 1B. Unresolved Staff Comments.

None.

Item 2. Properties.

The Company and American River Bank lease eleven and own two of their respective premises. The Company s headquarters is located at 3100 Zinfandel Drive, Suite 450, Rancho Cordova, California. The office space is located in a six-story office building. The location also houses a convenience office of American River Bank that performs limited branch related transactions and business development. The lease term is ninety-one (91) months and expires on May 6, 2013. The premises consist of 7,378 square feet on the fourth floor of the building. The space is leased from PGOCC, LLC.

American River Bank s main office is located at 1545 River Park Drive, Suite 107, Sacramento, California, in a modern, five-story building which has offstreet parking for its clients. American River Bank leases premises in the building from EOP-Point West, LLC. The lease term is ten (10) years and expires on March 31, 2010. The premises consist of 9,498 square feet on the ground floor.

American River Bank leases premises at 9750 Business Park Drive, Sacramento, California. The premises are leased from Bradshaw Plaza Group, which is owned in part by Charles D. Fite, a director of the Company. The lease term is ten (10) years and expires on November 30, 2016. The premises consist of 3,711 square feet on the ground floor.

American River Bank leases premises at 10123 Fair Oaks Boulevard, Fair Oaks, California. The premises are leased from Marjorie Taylor, a former director of the Company. The lease term is twelve (12) years and expires on March 1, 2009. The premises consist of 2,380 square feet on the ground floor.

American River Bank leases premises at 2240 Douglas Boulevard, Roseville, California. The premises are leased from Twin Tree Land Company. The lease term is ten (10) years and expires on November 30, 2016. The premises consist of 3,790 square feet on the ground floor.

American River Bank leases premises at 520 Capitol Mall, Sacramento, California. The premises are leased from 520 Capitol Mall, Inc. The lease term is ten (10) years and expires on June 1, 2014. The premises consist of 4,010 square feet on the ground floor.

American River Bank leases premises at 3330 Cameron Park Drive, Cameron Park, California for the purpose of a loan production office. The premises are leased from Sierra Investment Group. The lease term is one (1) year and expires on March 31, 2008. The premises consist of 720 square feet on the ground floor.

North Coast Bank, a division of American River Bank, leases premises at 8733 Lakewood Drive, Windsor, California. The premises are leased from R. and R. Partners. The lease term is two (2) years and expires on December 31, 2008. The premises consist of 2,200 square feet on the ground floor.

North Coast Bank, a division of American River Bank, owns premises at 412 Center Street, Healdsburg, California. The premises were purchased June 1, 1993. The purchase price for the land and building was $343,849. The building consists of 2,620 square feet. The land consists of 10,835 square feet.

North Coast Bank, a division of American River Bank, leases premises at 50 Santa Rosa Avenue, Santa Rosa, California. The premises are leased from HSG Trust. The lease term is ten (10) years and expires on January 31, 2009. The premises consist of 7,072 square feet on the ground floor.

Bank of Amador, a division of American River Bank, leases premises at 422 Sutter Street, Jackson, California. The premises are leased from the United States Postal Service. The lease term is five (5) years and expires on May 31, 2011. The premises consist of 6,400 square feet on the ground floor and second floor.

Bank of Amador, a division of American River Bank, leases land at 26395 Buckhorn Ridge Road, Pioneer, California. The premises are leased from Joseph T. Bellamy, Trustee of the Joseph T. Bellamy 2005 Trust. The lease term is ten (10) years and expires on October 31, 2017. The premises consist of 1,757 square feet of office space on the ground floor, an attached garage consisting of approximately 400 square feet and 1,223 feet of office space on the second floor.

Bank of Amador, a division of American River Bank, owns premises at 66 Main Street, Ione, California. The premises were purchased April 1, 1995. The purchase price for the land and building was $167,500. The building consists of 2,576 square feet. The land consists of 9,700 square feet.

Bank of Amador, a division of American River Bank, leases the parking lot at 276 North Main Street, Jackson, California. The parking lot is leased from Wilhelmina Petkovich. The lease term is on a month-to-month basis.

The leases on the premises located at 1545 River Park Drive, 9750 Business Park Drive, 50 Santa Rosa Avenue, 26395 Buckhorn Ridge Road, and 3100 Zinfandel Drive, contain options to extend for five years.

Included in the above are two facilities leased from current or former directors of the Company at terms and conditions which management believes are consistent with the commercial lease market.

The foregoing summary descriptions of leased premises are qualified in their entirety by reference to the lease agreements listed as exhibits in Part IV, Item 15 of this Form 10-K report.

Item 3. Legal Proceedings.

There are no material legal proceedings adverse to the Company and its subsidiaries to which any director, officer, affiliate of the Company, or 5% shareholder of the Company or its subsidiaries, or any associate of any such director, officer, affiliate or 5% shareholder of the Company or its subsidiaries are a party, and none of the above persons has a material interest adverse to the Company or its subsidiaries.

From time to time, the Company and/or its subsidiaries is a party to claims and legal proceedings arising in the ordinary course of business. The Company s management is not aware of any material pending legal proceedings to which either it or its subsidiaries may be a party or has recently been a party, which will have a material adverse effect on the financial condition or results of operations of the Company or its subsidiaries, taken as a whole.

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

There were no matters submitted to a vote of the shareholders during the fourth quarter of 2007.

PART II

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

Market Information

The Company s common stock began trading on the NASDAQ National Stock Market (Nasdaq) under the symbol AMRB on October 26, 2000. Effective July 3, 2006, the Company s common stock became listed and traded on the Nasdaq Global Select Market. The following table shows the high and the low prices for the common stock, for each quarter during 2007 and 2006, as reported by Nasdaq. The prices have been adjusted to reflect 5% stock dividends declared in 2007 and in 2006.

2007	High	Low
First quarter	$ 25.23	$ 22.40
Second quarter	23.33	22.25
Third quarter	22.76	20.53
Fourth quarter	21.43	15.80

2006	High	Low
First quarter	$ 26.30	$ 19.28
Second quarter	26.30	23.36
Third quarter	24.67	21.95
Fourth quarter	24.26	21.91

The closing price for the Company s common stock on March 4, 2008 was $17.35.

Holders

As of February 29, 2008, there were approximately 2,688 shareholders of record of the Company s common stock.

Dividends

The Company has paid quarterly cash dividends on its common stock since the first quarter of 2004; prior to that, the Company paid cash dividends twice a year since 1992. It is currently the intention of the Board of Directors of the Company to continue payment of cash dividends on a quarterly basis. In 2007 and 2006, the Company declared cash dividends in the amount of $.58 and $.55, respectively, per common share. The amounts have been adjusted to reflect 5% stock dividends declared in 2007 and in 2006. There is no assurance, however, that any dividends will be paid in the future since they are subject to regulatory restrictions, and dependent upon earnings, financial condition and capital requirements of the Company and its subsidiaries.

The California General Corporation Law (the Corporation Law) provides that a corporation may make a distribution to its shareholders if the corporation s retained earnings equal at least the amount of the proposed distribution. The Corporation Law further provides that, in the event that sufficient retained earnings are not available for the proposed distribution, a corporation may nevertheless make a distribution to its shareholders if it meets two conditions, which generally stated are as follows: (1) the corporation s assets equal at least 1-1/4 times its liabilities; and (2) the corporation s current assets equal at least its current liabilities or, if the average of the corporation s earnings before taxes on income and before interest expenses for the two preceding fiscal years was less than the average of the corporation s interest expenses for such fiscal years, then the corporation s current assets must equal at least 1-1/4 times its current liabilities.

The Board of Governors generally prohibits a bank holding company from declaring or paying a cash dividend which would impose undue pressure on the capital of subsidiary banks or would be funded only through borrowing or other arrangements that might adversely affect a bank holding company s financial position. The Board of Governors policy is that a bank holding company should not continue its existing rate of cash dividends on its common stock unless its net income is sufficient to fully fund each dividend and its prospective rate of earnings retention appears consistent with its capital needs, asset quality and overall financial condition.

The payment of cash dividends by American River Bank is subject to restrictions set forth in the California Financial Code (the Financial Code). The Financial Code provides that a bank may not make a cash distribution to its shareholders in excess of the lesser of (a) the bank s retained earnings; or (b) the bank s net income for its last three fiscal years, less the amount of any distributions made by the bank or by any majority-owned subsidiary of the bank to the shareholders of the bank during such period. However, a bank may, with the approval of the Commissioner, make a distribution to its shareholders in an amount not exceeding the greater of (a) its retained earnings; (b) its net income for its last fiscal year; or (c) its net income for its current fiscal year. In the event that the Commissioner determines that the shareholders equity of a bank is inadequate or that the making of a distribution by the bank would be unsafe or unsound, the Commissioner may order the bank to refrain from making a proposed distribution.

The FDIC may also restrict the payment of dividends by a subsidiary bank if such payment would be deemed unsafe or unsound or if after the payment of such dividends, the bank would be included in one of the undercapitalized categories for capital adequacy purposes pursuant to the FDIC Improvement Act of 1991.

As of December 31, 2007, American River Bank had $1,941,000 in retained earnings available for dividend payments to the Company, which in turn could be paid out to shareholders of the Company.

Stock Repurchases

On September 20, 2001, the Board of Directors of the Company authorized a stock repurchase program which calls for the repurchase of up to five percent (5%) annually of the Company s outstanding shares of common stock. Each year the Company may repurchase up to 5% of the shares outstanding (adjusted for stock splits or stock dividends). On October 17, 2007, the Board of Directors of the Company expanded the stock repurchase program for calendar year 2007 by an additional $2,000,000. The shares reported in the table as shares that may be repurchased under the plan represent shares eligible for the calendar year 2007. The repurchases are to be made from time to time in the open market as conditions allow and will be structured to comply with Commission Rule 10b-18. Management reports monthly to the Board of Directors on the status of the repurchase program. The Board of Directors has reserved the right to suspend, terminate, modify or cancel this repurchase program at any time for any reason. The following table lists shares repurchased during the quarter ended December 31, 2007 and the maximum amount available to repurchase under the repurchase plan.

Period	(a) Total Number of Shares (or Units) Purchased	(b) Average Price Paid Per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) That May Yet Be Purchased Under the Plans or Programs
Month #1				
October 1 through October 31, 2007	30,000	$22.25	30,000	27,179 shares plus $2,000,000
Month #2				
November 1 through November 30, 2007	118,000	$21.75	118,000	Zero shares-plan/ program complete
Month #3				
December 1 through December 31, 2007		$		N/A
Total	148,000	$21.85	148,000	

The Company repurchased 406,350 shares in 2007, 285,152 shares in 2006, 88,558 shares in 2005, 11,304 shares in 2004, 1,824 shares in 2003 and 79,759 shares in 2002. Share amounts have been adjusted for stock dividends and/or splits. On January 16, 2008, the Board of Directors of the Company established a new stock repurchase program, increasing the annual buyback percentage from 5.0% to 6.5%.

Item 6. Selected Financial Data.

FINANCIAL SUMMARY-The following table presents certain consolidated financial information concerning the business of the Company and its subsidiaries. This information should be read in conjunction with the Consolidated Financial Statements, the notes thereto, and Management s Discussion and Analysis included in this report. All per share data has been retroactively restated to reflect stock dividends and stock splits. In December 2004, the Company completed a merger with Bank of Amador. The merger transaction was accounted for using the purchase method of accounting and accordingly the results of their operations are included in the table below.

As of and for the Years Ended December 31,
(In thousands, except per share amounts and ratios)

	2007	2006	2005	2004	2003
STATEMENT OF OPERATIONS DATA:					
Net interest income	$ 26,402	$ 27,066	$ 26,462	$ 19,418	$ 16,866
Provision for loan and lease losses	450	320	322	895	946
Other income	2,599	2,443	2,329	2,395	2,253
Other expenses	14,833	14,388	13,493	11,713	10,372
Income before income taxes	13,718	14,801	14,976	9,205	7,801
Income taxes	5,240	5,739	5,792	3,378	3,060
Net income	$ 8,478	$ 9,062	$ 9,184	$ 5,827	$ 4,741
Earnings per share basic	$ 1.47	$ 1.49	$ 1.48	$ 1.12	$ 0.98
Earnings per share diluted	1.46	1.46	1.45	1.07	0.90
Cash dividends per share	0.58	0.55	0.49	0.38	0.24
Book value per share	10.73	10.50	10.15	9.59	7.19
Tangible book value per share	7.60	7.50	7.24	6.61	7.18
BALANCE SHEET DATA:					
Balance sheet totals-end of period:					
Assets	$ 573,685	$ 604,003	$ 612,763	$ 586,666	$ 397,393
Loans and leases, net	394,975	382,993	365,571	352,467	262,464
Deposits	455,645	493,875	500,706	475,387	322,507
Shareholders equity	59,973	62,371	62,746	58,990	35,457
Average balance sheet amounts:					
Assets	$ 575,225	$ 603,040	$ 596,670	$ 439,012	$ 363,175
Loans and leases	390,488	381,465	360,319	277,647	248,342
Earning assets	524,365	544,794	537,031	400,265	333,800
Deposits	479,344	488,026	494,905	357,420	279,883
Shareholders equity	60,533	62,570	60,641	39,163	33,461
SELECTED RATIOS:					
For the year:					
Return on average equity	14.01%	14.48%	15.14%	14.88%	14.17%
Return on average assets	1.47%	1.50%	1.54%	1.33%	1.31%
Efficiency ratio *	49.49%	47.11%	45.16%	53.12%	53.73%
Net interest margin *	5.10%	5.03%	4.98%	4.90%	5.10%
Net chargeoffs to average loans & leases	0.11%	0.03%	0.04%	0.08%	0.08%
At December 31:					
Average equity to average assets	10.52%	10.38%	10.16%	8.92%	9.21%
Leverage capital ratio	7.72%	7.81%	7.66%	8.35%	8.96%
Allowance for loan and leases losses to total loans and leases	1.47%	1.51%	1.53%	1.54%	1.48%

* fully taxable equivalent

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

The following is American River Bankshares management s discussion and analysis of the significant changes in income and expense accounts for the years ended December 31, 2007, 2006, and 2005.

Cautionary Statements Regarding Forward-Looking Statements

Certain matters discussed or incorporated by reference in this Annual Report on Form 10-K including, but not limited to, matters described in Item 7 - Management s Discussion and Analysis of Financial Condition and Results of Operations, are forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, Section 27A of the Securities Act of 1933, as amended, and subject to the safe-harbor provisions of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements may contain words related to future projections including, but not limited to, words such as believe, expect, anticipate, intend, may, will, should, c would, and variations of those words and similar words that are subject to risks, uncertainties and other factors that could cause actual results to differ materially from those projected. Factors that could cause or contribute to such differences include, but are not limited to, the following: (1) variances in the actual versus projected growth in assets; (2) return on assets; (3) loan and lease losses; (4) expenses; (5) changes in the interest rate environment including interest rates charged on loans, earned on securities investments and paid on deposits; (6) competition effects; (7) fee and other noninterest income earned; (8) general economic conditions nationally, regionally, and in the operating market areas of the Company and its subsidiaries; (9) changes in the regulatory environment; (10) changes in business conditions and inflation; (11) changes in securities markets; (12) data processing problems; (13) a decline in real estate values in the Company s operating market areas; (14) the effects of terrorism, the threat of terrorism or the impact of the current military conflicts in Afghanistan and Iraq and the conduct of the war on terrorism by the United States and its allies, as well as other factors. The factors set forth under Item 1A - Risk Factors in this report and other cautionary statements and information set forth in this report should be carefully considered and understood as being applicable to all related forward-looking statements contained in this report, when evaluating the business prospects of the Company and its subsidiaries.

Forward-looking statements are not guarantees of performance. By their nature, they involve risks, uncertainties and assumptions. The future results and shareholder values may differ significantly from those expressed in these forward-looking statements. You are cautioned not to put undue reliance on any forward-looking statement. Any such statement speaks only as of the date of this report, and in the case of any documents that may be incorporated by reference, as of the date of those documents. We do not undertake any obligation to update or release any revisions to any forward-looking statements, to report any new information, future event or other circumstances after the date of this report or to reflect the occurrence of unanticipated events, except as required by law. However, your attention is directed to any further disclosures made on related subjects in our subsequent reports filed with the Securities and Exchange Commission (the SEC) on Forms 10-K, 10-Q and 8-K.

Critical Accounting Policies

General

The Company s financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The financial information contained within our statements is, to a significant extent, financial information that is based on measures of the financial effects of transactions and events that have already occurred. We use historical loss data, peer group experience and the economic environment as factors, among others, in determining the inherent loss that may be present in our loan and lease portfolio. Actual losses could differ significantly from the historical factors that we use. Other estimates that we use are related to the expected useful lives of our depreciable assets. In addition, GAAP itself may change from one previously acceptable method to another method. Although the economics of our transactions would be the same, the timing of events that would impact our transactions could change.

Allowance for Loan and Lease Losses

The allowance for loan and lease losses is an estimate of the credit loss risk in our loan and lease portfolio. The allowance is based on two basic principles of accounting: (1) Statement of Financial Accounting Standards (SFAS) No. 5 Accounting for Contingencies, which requires that losses be accrued when it is probable that a loss 23 has occurred at the balance sheet date and such loss can be reasonably estimated; and (2) SFAS No. 114, Accounting by Creditors for Impairment of a Loan, which requires that losses be accrued on impaired loans based on the differences between the value of collateral, present value of future cash flows or values that are observable in the secondary market and the loan balance.

The allowance for loan and lease losses is determined based upon estimates that can and do change when the actual risk, loss events, or changes in other factors, occur. The analysis of the allowance uses an historical loss view as an indicator of future losses and as a result could differ from the loss incurred in the future. If the allowance for loan and lease losses falls below that deemed adequate (by reason of loan and lease growth, actual losses, the effect of changes in risk ratings, or some combination of these factors), the Company has a strategy for supplementing the allowance for loan and lease losses, over the short term. For further information regarding our allowance for loan and lease losses, see Allowance for Loan and Lease Losses Activity discussion later in this Item 7.

Stock-Based Compensation

Prior to January 1, 2006 the Company accounted for its stock-based compensation under the recognition and measurement principles of Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. Because the Company s 2000 Stock Option Plan provides for the issuance of options at a price of no less than the fair market value at the date of the grant, no compensation expense was recognized in the financial statements unless the options were modified after the grant date.

Effective January 1, 2006, the company adopted Financial Accounting Standards Board (the FASB) Statement Number 123 (revised 2004) (FAS 123 (R)), Share-Based Payments on a modified prospective basis. FAS 123 (R) requires all entities to recognize compensation expense in an amount equal to the fair value of share-based payments such as stock options granted to employees. The Company is required to record compensation expense (as previous awards continue to vest) for the unvested portion of previously granted awards that remain outstanding at the date of adoption. As a result of adopting Statement 123(R) on January 1, 2006, the Company s income before provision for income taxes and net income for the year ended December 31, 2007, was $301,000 and $251,000 lower, respectively, and for the year ended December 31, 2006 was $221,000 and $184,000, respectively than if it had continued to account for share-based compensation under APB Opinion No. 25. Diluted earnings per share and basic earnings per share for the year ended December 31, 2007 would have increased $0.05 and $0.04, respectively, and for the year ended December 31, 2006 would have increased $0.04 and $0.03, respectively, had the Company continued to account for share-based compensation under APB Opinion No. 25.

The fair value of each option is estimated on the date of grant and amortized over the service period using an option pricing model. Critical assumptions that affect the estimated fair value of each option include expected stock price volatility, dividend yields, option life and the risk-free interest rate.

Goodwill

Business combinations involving the Company s acquisition of the equity interests or net assets of another enterprise or the assumption of net liabilities in an acquisition of branches constituting a business may give rise to goodwill. Goodwill represents the excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed in transactions accounted for under the purchase method of accounting. The value of goodwill is ultimately derived from the Company s ability to generate net earnings after the acquisition. A decline in net earnings could be indicative of a decline in the fair value of goodwill and result in impairment. For that reason, goodwill is assessed for impairment at a reporting unit level at least annually following the year of acquisition. The Company performed an evaluation of the goodwill, recorded as a result of the Bank of Amador acquisition, during the fourth quarter of 2007 and determined that there was no impairment. While the Company believes all assumptions utilized in its assessment of goodwill for impairment are reasonable and appropriate, changes in earnings, the effective tax rate, historical earnings multiples and the cost of capital could all cause different results for the calculation of the present value of future cash flows.

Income Taxes

The Company files its income taxes on a consolidated basis with its subsidiaries. The allocation of income tax expense (benefit) represents each entity s proportionate share of the consolidated provision for income taxes.

The Company accounts for income taxes using the balance sheet method, under which deferred tax assets and liabilities are recognized for the tax consequences of temporary differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. On the consolidated balance sheet, net deferred tax assets are included in accrued interest receivable and other assets.

The provisions of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48) have been applied to all tax positions of the Company as of January 1, 2007. FIN 48 prescribes a recognition threshold and measurement standard for the financial statement recognition and measurement of an income tax position taken, or expected to be taken, in a tax return. Only tax positions that met the more-likely-than-not recognition threshold on January 1, 2007 were recognized or continue to be recognized upon adoption. The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more likely than not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the more-likely-than-not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination. The election has been made to record interest expense related to tax exposures in tax expense, if applicable, and the exposure for penalties related to tax exposures in tax expense, if applicable.

Overview

The Company recorded its 96th consecutive profitable quarter for the quarter ended December 31, 2007. Net income in 2007 decreased 6.4% to $8,478,000 versus $9,062,000 in 2006. Diluted earnings per share for 2007 and 2006 were identical--$1.46. For 2007, the Company realized a return on average equity of 14.01% and a return on average assets of 1.47%, as compared to 14.48% and 1.50% for 2006.

Net income for 2006 was $122,000 (1.3%) lower than the $9,184,000 recorded in 2005. Diluted earnings per share in 2005 were $1.45, return on average assets was 1.54% and return on average equity was 15.14%. Table One below provides a summary of the components of net income for the years indicated:

Table One: Components of Net Income

For the twelve months ended: **(dollars in thousands)**	**2007**	**2006**	**2005**
Net interest income*	$ 26,749	$ 27,396	$ 26,767
Provision for loan and lease losses	(450)	(320)	(322)
Noninterest income	2,599	2,443	2,329
Noninterest expense	(14,833)	(14,388)	(13,493)
Provision for income taxes	(5,240)	(5,739)	(5,792)
Tax equivalent adjustment	(347)	(330)	(305)
Net income	$ 8,478	$ 9,062	$ 9,184
Average total assets	$ 575,225	$ 603,040	$ 596,670
Net income as a percentage of average total assets	1.47%	1.50%	1.54%

* Fully taxable equivalent basis (FTE)

All share and per share data for 2007, 2006 and 2005 have been adjusted for 5% stock dividends distributed on December 20, 2007, December 22, 2006, and December 23, 2005.

During 2007, total assets of the Company decreased $30,318,000 (5.0%) to a total of $573,685,000 at year-end. At December 31, 2007, net loans totaled $394,975,000, up $11,982,000 (3.1%) from the ending balances on December 31, 2006. Deposits decreased 7.7% during 2007 resulting in ending deposit balances of $455,645,000. The Company ended 2007 with a Tier 1 capital ratio of 9.5% and a total risk-based capital ratio of 10.7%.

Results of Operations

Net Interest Income and Net Interest Margin

Net interest income represents the excess of interest and fees earned on interest earning assets (loans, securities, Federal funds sold and investments in time deposits) over the interest paid on deposits and borrowed funds. Net interest margin is net interest income expressed as a percentage of average earning assets.

The Company s fully taxable equivalent net interest margin was 5.10% in 2007 and 5.03% in 2006. The fully taxable equivalent net interest income was down $647,000 (2.4%) in 2007 compared to 2006.

The fully taxable equivalent interest income component decreased from $38,284,000 in 2006 to $37,825,000 in 2007, representing a 1.2% decrease. The decrease in the fully taxable equivalent interest income for 2007 compared to the same period in 2006 is broken down by rate (up $67,000) and volume (down $526,000). The rate increase can be attributed to an increase in the yield on the investment portfolio from 4.41% in 2006 to 4.72% in 2007. The increase in yield results from matured short-term securities with lower yields being redirected to reduce borrowings and fund the growth in loans and leaving the investment portfolio with longer maturity higher yielding investments, thus an overall higher average yield on the existing portfolio. The volume decrease was the result of a 3.7% decrease in average earning assets. The Company has made a decision to use the proceeds from principal reductions and maturing investment securities to reduce the level of outstanding borrowings and provide funding for loan growth. This strategy has reduced the average balances on investment securities by 18.3% from $162,970,000 during 2006 to $133,187,000 during 2007. Average balances of other borrowings were down $17,010,000 (36.4%) and average loan balances were up $9,023,000 (2.4%) during the same time period. The increase in average loans is the result of concentrated focus on business lending.

The fully taxable equivalent interest income component increased from $33,518,000 in 2005 to $38,284,000 in 2006, representing a 14.2% increase. The increase in the fully taxable equivalent interest income for 2006 compared to the same period in 2005 is broken down by rate (up $3,681,000) and volume (up $1,085,000). The rate increase can be attributed to increases implemented by the Company during 2004 and 2005 and continuing through the end of 2006 in response to the Federal Reserve Board (the FRB) increases in the Federal funds and discount rates. Increases by the FRB have resulted in seventeen 25 basis point increases from June 2004 through December 31, 2006. The overall increasing interest rate environment during that time frame resulted in a 79 basis point increase in the yield on average earning assets from 6.24% for 2005 to 7.03% for 2006. The volume increase was the result of a 1.5% increase in average earning assets and a shift in balances from lower earning investment balance to higher earning loan balances. Average loan balances were up $21,146,000 (5.9%) in 2006 over the balances in 2005, while average investment securities balances were down $10,066,000 (6.0%). The increase in average loans is the result of concentrated focus on business lending, the demand for commercial real estate and the effects of a favorable local market during this time frame.

Interest expense increased $188,000 (1.7%) in 2007 compared to 2006. The increase in rates paid on interest bearing liabilities resulted in an increase of $1,097,000 in interest expense. The rates paid on interest bearing liabilities increased 16 basis points on a year-over-year basis and was a result of the higher overall interest rate environment. A drop in average balances reduced much of this increase due to higher rates. The average balances on interest bearing liabilities were $14,447,000 (3.8%) lower in 2007 versus 2006. The lower balances accounted for a $909,000 decrease in interest expense. In 2007, average interest bearing deposits were up $2,563,000 (0.8%) but other borrowings were down $17,010,000 (36.4%) creating the overall drop in interest bearing balances. In 2007, the Company focused on reducing the higher cost borrowings; the decrease in other borrowings accounting for $806,000 in reduced interest costs from volume compared to 2006. The Company also focused on bringing in additional checking, money market, and savings accounts, and reducing higher priced time deposits and as a result, the average balances on interest checking, money market and savings accounts were up $8,033,000 (4.0%) adding $119,000 to interest expense attributable to the increased volume, while the average time deposit balances were down $5,470,000 (4.2%) reducing the expense by $222,000.

Interest expense increased $4,137,000 (61.3%) in 2006 compared to 2005. The increase in rates paid on interest bearing liabilities resulted in an increase of $3,561,000 in interest expense. The rates paid on interest bearing liabilities increased 107 basis points on a year-over-year basis and was a result of the higher overall interest rate environment as well as an increase in higher cost other borrowings. The increase in other borrowings is primarily the result of a decline in deposit balances both interest bearing and noninterest bearing. The decline in deposit balances is primarily related to an increase in the number of financial institutions in the Sacramento market. In addition, the Company has seen a decline in the deposit balances in a number of its business accounts as a result of these businesses paying down debt and/or investing in real estate or business inventory. Although these balances declined the customer relationships were maintained and the decreasing deposit balances were replaced with funds from other borrowing sources. The average balances on interest bearing liabilities were $5,226,000 (1.4%) higher in 2006 versus 2005. The higher balances accounted for a $576,000 increase in interest expense. In 2006, average deposits were down $6,879,000 (1.4%) and other borrowings were up $11,687,000 (33.4%)

Table Two, Analysis of Net Interest Margin on Earning Assets, and Table Three, Analysis of Volume and Rate Changes on Net Interest Income and Expenses, are provided to enable the reader to understand the components and past trends of the Company s interest income and expenses. Table Two provides an analysis of net interest margin on earning assets setting forth average assets, liabilities and shareholders equity; interest income earned and interest expense paid and average rates earned and paid; and the net interest margin on earning assets. Table Three sets forth a summary of the changes in interest income and interest expense from changes in average asset and liability balances (volume), computed on a daily average basis, and changes in average interest rates.

Table Two: Analysis of Net Interest Margin on Earning Assets

Year Ended December 31,	2007			2006			2005		
(Taxable Equivalent Basis) (dollars in thousands)	**Avg Balance**	**Interest**	**Avg Yield**	**Avg Balance**	**Interest**	**Avg Yield**	**Avg Balance**	**Interest**	**Avg Yield**
Assets:									
Earning assets									
Loans and leases (1)	$ 390,488	$ 31,508	8.07%	$ 381,465	$ 31,082	8.15%	$ 360,319	$ 26,536	7.36%
Taxable investment securities	100,086	4,544	4.54%	129,608	5,545	4.28%	141,855	5,436	3.83%
Tax-exempt investment securities (2)	27,745	1,436	5.18%	27,886	1,355	4.86%	25,705	1,228	4.78%
Corporate stock	407	32	7.86%	559	42	7.51%	559	40	7.16%
Federal funds sold	690	34	4.93%	359	19	5.29%	2,826	90	3.18%
Interest bearing balances in other banks	4,949	271	5.48%	4,917	241	4.90%	5,767	188	3.26%
Total earning assets	524,365	37,825	7.21%	544,794	38,284	7.03%	537,031	33,518	6.24%
Cash & due from banks	17,263			28,401			29,566		
Other assets	39,529			35,708			35,760		
Allowance for loan & lease losses	(5,932)			(5,863)			(5,687)		
	$ 575,225			$ 603,040			$ 596,670		
Liabilities & Shareholders Equity:									
Interest bearing liabilities:									
NOW & MMDA	$ 173,382	3,781	2.18%	$ 168,128	3,204	1.91%	$ 185,634	2,247	1.21%
Savings	37,690	546	1.45%	34,911	242	0.69%	39,102	150	0.38%
Time deposits	123,485	5,233	4.24%	128,955	5,231	4.06%	113,719	3,249	2.86%
Other borrowings	29,680	1,516	5.11%	46,690	2,211	4.74%	35,003	1,105	3.16%
Total interest bearing liabilities	364,237	11,076	3.04%	378,684	10,888	2.88%	373,458	6,751	1.81%
Demand deposits	144,787			156,032			156,450		
Other liabilities	5,668			5,754			6,121		
Total liabilities	514,692			540,470			536,029		
Shareholders equity	60,533			62,570			60,641		
	$ 575,225			$ 603,040			$ 596,670		
Net interest income & Margin (3)		$ 26,749	5.10%		$ 27,396	5.03%		$ 26,767	4.98%

(1) Loan and lease interest includes loan and lease fees of $529,000, $873,000 and $1,091,000 in 2007, 2006 and 2005, respectively.

(2) Includes taxable-equivalent adjustments that primarily relate to income on certain securities that is exempt from federal income taxes. The effective federal statutory tax rate was 34.5% in 2007 and 2006 and 34.0% in 2005.

(3) Net interest margin is computed by dividing net interest income by total average earning assets.

Table Three: Analysis of Volume and Rate Changes on Net Interest Income and Expenses

Year ended December 31, 2007 over 2006 (dollars in thousands)
Increase (decrease) due to change in:

	Volume	Rate (4)	Net Change
Interest-earning assets:			
Net loans and leases (1)(2)	$ 735	$ (309)	$ 426
Taxable investment securities	(1,263)	262	(1,001)
Tax-exempt investment securities (3)	(7)	88	81
Corporate stock	(11)	1	(10)
Federal funds sold & other	18	(3)	15
Interest bearing balances in other banks	2	28	30
Total	(526)	67	(459)
Interest-bearing liabilities:			
Demand deposits	100	477	577
Savings deposits	19	285	304
Time deposits	(222)	224	2
Other borrowings	(806)	111	(695)
Total	(909)	1,097	188
Interest differential	$ 383	$ (1,030)	$ (647)

Year Ended December 31, 2006 over 2005 (in thousands)
Increase (decrease) due to change in:

	Volume	Rate (4)	Net Change
Interest-earning assets:			
Net loans and leases (1)(2)	$ 1,557	$ 2,989	$ 4,546
Taxable investment securities	(469)	578	109
Tax-exempt investment securities (3)	104	23	127
Corporate stock		2	2
Federal funds sold & other	(79)	8	(71)
Interest bearing balances in other banks	(28)	81	53
Total	1,085		