

SANDY SPRING BANCORP INC  
Form 10-K  
March 05, 2008

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

**FORM 10-K**

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

For the Year Ended December 31, 2007

Commission File Number 0-19065

**SANDY SPRING BANCORP, INC.**

(Exact name of registrant as specified in its charter)

Maryland  
(State or other jurisdiction of  
incorporation or organization)

52-1532952  
(I.R.S. Employer  
Identification No.)

17801 Georgia Avenue, Olney, Maryland  
(Address of principal executive offices)

20832  
(Zip Code)

Registrant's telephone number, including area code: 301-774-6400.

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

Title of each class  
Common Stock, par value \$1.00 per share

Name of each exchange on which registered  
The NASDAQ Stock Market, LLC

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

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

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

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  No

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

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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

company” in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

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

The aggregate market value of the voting common stock of the registrant held by nonaffiliates on June 30, 2007, the last day of the registrant’s most recently completed second fiscal quarter, was approximately \$492 million, based on the closing sales price of \$30.95 per share of the registrant's Common Stock on that date.

As of the close of business on February 19, 2008, 16,380,033 shares of the registrant's Common Stock were outstanding.

**Documents Incorporated By Reference**

Part III: Portions of the definitive proxy statement for the Annual Meeting of Shareholders to be held on April 23, 2008 (the "Proxy Statement").

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\* The registrant is required to file reports pursuant to Section 13 of the Act.

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**Forward-Looking Statements**

Sandy Spring Bancorp, Inc. (the "Company") makes forward-looking statements in the Management's Discussion and Analysis of Financial Condition and Results of Operations and other portions of this Annual Report on Form 10-K that are subject to risks and uncertainties. These forward-looking statements include: statements of goals, intentions, earnings expectations, and other expectations; estimates of risks and of future costs and benefits; assessments of probable loan and lease losses; assessments of market risk; and statements of the ability to achieve financial and other goals. These forward-looking statements are subject to significant uncertainties because they are based upon or are affected by: management's estimates and projections of future interest rates, market behavior, and other economic conditions; future laws and regulations; and a variety of other matters which, by their nature, are subject to significant uncertainties. Because of these uncertainties, the Company's actual future results may differ materially from those indicated. In addition, the Company's past results of operations do not necessarily indicate its future results. Please also see the discussion of "Risk Factors" on page 68.

**SANDY SPRING BANCORP, INC.****FORM 10-K CROSS REFERENCE SHEET OF MATERIAL INCORPORATED BY REFERENCE**

The following table shows the location in this Annual Report on Form 10-K or the accompanying Proxy Statement of the information required to be disclosed by the United States Securities and Exchange Commission (“SEC”) Form 10-K. Where indicated below, information has been incorporated by reference in this Report from the Proxy Statement that accompanies it. Other portions of the Proxy Statement are not included in this Report. This Report is not part of the Proxy Statement. References are to pages in this report unless otherwise indicated.

	<b>Item of Form 10-K</b>	<b>Location</b>
<b>PART I</b>		
Item 1.	Business	“Forward-Looking Statements” on page 2, “Sandy Spring Bancorp, Inc.” and “About this Report” on page 4, and “Business” on pages 60 through 68.
Item 1A.	Risk Factors	“Forward-Looking Statements” on page 2, “Risk Factors” on pages 68 through 71.
Item 1B.	Unresolved Staff Comments	Not applicable.
Item 2.	Properties	“Properties” on pages 72 and 73.
Item 3.	Legal Proceedings	Note 19 “Litigation” on page 54.
Item 4.	Submission of Matters to a Vote of Security Holders	Not applicable. No matter was submitted to a vote of security holders during the fourth quarter of 2007.
<b>PART II</b>		
Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities	“Securities Listing, Prices, and Dividends” on page 6 “Equity Compensation Plans” on page 8.
Item 6.	Selected Financial Data	“Six Year Summary of Selected Financial Data” on page 5.
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	“Forward-Looking Statements” on page 2 and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” on pages 9 through 24.
Item 7A.	Quantitative and Qualitative Disclosures about Market Risk	“Forward-Looking Statements” on page 2 and “Market Risk Management” on pages 22 through 24.
Item 8.	Financial Statements and Supplementary Data	Pages 27 through 60.

Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	Not applicable.
Item 9A.	Controls and Procedures	“Controls and Procedures” on page 24.
Item 9B.	Other Information	Not applicable.
PART III		
Item 10.	Directors, Executive Officers and Corporate Governance	The material labeled “Election of Directors Information as to Nominees and Incumbent Directors,” “Corporate Governance,” “Code of Business Conduct,” “Compliance with Section 16(a) of the Securities Exchange Act of 1934,” “Shareholder Proposals and Communications,” and “Report of the Audit Committee” in the Proxy Statement is incorporated in this Report by reference. Information regarding executive officers is included under the caption “Executive Officers” on page 72 of this Report.
Item 11.	Executive Compensation	The material labeled "Corporate Governance and Other Matters," "Executive Compensation," and "Compensation Committee Report" in the Proxy Statement is incorporated in this Report by reference.
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	The material labeled “Owners of More than 5% of Bancorp’s Common Stock” and, "Stock Ownership of Directors and Executive Officers" in the Proxy Statement is incorporated in this Report by reference. Information regarding securities authorized for issuance under equity compensation plans is included under “Equity Compensation Plans” on page 8.
Item 13.	Certain Relationships and Related Transactions and Director Independence	The material labeled “Director Independence” and "Transactions and Relationships with Management" in the Proxy Statement is incorporated in this Report by reference.
Item 14.	Principal Accounting Fees and Services	The material labeled Audit and Non-Audit Fees in the Proxy Statement is incorporated in this Report by reference.

PART IV

Item 15.

Exhibits, Financial Statement Schedules “Exhibits, Financial Statement Schedules” on pages 74 through 75.

SIGNATURES

“Signatures” on page 76.

## **Sandy Spring Bancorp, Inc.**

With \$3.0 billion in assets, Sandy Spring Bancorp, Inc. is the holding company for Sandy Spring Bank and its principal subsidiaries, Sandy Spring Insurance Corporation, The Equipment Leasing Company, and West Financial Services, Inc. Sandy Spring Bancorp, Inc. is the second largest publicly traded banking company headquartered in Maryland. Sandy Spring Bank is a community banking organization that focuses its lending and other services on businesses and consumers in the local market area. Independent and community-oriented, Sandy Spring Bank was founded in 1868 and offers a broad range of commercial banking, retail banking, and trust services through 42 community offices in Anne Arundel, Carroll, Frederick, Howard, Montgomery, and Prince George's counties in Maryland, and Fairfax and Loudoun counties in Virginia. Through its subsidiaries, Sandy Spring Bank also offers a comprehensive menu of leasing, insurance, and investment management services. Visit [www.sandyspringbank.com](http://www.sandyspringbank.com) to locate an ATM near you or for more information about Sandy Spring Bank.

## **About This Report**

This report comprises the entire 2007 Form 10-K, other than exhibits, as filed with the SEC. The 2007 annual report to shareholders, included in this report, and the proxy materials for the 2008 annual meeting are being distributed together to shareholders. See page 75 for information regarding how to obtain copies of exhibits and additional copies of the Form 10-K.

This report is provided along with the annual proxy statement for convenience of use and to decrease costs, but is not part of the proxy materials.

**The SEC has not approved or disapproved this report or passed upon its accuracy or adequacy.**

**SIX YEAR SUMMARY OF SELECTED FINANCIAL DATA**

<i>(Dollars in thousands, except per share data)</i>	2007	2006	2005	2004	2003	2002
<b>Results of Operations:</b>						
Tax-equivalent interest income	\$ 186,481	\$ 159,686	\$ 129,288	\$ 117,137	\$ 120,285	\$ 129,300
Interest expense	76,149	58,687	33,982	34,768	37,432	44,100
Tax-equivalent net interest income	110,332	100,999	95,306	82,369	82,853	85,199
Tax-equivalent adjustment	5,506	6,243	7,128	8,156	8,237	6,900
Provision for loan and lease losses	4,094	2,795	2,600	0	0	2,800
Net interest income after provision for loan and lease losses	100,732	91,961	85,578	74,213	74,616	75,400
Noninterest income	44,289	38,895	36,909	30,949	33,969	29,900
Noninterest expenses	99,788	85,096	77,194	92,474	67,040	63,800
Income before taxes	45,233	45,760	45,293	12,688	41,545	41,500
Income tax expense (benefit)	12,971	12,889	12,195	(1,679)	9,479	10,900
Net income	32,262	32,871	33,098	14,367	32,066	30,500
Cash dividends	14,988	13,028	12,329	11,332	10,725	10,000
<b>Per Share Data:</b>						
Net income – basic	\$ 2.01	\$ 2.22	\$ 2.26	\$ 0.99	\$ 2.21	\$ 2.20
Net income – diluted	2.01	2.20	2.24	0.98	2.18	2.00
Dividends declared	0.92	0.88	0.84	0.78	0.74	0.60
Book value (at year end)	19.31	16.04	14.73	13.34	13.35	12.20
Tangible book value (at year end) <sup>(1)</sup>	13.60	14.48	13.09	12.16	12.03	10.70
<b>Financial Condition (at year end):</b>						
Assets	\$ 3,043,953	\$ 2,610,457	\$ 2,459,616	\$ 2,309,343	\$ 2,334,424	\$ 2,308,400
Deposits	2,273,868	1,994,223	1,803,210	1,732,501	1,561,830	1,492,200
Loans and leases	2,277,031	1,805,579	1,684,379	1,445,525	1,153,428	1,063,800
Securities	445,273	540,908	567,432	666,108	998,205	1,046,200
Borrowings	426,525	351,540	417,378	361,535	563,381	613,700
Stockholders' equity	315,640	237,777	217,883	195,083	193,449	178,000
<b>Financial Condition (average for the year):</b>						
Assets	2,935,451	2,563,673	2,352,061	2,406,318	2,344,743	2,161,600
Deposits	2,253,979	1,866,346	1,771,381	1,652,306	1,541,336	1,412,600
Loans and leases	2,113,476	1,788,702	1,544,990	1,292,209	1,103,279	1,056,800
Securities	495,928	559,350	603,882	906,901	1,059,583	931,100
Borrowings	361,884	451,251	355,537	536,758	593,684	571,000
Stockholders' equity	290,224	229,360	204,142	197,556	185,418	161,900
<b>Performance Ratios (for the year):</b>						
Return on average equity	11.12%	14.33%	16.21%	7.27%	17.29%	18.30%
Return on average assets	1.10	1.28	1.41	0.60	1.37	1.40
Yield on average interest-earning assets	6.98	6.73	5.95	5.23	5.49	6.30
Rate on average interest-bearing liabilities	3.50	3.08	2.02	1.94	2.08	2.50
Net interest spread	3.48	3.65	3.93	3.29	3.41	3.80
Net interest margin	4.13	4.26	4.39	3.68	3.78	4.20
Efficiency ratio – GAAP based <sup>(2)</sup>	66.92	63.67	61.71	87.93	61.74	58.90
Efficiency ratio – traditional <sup>(2)</sup>	61.92	58.71	58.16	62.86	56.26	54.00
Dividends declared per share to diluted net income per share	45.77	40.00	37.50	79.59	33.94	33.00
<b>Capital and Credit Quality Ratios:</b>						
Average equity to average assets	9.89%	8.95%	8.68%	8.21%	7.91%	7.40%



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Total risk-based capital ratio	<b>11.28</b>	13.62	13.22	13.82	15.51	14.9
Allowance for loan losses to loans and leases	<b>1.10</b>	1.08	1.00	1.01	1.29	1.4
Non-performing assets to total assets	<b>1.15</b>	0.15	0.06	0.08	0.13	0.1
Net charge-offs to average loans and leases	<b>0.06</b>	0.01	0.02	0.02	0.01	0.0

<sup>(1)</sup>Total stockholders' equity, net of goodwill and other intangible assets, divided by the number of shares of common stock outstanding at year end.

<sup>(2)</sup>See the discussion of the efficiency ratio in the section of Management's Discussion and Analysis of Financial Condition and Results of Operations entitled "Operating Expense Performance."

**SECURITIES LISTING, PRICES AND DIVIDENDS****Stock Listing**

Common shares of Sandy Spring Bancorp, Inc. are traded on the NASDAQ Global Select Market under the symbol SASR.

**Transfer Agent and Registrar**

American Stock Transfer and Trust Company  
59 Maiden Lane  
New York, New York 10038

**Recent Stock Prices and Dividends**

Shareholders received quarterly cash dividends totaling \$15.0 million in 2007 and \$13.0 million in 2006. Sandy Spring Bancorp, Inc. (the "Company") has increased its dividends per share each year for the past twenty-seven years. Since 2002, dividends per share have risen at a compound annual growth rate of 6%. The increase in dividends per share was 5% in 2007.

The ratio of dividends per share to diluted net income per share was 46% in 2007, compared to 40% for 2006. The dividend amount is established by the Board of Directors each quarter. In making its decision on dividends, the Board considers operating results, financial condition, capital adequacy, regulatory requirements, shareholder returns, and other factors.

Shares issued under the employee stock purchase plan, which commenced on July 1, 2001, totaled 25,147 in 2007 and 19,439 in 2006, while issuances pursuant to exercises of stock options and grants of restricted stock were 84,342 and 35,998 in the respective years. Shares issued under the director stock purchase plan totaled 2,402 shares in 2007 and 2,381 shares in 2006. Shares issued in connection with acquisitions totaled 1,577,036 in 2007.

The Company has a stock repurchase program that permits the repurchase of up to 5% (approximately 786,000 shares) of its outstanding common stock. Repurchases are made in connection with shares expected to be issued under the Company's stock option, benefit and compensation plans, as well as for other corporate purposes. A total of 1,332,869 shares have been repurchased since 1997, when stock repurchases began, through December 31, 2007 under the stock repurchase program. There were 156,249 shares repurchased in 2007 and 25,000 shares repurchased in 2006 under the stock repurchase program.

The number of common shareholders of record was approximately 2,800 as of February 7, 2008.

**Quarterly Stock Information**

Quarter	2007			2006		
	Stock Price Range		Per Share Dividend	Stock Price Range		Per Share Dividend
	Low	High		Low	High	
1 <sup>st</sup>	\$ 32.41	\$ 38.97	\$ 0.23	\$ 34.70	\$ 37.99	\$ 0.22
2 <sup>nd</sup>	30.98	35.94	0.23	33.98	37.54	0.22
3 <sup>rd</sup>	25.60	32.99	0.23	34.22	37.13	0.22
4 <sup>th</sup>	26.00	31.57	0.23	34.76	38.82	0.22
Total			\$ 0.92			\$ 0.88

**Issuer Purchases of Equity Securities**

Period	Total Number of	Average Price	Total Number of Shares	Maximum Number that
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	Shares Purchased <sup>(1)</sup>	Paid per Share	Purchased as Part of Publicly Announced Plans or Programs	May Yet Be Purchased Under the Plans or Programs <sup>(2)(3)</sup>
October 2007	39,195	\$ 28.69	39,195	692,212
November 2007	62,216	\$ 28.15	62,216	629,996
December 2007	0	N/A	0	629,996

<sup>(1)</sup>Includes purchases of the Company's stock made by or on behalf of the Company or any affiliated purchasers of the Company as defined in SEC Rule 10b-18.

<sup>(2)</sup> On March 28, 2007, the Company's board of directors approved a continuation of the stock repurchase program that permits the repurchase of up to 5%, or 786,245 shares, of its outstanding common stock. The current program continued a similar plan that expired on March 31, 2007. Repurchases under the program may be made on the open market and in privately negotiated transactions from time to time until March 31, 2009, or earlier termination of the program by the board. The repurchases are made in connection with shares expected to be issued under the Company's various benefit plans, as well as for other corporate purposes.

<sup>(3)</sup> Indicates the number of shares remaining under the plan at the end of the indicated month.

The following graph and table show the cumulative total return on the Common Stock of Bancorp over the last five years, compared with the cumulative total return of a broad stock market index (the Standard and Poor's 500 Index or "S&P 500"), a narrower index of Mid-Atlantic bank holding company peers with assets of \$1 billion to \$3 billion used in prior years ("Old Peer Group"), and a new index of Mid-Atlantic bank holding company peers with assets of \$2 billion to \$7 billion ("New Peer Group"). The decision to select the "New Peer Group" was made in keeping with the growth and geographic diversification experienced by the Company. The cumulative total return on the stock or the index equals the total increase in value since December 31, 2002, assuming reinvestment of all dividends paid into the stock or the index. The graph and table were prepared assuming that \$100 was invested on December 31, 2002, in the Common Stock and the securities included in the indexes.

#### Total Return Comparison

	2002	2003	2004	2005	2006	2007
<b>Sandy Spring Bancorp, Inc.</b>	<b>\$100.0</b>	<b>\$121.1</b>	<b>\$127.8</b>	<b>\$118.5</b>	<b>\$132.9</b>	<b>\$99.8</b>
<b>S&amp;P 500 Index</b>	<b>\$100.0</b>	<b>\$128.7</b>	<b>\$142.7</b>	<b>\$149.7</b>	<b>\$173.3</b>	<b>\$182.8</b>
<b>"Old Peer Group" Index</b>	<b>\$100.0</b>	<b>\$134.4</b>	<b>\$153.8</b>	<b>\$151.5</b>	<b>\$169.2</b>	<b>\$131.0</b>
<b>"New Peer Group" Index</b>	<b>\$100.0</b>	<b>\$129.1</b>	<b>\$152.1</b>	<b>\$140.0</b>	<b>\$150.5</b>	<b>\$119.9</b>

The "Old Peer Group" index includes twenty-four publicly-traded bank holding companies, other than Bancorp, headquartered in the states of Maryland, Virginia, Pennsylvania, New Jersey, and West Virginia (the Mid-Atlantic Region) with assets at December 31, 2007, of at least \$1 billion and not more than \$3 billion. The institutions included in this index are Burke & Herbert Bank & Trust Company; Cardinal Financial Company; City Holding Company; Center Bancorp, Inc.; Citizens & Northern Corporation; First Community Bancshares, Inc.; First Mariner Bancorp; First National Community Bancorp, Inc.; First United Corporation; FNB Corporation; Interchange Financial Services Corporation; Gateway Bank & Trust Co.; Lakeland Bancorp, Incorporated; Omega Financial Corp.; Peapack-Gladstone Financial Corporation; Pennsylvania Commerce Bancorp, Inc.; Royal Bancshares of Pennsylvania, Inc.; Summit Financial Group, Inc.; TowneBank; Union Bankshares Corporation; Univest Corporation of Pennsylvania; Virginia Commerce Bancorp, Inc.; Virginia Financial Group, Inc.; and Yardville National Bancorp. Returns are weighted according to the issuer's stock market capitalization at the beginning of each year shown.

The "New Peer Group" index includes twenty-one publicly traded bank holding companies, other than Bancorp, headquartered in the Mid-Atlantic Region as noted and with assets of \$2 billion to \$7 billion. The companies included in this index are: Carter Bank & Trust (VA); City Holding Company (WV); Pennsylvania Commerce Bancorp, Inc. (PA); First Bancorp, Inc. (NC); First Community Bancshares, Inc. (VA); First Charter Corporation (NC); First Commonwealth Financial Corporation (PA); First Financial Bancorp (OH); F.N.B. Corporation (PA); Harleysville National Corporation (PA); Lakeland Bancorp, Inc. (NJ); NewBridge Bancorp (NC); National Penn Bancshares, Inc. (PA); Provident Bankshares Corporation (MD); Park National Corporation (OH); Sun Bancorp, Inc. (NJ); S&T Bancorp, Inc. (PA); TowneBank (VA); Union Bankshares Corporation (VA); Virginia Commerce Bancorp, Inc. (VA); Wesbanco, Inc. (WV). Returns are weighted according to the issuer's stock market capitalization at the beginning of each year shown.

**Equity Compensation Plans**

The following table presents disclosure regarding equity compensation plans in existence at December 31, 2007, consisting only of the 1992 and 1999 stock option plans (each expired but with outstanding options that may still be exercised) and the 2005 Omnibus Stock Plan, each of which was approved by the shareholders.

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted average exercise price of outstanding options and warrants	Number of securities remaining available for future issuance under equity compensation plans excluding securities reflected in column
Equity compensation plans approved by security holders	996,365	\$33.72	1,365,708
Equity compensation plans not approved by security holders	0	0	0
Total	996,365	\$33.72	1,365,708

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### Overview

Sandy Spring Bancorp, Inc. and subsidiaries (the "Company") achieved solid earnings for the year ended December 31, 2007. Net income for the year ended December 31, 2007, totaled \$32.3 million (\$2.01 per diluted share), as compared to \$32.9 million (\$2.20 per diluted share) for the prior year. These results reflect the following events:

- An 11% increase in net interest income due primarily to continued growth in the loan portfolio, which was offset somewhat by a decrease in the net interest margin from 4.26% in 2006 to 4.13% in 2007.
- An increase in the provision for loan and lease losses to \$4.1 million in 2007 from \$2.8 million in 2006 due mainly to growth in the loan portfolio and a higher level of nonperforming loans.
- An increase of 14% in noninterest income over the prior year due in large part to increased service charges on deposit accounts and higher trust and investment management fees, offset by a decrease in gains on sales of mortgage loans.
- An increase of 17% in noninterest expenses compared to the prior year due primarily to an increase in salaries and employee benefits, occupancy expense, equipment expense and amortization of intangible assets reflecting the acquisitions of Potomac Bank of Virginia and County National Bank.

The Company maintained steady growth during 2007. Loan balances increased by 26% over the prior year primarily due to the acquisition of Potomac Bank of Virginia ("Potomac") and CN Bancorp, Inc. ("County") in 2007. Customer funding sources, which include deposits plus other short-term borrowings from core customers, increased 13% over 2006. Again, much of this increase was due to the two acquisitions.

Net interest income increased by \$10.0 million, or 11%, due primarily to growth in the loan portfolio and higher loan yields, which were offset, in part, by increased rates on interest bearing deposits. The net interest margin decreased from 4.26% for the year 2006 to 4.13% for the year 2007. Noninterest income increased by 14% to \$44.3 million compared to the prior year. This increase was due primarily to an increase of \$3.2 million in service charges on deposit accounts and an increase of \$0.8 million in trust and investment management fees, partially offset by a decrease of \$0.2 million in gains on sales of mortgage loans. Expressed as a percentage of net interest income and noninterest income, noninterest income totaled 30% of total revenue. Noninterest expenses grew by \$14.7 million or 17% versus the prior year primarily due to an increase of \$4.7 million in salaries and benefits resulting from the acquisitions of Potomac and County, an increase in occupancy and equipment expenses of \$3.0 million and growth of \$1.1 million in intangibles amortization as a result of the acquisitions mentioned above.

Comparing December 31, 2007 balances to December 31, 2006, total assets increased 17% to \$3.0 billion. Total deposits grew 14% to \$2.3 billion, while total loans and leases grew to \$2.3 billion from \$1.8 billion, a 26% increase. During the same period, stockholders' equity increased to \$315.6 million or 10% of total assets.

While non-performing assets grew substantially over the prior year, the Company continues to believe that its asset quality will prove to be a significant strength given the current volatile condition of the economy. Non-performing assets represented 1.15% of total assets at year-end 2007, versus 0.15% at year-end 2006. The ratio of net charge-offs to average loans and leases was 0.06% in 2007, compared to 0.01% in 2006.

### Critical Accounting Policies

The Company's consolidated financial statements are prepared in accordance with generally accepted accounting principles ("GAAP") in the United States of America and follow general practices within the industry in which it operates. Application of these principles requires management to make estimates, assumptions, and judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions, and judgments are based on information available as of the date of the financial statements; accordingly, as this

information changes, the financial statements may reflect different estimates, assumptions, and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions, and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions, and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the financial statements at fair value warrants an impairment write-down or valuation allowance to be established, or when an asset or liability must be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility.

The fair values and the information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or are provided by other third-party sources, when readily available.

The allowance for loan and lease losses is an estimate of the losses that may be sustained in the 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 they are probable of occurring and estimable, and (2) SFAS No. 114, “Accounting by Creditors for Impairment of a Loan,” which requires that losses be accrued when it is probable that the Company will not collect all principal and interest payments according to the loan’s or lease’s contractual terms.

Management believes that the allowance is adequate. However, its determination requires significant judgment, and estimates of probable losses in the loan and lease portfolio can vary significantly from the amounts actually observed. While management uses available information to recognize probable losses, future additions to the allowance may be necessary based on changes in the loans and leases comprising the portfolio and changes in the financial condition of borrowers, such as may result from changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, and independent consultants engaged by the Company, periodically review the loan and lease portfolio and the allowance. Such review may result in additional provisions based on their judgments of information available at the time of each examination.

The Company's allowance for loan and lease losses has two basic components: the formula allowance reflecting historical losses by loan category, as adjusted by several factors whose effects are not reflected in historical loss ratios, and specific allowances. Each of these components, and the systematic allowance methodology used to establish them, are described in detail in Note 1 of the Notes to the Consolidated Financial Statements. The amount of the allowance is reviewed monthly by the Senior Loan Committee, and reviewed and approved quarterly by the Board of Directors.

The portion of the allowance that is based upon historical loss factors, as adjusted, establishes allowances for the major loan categories based upon adjusted historical loss experience over the prior eight quarters, weighted so that losses realized in the most recent quarters have the greatest effect. The use of these historical loss factors is intended to reduce the differences between estimated losses inherent in the loan and lease portfolio and actual losses. The factors used to adjust the historical loss ratios address changes in the risk characteristics of the Company's loan and lease portfolio that are related to (1) trends in delinquencies and other non-performing loans, (2) changes in the risk level of the loan portfolio related to large loans, (3) changes in the categories of loans comprising the loan portfolio, (4) concentrations of loans to specific industry segments, (5) changes in economic conditions on both a local and national level, (6) changes in the Company's credit administration and loan and lease portfolio management processes, and (7) quality of the Company's credit risk identification processes. This component comprised 79% and 84% of the total allowance at December 31, 2007 and 2006, respectively.

The specific allowance is used primarily to establish allowances for risk-rated credits on an individual or portfolio basis, and accounted for 21% and 16% of the total allowance at December 31, 2007 and 2006, respectively. The Company has historically had favorable credit quality. The actual occurrence and severity of losses involving risk-rated credits can differ substantially from estimates, and some risk-rated credits may not be identified.



**Table 1 – Consolidated Average Balances, Yields and Rates<sup>(1)</sup>***(Dollars in thousands and tax equivalent)*

	2007			2006			2005		
	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate
<b>Assets</b>									
Loans and leases <sup>(2)</sup>									
Residential real estate <sup>(3)</sup>	\$ 586,141	\$ 37,441	6.39%	\$ 588,426	\$ 36,723	6.24%	\$ 550,129	\$ 31,628	5.75%
Consumer	365,334	25,367	6.94	344,316	23,172	6.73	323,534	17,856	5.52
Commercial loans and leases	1,162,001	90,730	7.81	855,960	66,657	7.79	671,327	46,151	6.87
Total loans and leases	2,113,476	153,538	7.26	1,788,702	126,552	7.08	1,544,990	95,635	6.19
Securities:									
Taxable	279,881	14,603	5.22	310,740	14,710	4.73	309,769	12,875	4.16
Nontaxable	216,047	15,060	6.97	248,610	17,220	6.93	294,113	19,996	6.80
Total securities	495,928	29,663	5.98	559,350	31,930	5.71	603,882	32,871	5.44
Interest-bearing deposits with banks	21,600	1,123	5.20	2,501	123	4.92	2,095	63	3.01
Federal funds sold	42,305	2,157	5.10	21,145	1,081	5.12	22,082	719	3.26
<b>Total earning assets</b>	<b>\$ 2,673,309</b>	<b>186,481</b>	<b>6.98%</b>	<b>\$ 2,371,698</b>	<b>159,686</b>	<b>6.73%</b>	<b>\$ 2,173,049</b>	<b>129,288</b>	<b>5.95%</b>
Less: allowances for loan and lease losses	(22,771)			(18,584)			(15,492)		
Cash and due from banks	54,294			46,741			46,682		
Premises and equipment, net	52,604			45,980			44,945		
Other assets	178,015			117,838			102,877		
<b>Total assets</b>	<b>\$ 2,935,451</b>			<b>\$ 2,563,673</b>			<b>\$ 2,352,061</b>		
<b>Liabilities and Stockholders' Equity:</b>									
Interest-bearing demand deposits	\$ 236,940	\$ 808	0.34%	\$ 226,699	\$ 657	0.29%	\$ 237,511	\$ 640	0.27%
Regular savings deposits	165,134	535	0.32	182,610	687	0.38	216,951	801	0.37
Money market savings deposits	643,047	23,809	3.70	409,578	12,655	3.09	376,090	6,268	1.67
Time deposits	768,005	34,764	4.53	631,712	25,335	4.01	498,774	13,773	2.76
Total interest-bearing deposits	1,813,126	59,916	3.30	1,450,599	39,334	2.71	1,329,326	21,482	1.62
	319,418	13,673	4.28	414,274	17,049	4.12	295,462	9,638	3.26

Short-term borrowings									
Long-term borrowings	<b>42,466</b>	<b>2,560</b>	<b>6.03</b>	36,977	2,304	6.23	60,075	2,862	4.76
<b>Total interest-bearing liabilities</b>	<b>2,175,010</b>	<b>76,149</b>	<b>3.50</b>	1,901,850	58,687	3.08	1,684,863	33,982	2.02
Net interest income and spread		<b>\$ 110,332</b>	<b>3.48%</b>		<b>\$ 100,999</b>	<b>3.65%</b>		<b>\$ 95,306</b>	<b>3.93%</b>
Noninterest-bearing demand deposits	<b>440,853</b>			415,747			442,055		
Other liabilities	<b>29,364</b>			16,716			21,001		
Stockholders' equity	<b>290,224</b>			229,360			204,142		
Total liabilities and stockholders' equity	<b>\$ 2,935,451</b>			\$ 2,563,673			\$ 2,352,061		
Interest income/earning assets			<b>6.98%</b>			<b>6.73%</b>			<b>5.95%</b>
Interest expense/earning assets			<b>2.85</b>			<b>2.47</b>			<b>1.56</b>
Net interest margin			<b>4.13%</b>			<b>4.26%</b>			<b>4.39%</b>

(1) Interest income includes the effects of taxable-equivalent adjustments (reduced by the nondeductible portion of interest expense) using the appropriate marginal federal income tax rate of 35.00% and, where applicable, the marginal state income tax rate of 6.55% (or a combined marginal federal and state rate of 39.26%) for 2007 and a marginal state income tax rate of 7.00% (or a combined federal and state rate of 39.55%) for 2006 and 2005, to increase tax-exempt interest income to a taxable-equivalent basis. The taxable-equivalent adjustment amounts utilized in the above table to compute yields totaled to \$5.5 million in 2007, \$6.2 million in 2006, and \$7.1 million in 2005.

(2) Non-accrual loans are included in the average balances.

(3) Includes residential mortgage loans held for sale. Home equity loans and lines are classified as consumer loans.

### Net Interest Income

The largest source of the Company's operating revenue is net interest income, which is the difference between the interest earned on interest-earning assets and the interest paid on interest-bearing liabilities.

Net interest income for 2007 was \$104.8 million, representing an increase of \$10.0 million or 11% from 2006. Comparing 2006 to 2005, net interest income increased 7% to \$94.8 million.

For purposes of this discussion and analysis, the interest earned on tax-exempt investment securities has been adjusted to an amount comparable to interest subject to normal income taxes. The result is referred to as tax-equivalent interest income and tax-equivalent net interest income.

The tabular analysis of net interest income performance (entitled "Table 1 - Consolidated Average Balances, Yields and Rates") shows a decrease in net interest margin for 2007 of 13 basis points, or 3% when compared to 2006. Comparing the years 2007 and 2006 shown in Table 1, average earning assets increased by 13%. Table 2 shows the extent to which interest income, interest expense and net interest income were affected by rate changes and volume changes. The decrease in tax-equivalent net interest margin in 2007 resulted primarily from the growth in the cost of interest bearing deposits reflecting the intense competition for deposits in the Company's markets and a flat yield curve environment. While average noninterest bearing deposits increased in 2007, due primarily to the acquisitions mentioned above, the percentage of noninterest bearing deposits to total deposits decreased to 20% in 2007 compared to 22% in 2006 and 25% in 2005. The decrease in the tax-equivalent net interest margin in 2006 resulted mainly from a decrease in the average balance of noninterest bearing deposits combined with a higher yield on interest bearing deposits due to the existing flat yield curve. Tax-equivalent net interest income increased by 9% in 2007 (to \$110.3 million in 2007 from \$101.0 million in 2006) and increased 6% in 2006 (from \$95.3 million in 2005). Pressure on the net interest margin in recent years has been an industry-wide trend and a significant challenge for management. It has led to greater sophistication in margin management and heightened emphasis on noninterest revenues. During 2007, margin compression continued as a result of a flat yield curve environment and intense competition for deposits among banks and other providers of financial services. The Company is continuing its emphasis on producing consistent earnings results from its core loan, deposit and noninterest income businesses.

**Table 2 – Effect of Volume and Rate Changes on Net Interest Income**

	2007 vs. 2006			2006 vs. 2005		
	Increase Or (Decrease)	Due to Change In Average:*		Increase Or (Decrease)	Due to Change In Average:*	
<i>(In thousands and tax equivalent)</i>		Volume	Rate		Volume	Rate
Interest income from earning assets:						
Loans and leases	\$ 26,986	\$ 23,515	\$ 3,471	\$ 30,916	\$ 16,217	\$ 14,699
Securities	(2,267)	(3,742)	1,475	(941)	(2,495)	1,554
Other investments	2,076	2,067	9	423	(18)	441
Total interest income	26,795	21,840	4,955	30,398	13,704	16,694
Interest expense on funding of earning assets:						
Interest-bearing demand deposits	151	30	121	17	(30)	47
Regular savings deposits	(152)	(62)	(90)	(114)	(129)	15
Money market savings deposits	11,154	8,276	2,878	6,387	603	5,784
Time deposits	9,429	5,906	3,523	11,562	4,287	7,275

Total borrowings	(3,120)	(3,976)	856	6,853	3,772	3,081
Total interest expense	17,462	10,174	7,288	24,705	8,503	16,202
Net interest income	\$ 9,333	\$ 11,666	\$ (2,333)	\$ 5,693	\$ 5,201	\$ 492

\* Where volume and rate have a combined effect that cannot be separately identified with either, the variance is allocated to volume and rate based on the relative size of the variance that can be separately identified with each.

### Interest Income

The Company's interest income increased by \$27.5 million or 18% in 2007, compared to 2006, preceded by an increase of \$31.3 million or 26% over 2005. On a tax-equivalent basis, the respective changes were an increase of 17% in 2007, and an increase of 24% in 2006. Table 2 shows that, in 2007, the increase in interest income resulted primarily from the higher growth in average earning assets over interest bearing liabilities which was somewhat offset by a narrowing net interest margin.

During 2007, average loans and leases, yielding 7.26% versus 7.08% a year earlier, grew 18% to \$2.1 billion, due mainly to a 36% increase in average commercial loans and leases. Average residential real estate loans decreased slightly (attributable to construction lending), average consumer loans increased 6% due to higher home equity loans and lines, while the increase in average commercial loans and leases reflected growth in all categories of such loans. In 2007, average loans and leases comprised 79% of average earning assets, compared to ratios of 75% in 2006 and 71% in 2005. Average total securities, yielding 5.98% in 2007 versus 5.71% last year, declined 11% to \$495.9 million. Non-taxable securities declined in 2007 by 15% compared to 2006. Average total securities comprised 19% of average earning assets in 2007, compared to 24% in 2006 and 28% in 2005. These results were consistent with the Company's strategic plan to migrate an increasing share of its assets from investment securities to its commercial loan portfolio.

### **Interest Expense**

Interest expense increased by 30% or \$17.5 million in 2007, compared to 2006, as a result of growth in interest-bearing deposits coupled with a 42 basis point rise in the average rate paid on deposits and borrowings (increasing to 3.50% from 3.08%).

Deposit and borrowing activity during 2007 was driven primarily by the flat yield curve rate environment which brought about an extremely competitive market for deposits as market interest rates on deposits remained relatively high through most of the year. Also contributing to this situation was the market volatility experienced in the second half of the year as other banks competing for deposits in the Company's markets increased rates offered on deposits to maintain their liquidity. The flat yield curve together with this intensely competitive market for deposits caused the Company to pay somewhat higher rates on interest bearing deposits in order to maintain its market share of such deposits. This resulted in an increase in average rates in several categories of interest-bearing liabilities. Average borrowings decreased \$89.3 million or 20% compared to 2006.

In 2006, interest expense increased principally due to a 106 basis point increase in the average rate paid on deposits and borrowings, due in large part, to the flat yield curve environment and a very competitive market for deposits.

### **Interest Rate Performance**

The net interest margin decreased by 13 basis points in 2007, as compared to a decrease in net interest spread of 17 basis points. The difference between these two indicators of interest rate performance is attributable primarily to an increase in the benefit of funding average earning assets from interest-free sources, which is reflected in the net interest margin. During 2007, the Company experienced a greater relative increase in the funding rate compared to the yield on earning assets, resulting in a decrease in the net interest margin and spread.

In 2006 versus 2005, a greater relative increase in the funding rate compared to the yield on earning assets resulted in a decrease in the net interest margin and spread.

### **Noninterest Income**

Total noninterest income was \$44.3 million in 2007, a \$5.4 million or 14% increase from 2006. The primary reasons for the increase in noninterest income for 2007, as compared to 2006 were a \$3.2 million increase in service charges on deposit accounts, due primarily to higher overdraft fees and a \$0.8 million increase in trust and investment management fees due to growth in assets under management. In addition, the Company experienced increases in income from bank owned life insurance of \$0.5 million, Visa check fees of \$0.4 million and other income of \$0.5 million. These increases were partially offset by a decrease in gains on sales of mortgage loans of \$0.2 million. Comparing 2006 to 2005, noninterest income increased \$2.0 million or 5%. This increase was mainly due to an increase in trust and investment management fees which resulted from the acquisition of West Financial Services late in 2005 and an increase in insurance agency commissions due, in part, to the acquisition of Neff & Associates in January 2006.

There were virtually no securities gains in 2007 or 2006 while the Company recognized net gains of \$3.3 million in 2005. During 2005, sales of available-for-sale securities generated \$4.0 million in gains and \$0.7 million in losses.

Service charges on deposits totaled \$11.1 million in 2007, an increase of \$3.2 million or 41% due primarily to higher overdraft fees. Visa check fees increased to \$2.8 million from \$2.4 million, an increase of \$0.4 million or 17% over 2006 due largely to an increased volume of electronic transactions.

Trust and investment management fee income amounted to \$9.6 million in 2007, an increase of \$0.8 million or 9% over 2006, reflecting increased assets under management. During 2007, investment management fees in West Financial Services increased to \$4.6 million, an increase of \$0.5 million or 11% over 2006 due to a revised fee structure and growth in assets under management. Trust services fees increased to \$5.0 million, an increase of \$0.3 million or 8% over the prior year due mainly to a 12% increase in assets under management. Trust and investment management fees of \$8.8 million for 2006 represented an increase of \$3.8 million or 75% over 2005. This increase was due primarily to the acquisition of West Financial Services in the fourth quarter of 2005. Fees on sales of investment products remained virtually level in 2007 compared to 2006 and increased by \$0.9 million or 40% in 2006 compared to 2005. The lack of growth in 2007 was due primarily to current uncertain economic conditions and eroding consumer confidence while the increase in 2006 reflects the emphasis on sales of mutual funds that pay trailer fees, thus providing an annuitized stream of revenue, instead of one-time fees payable at the time of sale. Total assets under management for West Financial Services, trust and investment services increased \$163.4 million or 10% to \$1.8 billion at December 31, 2007.

Insurance agency commissions increased by \$0.1 million or 2% in 2007 compared to 2006 after an increase of \$1.2 million or 22% in 2006 compared to 2005. The increase in 2006 was due to the acquisition of Neff & Associates in January 2006 together with higher commissions on commercial lines.

Gains on mortgage sales decreased by \$0.2 million or 8% in 2007 compared to 2006, after a decrease of 21% in 2006 compared to 2005. The Company achieved gains of \$2.7 million on sales of \$286.4 million in 2007 compared to \$3.0 million on sales of \$296.9 million in 2006 and gains of \$3.8 million on sales of \$326.0 million in 2005.

Income from bank owned life insurance reflected an increase of \$0.5 million or 20% in 2007 compared to 2006 and an increase of \$0.1 million or 4% from 2006 to 2005. The increase in 2007 was due primarily to higher rates and insurance policies added from the two acquisitions. The Company invests in bank owned life insurance products in order to better manage the cost of employee benefit plans. Investments totaled \$70.0 million at December 31, 2007 and were well diversified by carrier in accordance with defined policies and practices. The average tax-equivalent yield on these insurance contract assets was 7.02% for 2007.

### **Noninterest Expenses**

Noninterest expenses increased \$14.7 million or 17% in 2007, compared to 2006. The increase in expenses in 2007 was primarily due to a 9% increase in salaries and employee benefits and a 47% increase in other noninterest expenses. Comparing 2006 to 2005, noninterest expenses increased \$7.9 million or 10% due to a \$3.5 million or 7% increase in salaries and employees benefits.

Salaries and employee benefits, the largest component of noninterest expenses, increased \$4.7 million or 9% in 2007, primarily due to the acquisition of Potomac and County. This increase was somewhat offset by a \$0.5 million reduction due to the elimination of an executive medical benefit plan. Salaries and employee benefits increased \$3.5 million or 7% in 2006 due largely to an increase in salaries of \$3.3 million or 9%. This was due to the acquisition of West Financial Services in the fourth quarter of 2005 and Neff & Associates in January 2006 as well as a larger staff. Average full-time equivalent employees reached 709 in 2007, representing an increase of 13% from 626 in 2006, which was 6% above the 591 full-time equivalent employees in 2005.

In 2007, occupancy expense increased \$1.9 million or 22%. This increase was due to rent increases on existing properties and the addition of acquired branches. The rate of increase was \$0.4 million or 5% in 2006 over 2005 due to the opening of two new branches in 2006. Equipment expenses increased \$1.1 million or 20% in 2007 compared to 2006. This increase was due to mainly to the acquisitions. Marketing expense decreased by \$0.3 million or 13% in 2007 following an increase of \$1.4 million or 111% in 2006. The decrease in 2007 was due mainly to the Company's efforts to better control its noninterest expenses in 2007 while the increase in 2006 was part of the Company's decision to increase brand awareness within the markets that the Company serves.

Expenses for outside data services increased \$0.8 million or 24% in 2007 compared to 2006 due to the overall growth of the loan and deposit portfolios and the ten new branches added from the acquisitions of County and Potomac. Outside data services increased \$0.3 million or 9% in 2006 compared to 2005 due to growth in the loan and deposit portfolios.

Other noninterest expenses of \$17.4 million was \$5.5 million or 46% above the \$11.9 million recorded for 2006. This increase was due primarily to merger expenses of \$1.5 million. Higher consulting and professional fees, franchise taxes and an expense accrual for possible Visa, Inc. litigation costs also contributed to this increase. Other noninterest expenses increased \$1.5 million or 14% in 2006 compared to 2005 due mainly to an increase in consulting and professional fees.

Amortization of intangible assets increased \$1.1 million or 38% over 2006 as a result of the two acquisitions. The Company's intangible assets are being amortized over relatively short amortization periods averaging approximately

five years at December 31, 2007. Intangible assets arising from branch acquisitions were not classified as goodwill and continue to be amortized since the acquisitions did not meet the definition for business combinations.

In October 2007, Sandy Spring Bank, as a member of Visa U.S.A. Inc. ("Visa U.S.A."), received shares of restricted stock in Visa, Inc. ("Visa") as a result of its participation in the global restructuring of Visa U.S.A., Visa Canada Association, and Visa International Service Association in preparation for an initial public offering. On November 7, Visa announced that it had reached a settlement with American Express related to an antitrust lawsuit. Sandy Spring Bank and other Visa U.S.A. member banks are obligated to share in potential losses resulting from this and certain other litigation. In consideration of the announced American Express settlement, Sandy Spring Bank's proportionate membership share of Visa U.S.A., and accounting guidance provided by the SEC, the Company has recorded a liability and corresponding expense in the fourth quarter of \$0.2 million with respect to the American Express and certain other litigation with Visa U.S.A. The Company has not reflected in its financial statements any value for its membership interest in Visa as a result of the Visa reorganization. Upon completion of the anticipated IPO, the fair value of such interest will be realized based on the value of shares utilized to establish the escrow account (limited to the obligation recorded) and shares redeemed for cash. The Company expects the value of these shares to exceed the aggregate amount of this charge.



### Operating Expense Performance

Management views the efficiency ratio as an important measure of expense performance and cost management. The ratio expresses the level of noninterest expenses as a percentage of total revenue (net interest income plus total noninterest income). This is a GAAP financial measure. Lower ratios indicate improved productivity.

### Non-GAAP Financial Measure

The Company has for many years used a traditional efficiency ratio that is a non-GAAP financial measure of operating expense control and efficiency of operations. Management believes that its traditional ratio better focuses attention on the operating performance of the Company over time than does a GAAP based ratio, and is highly useful in comparing period-to-period operating performance of the Company's core business operations. It is used by management as part of its assessment of its performance in managing noninterest expenses. However, this measure is supplemental, and is not a substitute for an analysis of performance based on GAAP measures. The reader is cautioned that the traditional efficiency ratio used by the Company may not be comparable to GAAP or non-GAAP efficiency ratios reported by other financial institutions.

In general, the efficiency ratio is noninterest expenses as a percentage of net interest income plus noninterest income. Noninterest expenses used in the calculation of the traditional, non-GAAP efficiency ratio exclude the goodwill impairment loss in 2004, the amortization of intangibles, and non-recurring expenses. Income for the traditional ratio is increased for the favorable effect of tax-exempt income (see Table 1), and excludes securities gains and losses, which vary widely from period to period without appreciably affecting operating expenses, and non-recurring gains. The measure is different from the GAAP based efficiency ratio, which also is presented in this report. The GAAP based measure is calculated using noninterest expense and income amounts as shown on the face of the Consolidated Statements of Income. The GAAP and traditional based efficiency ratios are reconciled in Table 3. As shown in Table 3, both efficiency ratios, GAAP based and traditional, increased in 2007. This increase was mainly the result of the rise in noninterest expenses in 2007 over 2006 coupled with the decrease in the net interest margin from 4.26% in 2006 to 4.13% in 2007.

**Table 3 – GAAP based and traditional efficiency ratios**

<i>(In thousands)</i>	2007	2006	2005	2004	2003
Noninterest expenses – GAAP based	\$ 99,788	\$ 85,096	\$ 77,194	\$ 92,474	\$ 67,040
Net interest income plus noninterest income – GAAP based	149,115	133,651	125,087	105,162	108,585
Efficiency ratio – GAAP based	66.92%	63.67%	61.71%	87.93%	61.74%
Noninterest expenses – GAAP based	\$ 99,788	\$ 85,096	\$ 77,194	\$ 92,474	\$ 67,040
Less non-GAAP adjustments:					
Amortization of intangible assets	4,080	2,967	2,198	1,950	2,480
Goodwill impairment loss	0	0	0	1,265	0
FHLB prepayment penalties	0	0	0	18,363	0
Noninterest expenses – traditional ratio	\$ 95,708	\$ 82,129	\$ 74,996	\$ 70,896	\$ 64,560
Net interest income plus noninterest income – GAAP	149,115	133,651	125,087	105,162	108,585

based					
Plus non-GAAP adjustment:					
Tax-equivalency	<b>5,506</b>	6,243	7,128	8,156	8,237
Less non-GAAP adjustments:					
Securities gains	<b>43</b>	1	3,262	540	996
Income from early termination of a sublease	<b>0</b>	0	0	0	1,077
Net interest income plus noninterest Income – traditional ratio	<b>\$ 154,578</b>	\$ 139,893	\$ 128,953	\$ 112,778	\$ 114,749
Efficiency ratio – traditional	<b>61.92%</b>	58.71%	58.16%	62.86%	56.26%

### Provision for Income Taxes

The Company had an income tax expense of \$13.0 million in 2007, compared with an income tax expense of \$12.9 million in 2006 and \$12.2 million in 2005. The resulting effective tax rates were 29% for 2007, 28% for 2006, and 27% for 2005.

### **Balance Sheet Analysis**

The Company's total assets increased \$433.5 million to \$3.0 billion at December 31, 2007. Earning assets increased \$342.8 million to \$2.8 billion at December 31, 2007. These increases were mainly the result of the two acquisitions completed in 2007.

### **Loans and Leases**

Residential real estate loans, comprised of residential construction and permanent residential mortgage loans, increased \$81.0 million or 15%, during 2007 to \$623.3 million at December 31, 2007. Residential construction loans, a specialty of the Company for many years, increased to \$167.0 million in 2007, an increase of \$15.6 million or 10%. Permanent residential mortgages, most of which are 1-4 family, increased by \$65.4 million or 17%, to \$456.3 million.

Over the years, the Company's commercial loan clients have come to represent a diverse cross-section of small to mid-size local businesses, whose owners and employees are often established Bank customers. The Company's long-standing community roots and extensive experience in this market segment make it a natural growth area, while building and expanding such banking relationships are natural results of the Company's increased emphasis on client relationship management. The Company believes that its acquisitions during the past year reflect a natural extension of this philosophy.

Consistent with this strategy, the Company has targeted growth in the commercial loan portfolio as a central tenet of its long-term strategic plan. This involves a planned migration of assets from the investment portfolio to the commercial loan portfolio and emphasis on growth in related deposit accounts and other services such as investment management and insurance services.

Commercial loans and leases increased by \$358.9 million or 39% during 2007, to \$1.3 billion at December 31, 2007. Included in this category are commercial real estate loans, commercial construction loans, equipment leases and other commercial loans. The two acquisitions accounted for approximately 64% of the year-over-year commercial loan growth. Excluding the acquisitions, the commercial loan and lease portfolio increased 14% over the prior year.

In general, the Company's commercial real estate loans consist of owner occupied properties where an established banking relationship exists or, to a lesser extent, involve investment properties for warehouse, retail, and office space with a history of occupancy and cash flow. Commercial mortgages rose \$153.1 million or 30% during 2007, to \$662.8 million at year-end. Commercial construction loans grew \$70.2 million or 37% during the year, to \$262.8 million at December 31, 2007. The Company lends for commercial construction in markets it knows and understands, works selectively with local, top-quality builders and developers, and requires substantial equity from its borrowers. Other commercial loans increased \$133.9 million or 74% during 2007 to \$316.1 million at year-end. The increases noted above were primarily due to the Potomac and County acquisitions.

The Company's equipment leasing business provides leases for essential commercial equipment used by small to medium sized businesses. Equipment leasing is conducted through vendor relations and direct solicitation to end-users located primarily in states along the east coast from New Jersey to Florida. The typical lease is "small ticket" by industry standards, averaging less than \$100 thousand, with individual leases generally not exceeding \$500 thousand. The Company's equipment leasing business saw growth during 2007. The leasing portfolio grew \$1.6 million or 5% in 2007, to \$35.7 million at year-end.

Consumer lending continues to be very important to the Company's full-service, community banking business. This category of loans includes primarily home equity loans and lines of credit. The consumer loan portfolio increased 9% or \$31.5 million, to \$376.3 million at December 31, 2007. This growth was driven largely by an increase of \$37.0 million or 14% in home equity lines and loans during 2007 to \$308.5 million at year-end. This increase was primarily a result of the acquisitions and the Company's continuing strategy to place more emphasis on this product as part of a multi-product client relationship.

**Table 4 – Analysis of Loans and Leases**

This table presents the trends in the composition of the loan and lease portfolio over the previous five years.

<i>(In thousands)</i>	December 31,				
	2007	2006	2005	2004	2003
<b>Residential real estate:</b>					
Residential mortgages	\$ 456,305	\$ 390,852	\$ 413,324	\$ 371,924	\$ 331,129
Residential construction	166,981	151,399	155,379	137,880	88,500
<b>Commercial loans and leases:</b>					
Commercial real estate	662,837	509,726	415,983	386,911	323,099
Commercial construction	262,840	192,547	178,764	88,974	51,518
Leases	35,722	34,079	23,644	15,618	16,031
Other commercial	316,051	182,159	162,036	135,116	100,290
Consumer	376,295	344,817	335,249	309,102	242,861
<b>Total loans and leases</b>	<b>\$ 2,277,031</b>	<b>\$ 1,805,579</b>	<b>\$ 1,684,379</b>	<b>\$ 1,445,525</b>	<b>\$ 1,153,428</b>

**Table 5 – Loan Maturities and Interest Rate Sensitivity**

<i>(In thousands)</i>	At December 31, 2007			
	Remaining Maturities of Selected Credits in Years			
	1 or less	Over 1-5	Over 5	Total
Residential construction loans	\$ 72,122	\$ 94,843	\$ 16	\$ 166,981
Commercial construction loans	262,840	0	0	262,840
Commercial loans not secured by real estate	217,295	87,397	11,359	316,051
<b>Total</b>	<b>\$ 552,257</b>	<b>\$ 182,240</b>	<b>\$ 11,375</b>	<b>\$ 745,872</b>
<b>Rate Terms:</b>				
Fixed	\$ 38,434	\$ 76,356	\$ 11,359	\$ 126,149
Variable or adjustable	513,823	105,884	16	619,723
<b>Total</b>	<b>\$ 552,257</b>	<b>\$ 182,240</b>	<b>\$ 11,375</b>	<b>\$ 745,872</b>

**Securities**

The investment portfolio, consisting of available-for-sale, held-to-maturity and other equity securities, decreased 18% or \$95.6 million to \$445.3 million at December 31, 2007, from \$540.9 million at December 31, 2006. The investment portfolio declined due to the maturity of securities, which provided liquidity needed to fund loan growth in 2007.

As investments mature or are called, the proceeds will be reinvested to further reduce duration and interest rate risk by reducing the heavy concentration in municipal bonds and pledged agency securities into shorter duration agencies or MBS, whichever exhibits higher yields at a value price. These strategies will be executed with consideration given to interest rate trends and the structure of the yield curve with constant due diligence of economic projections and analysis.

**Table 6 – Analysis of Securities**

The composition of securities at December 31 for each of the latest three years was:

<i>(In thousands)</i>	2007	2006	2005
<b>Available-for-Sale: <sup>(1)</sup></b>			
U.S. Treasury	\$ 2,973	\$ 597	\$ 594
U.S. Agencies and Corporations	139,310	243,089	242,339
State and municipal	2,761	2,390	2,414
Mortgage-backed <sup>(2)</sup>	32,356	1,577	1,721
Corporate debt	0	0	0
Trust preferred	9,051	8,992	9,303
Marketable equity securities	350	200	200
<b>Total</b>	<b>186,801</b>	<b>256,845</b>	<b>256,571</b>
<b>Held-to-Maturity and Other Equity</b>			
U.S. Agencies and Corporations	34,419	34,408	34,398
State and municipal	199,427	232,936	261,250
Mortgage-backed <sup>(2)</sup>	860	0	0
Other equity securities	23,766	16,719	15,213
<b>Total</b>	<b>258,472</b>	<b>284,063</b>	<b>310,861</b>
<b>Total securities <sup>(3)</sup></b>	<b>\$ 445,273</b>	<b>\$ 540,908</b>	<b>\$ 567,432</b>

(1) At estimated fair value.

- (2) Issued by a U. S. Government Agency or secured by U.S. Government Agency collateral.
- (3) The outstanding balance of no single issuer, except for U.S. Government Agency securities, exceeded ten percent of stockholders' equity at December 31, 2007, 2006 or 2005.

Maturities and weighted average yields for debt securities available for sale and held to maturity at December 31, 2007 are presented in Table 7. Amounts appear in the table at amortized cost, without market value adjustments, by stated maturity adjusted for estimated calls.

**Table 7 – Maturity Table for Debt Securities at December 31, 2007**

<i>(In thousands)</i>	Years to Maturity									
	Within 1		Over 1 Through 5		Over 5 Through 10		Over 10		Total	Yield
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield		
<b>Debt Securities</b>										
<b>Available-for-Sale<sup>(1)</sup></b>										
U.S. Treasury	\$ 2,953	4.78%	\$ 0	0.00%	\$ 0	0.00%	\$ 0	0.00%	\$ 2,953	4.78%
U. S. Agencies and Corporations	136,821	4.64	2,236	5.51	0	0.00	0	0.00	139,057	4.66
State and municipal <sup>(2)</sup>	0	0.00	2,063	7.42	597	6.01	0	0.00	2,660	7.10
Mortgage-backed	3,074	5.56	23,908	5.08	5,178	5.74	0	0.00	32,160	5.23
Corporate debt	0	0.00	0	0.00	0	0.00	0	0.00	0	0.00
Trust preferred	3,104	9.41	4,783	9.23	0	0.00	0	0.00	7,887	9.30
<b>Total</b>	<b>\$ 145,952</b>	<b>4.77%</b>	<b>\$ 32,990</b>	<b>5.86%</b>	<b>\$ 5,775</b>	<b>5.77%</b>	<b>\$ 0</b>	<b>0.00%</b>	<b>\$ 184,717</b>	<b>4.99%</b>
<b>Debt Securities</b>										
<b>Held-to-Maturity<sup>(1)</sup></b>										
U. S. Agencies and Corporations	\$ 34,419	4.86%	\$ 0	0.00%	\$ 0	0.00%	\$ 0	0.00%	\$ 34,419	4.86%
State and municipal	45,551	6.93	136,356	7.04	11,155	6.64	6,365	7.29	199,427	7.00
Mortgage-backed	0	0.00	258	8.98	602	8.30	0		860	8.51
<b>Total</b>	<b>\$ 79,970</b>	<b>6.04%</b>	<b>\$ 136,614</b>	<b>7.04%</b>	<b>\$ 11,757</b>	<b>6.73%</b>	<b>\$ 6,365</b>	<b>7.29%</b>	<b>\$ 234,706</b>	<b>6.69%</b>

(1) At cost, adjusted for amortization and accretion of purchase premiums and discounts, respectively.

(2) Yields on state and municipal securities have been calculated on a tax-equivalent basis using the applicable federal income tax rate of 35%.

### Other Earning Assets

Residential mortgage loans held for sale decreased \$3.5 million to \$7.1 million as of December 31, 2007 from \$10.6 million as of December 31, 2006. Originations and sales of these loans and the resulting gains on sales decreased during 2007 due to relatively high short-term interest rates and volatile market conditions during much of the second half of the year.

The aggregate of federal funds sold and interest-bearing deposits with banks decreased \$29.5 million to \$22.4 million in 2007.

Bank owned life insurance increased \$9.9 million or 16% to \$69.9 million as of December 31, 2007 due to the increase in cash surrender value of the underlying policies and policies acquired with the acquisitions.

### Deposits and Borrowings

Total deposits were \$2.3 billion at December 31, 2007, increasing \$279.6 million or 14% from \$2.0 billion at December 31, 2006. Year-end balances for noninterest-bearing demand deposits, increased \$39.4 million or 10% over the prior year. For the same period, interest-bearing deposits grew \$240.2 million or 15%, attributable in large part to an increase in money market savings, which increased 40% (up \$208.5 million). In addition, demand deposits increased 9% (up \$21.0 million) and certificates of deposit increased by 2% (up \$16.8 million). These increases were somewhat offset by a decline in regular savings of 4% (down \$6.1 million). When deposits are combined with short-term borrowings from core customers, such growth in customer funding sources totaled 13% over the prior year.

Most of the growth in deposits mentioned above was due to the two acquisitions in 2007. Excluding the acquisitions, deposits grew 1% over 2006.

Total borrowings increased by \$75.0 million or 21% during 2007, to \$426.5 million at December 31, 2007, primarily to fund loan growth.

### **Capital Management**

Management monitors historical and projected earnings, dividends and asset growth, as well as risks associated with the various types of on- and off-balance sheet assets and liabilities, in order to determine appropriate capital levels. During 2007, total stockholders' equity increased 33% or \$77.8 million to \$315.6 million at December 31, 2007, from \$237.8 million at December 31, 2006.

External capital formation, resulting from stock issued for acquisitions, exercises of stock options, vesting of restricted stock and from stock issuances under the employee and director stock purchase plans totaled \$60.7 million during 2007. Share repurchases amounted to \$4.4 million over the same period, for a net increase in stockholders' equity from these sources of \$56.3 million. The ratio of average equity to average assets was 9.89% for 2007, as compared to 8.95% for 2006 and 8.68% for 2005. In addition, internal capital generation (net income less dividends) totaled \$17.3 million for the year.



Stockholders' equity was also affected by an increase of \$3.0 million in accumulated other comprehensive income (comprised of net unrealized gains and losses on available-for-sale securities after tax effects and an adjustment to reflect the curtailment of the Company's defined benefit pension plan, net of tax effect) from (\$4.0 million) at December 31, 2006 to (\$1.1 million) at December 31, 2007.

Bank holding companies and banks are required to maintain capital ratios in accordance with guidelines adopted by the federal bank regulators. These guidelines are commonly known as Risk-Based Capital guidelines. On December 31, 2007, the Company exceeded all applicable capital requirements, with a total risk-based capital ratio of 11.28%, a Tier 1 risk-based capital ratio of 10.28%, and a leverage ratio of 8.87%. Tier 1 capital of \$258.5 million and total qualifying capital of \$283.6 million each included \$35.0 million in trust preferred securities as permitted under Federal Reserve Guidelines (see "Note 11—Long-term Borrowings" of the Notes to the Consolidated Financial Statements). Trust preferred securities are considered regulatory capital for purposes of determining the Company's Tier 1 capital ratio. As of December 31, 2007, the Bank met the criteria for classification as a "well-capitalized" institution under the prompt corrective action rules of the Federal Deposit Insurance Act. Designation as a well-capitalized institution under these regulations is not a recommendation or endorsement of the Company or the Bank by federal bank regulators. Additional information regarding regulatory capital ratios is included in "Note 22—Regulatory Matters" of the Notes to the Consolidated Financial Statements.

### **Credit Risk Management**

The Company's loan and lease portfolio is subject to varying degrees of credit risk. Credit risk is mitigated through portfolio diversification, which limits exposure to any single customer, industry or collateral type. The Company maintains an allowance for loan and lease losses (the "allowance") to absorb estimated losses in the loan and lease portfolio. The allowance is based on consistent, continuous review and evaluation of the loan and lease portfolio, along with ongoing, quarterly assessments of the probable losses in that portfolio. The methodology for assessing the appropriateness of the allowance includes: (1) the formula allowance reflecting historical losses, as adjusted, by credit category, and (2) the specific allowance for risk-rated credits on an individual or portfolio basis. This systematic allowance methodology is further described in the section entitled "Critical Accounting Policies" and in "Note 1 - Significant Accounting Policies" of the Notes to the Consolidated Financial Statements. The amount of the allowance is reviewed monthly by the Senior Loan Committee, and reviewed and approved quarterly by the board of directors.

The allowance is increased by provisions for loan and lease losses, which are charged to expense. Charge-offs of loan and lease amounts determined by management to be uncollectible or impaired decrease the allowance, while recoveries of previous charge-offs are added back to the allowance. The Company makes provisions for loan and lease losses in amounts necessary to maintain the allowance at an appropriate level, as established by use of the allowance methodology. Provisions amounted to \$4.1 million in 2007, \$2.8 million in 2006 and \$2.6 million in 2005. Net charge-offs of \$1.3 million, \$0.2 million and \$0.4 million, were recorded in 2007, 2006 and 2005, respectively. The ratio of net charge-offs to average loans and leases was 0.06% in 2007, 0.01% in 2006 and 0.02% in 2005. At December 31, 2007, the allowance for loan and lease losses was \$25.1 million, or 1.10% of total loans and leases, compared to \$19.5 million, or 1.08% of total loans and leases, at December 31, 2006.

Management believes that the allowance is adequate. However, its determination requires significant judgment, and estimates of probable losses in the loan and lease portfolio can vary significantly from the amounts actually observed. While management uses available information to recognize probable losses, future additions to the allowance may be necessary based on changes in the credits comprising the portfolio and changes in the financial condition of borrowers, such as may result from changes in economic conditions. In addition, federal and state regulatory agencies, as an integral part of their examination process, and independent consultants engaged by the Bank, periodically review the loan and lease portfolio and the allowance. Such reviews may result in adjustments to the provision based upon their judgments of information available at the time of each examination.

Table 8 presents a five-year history for the allocation of the allowance, reflecting consistent use of the methodology outlined above, along with the credit mix (year-end loan and lease balances by category as a percent of total loans and leases). The allowance is allocated in the following table to various loan and lease categories based on the methodology used to estimate loan losses; however, the allocation does not restrict the usage of the allowance for any specific loan or lease category.

**Table 8 – Allowance for Loan and Lease Losses**

	2007		2006		December 31, 2005		2004		2003	
	Amount	% of Loans and Leases	Amount	% of Loans and Leases	Amount	% of Loans and Leases	Amount	% of Loans and Leases	Amount	% of Loans and Leases
<i>(In thousands)</i>										
Amount applicable to:										
Residential real estate:										
Residential mortgages	\$ 3,807	20%	\$ 2,411	22%	\$ 2,896	24%	\$ 2,571	26%	\$ 2,733	29%
Residential construction	1,639	7	1,616	8	1,754	9	1,520	10	681	8
Total	5,446	27	4,027	30	4,650	33	4,091	36	3,414	37
Commercial loans and leases:										
Commercial real estate	7,854	29	5,461	28	4,119	25	4,722	27	5,437	25
Commercial construction	4,092	12	2,197	11	2,152	11	834	6	553	4
Other commercial	5,317	14	4,857	10	2,587	10	1,918	9	2,338	12
Subtotal	17,263	55	12,515	49	8,858	46	7,474	42	8,328	41
Leases	525	2	364	2	298	1	128	1	283	1
Total	17,788	57	12,879	51	9,156	47	7,602	43	8,611	42
Consumer	1,858	16	2,586	19	3,080	20	2,961	21	2,029	21
Unallocated	0		0		0		0		826	
Total allowance	\$ 25,092		\$ 19,492		\$ 16,886		\$ 14,654		\$ 14,880	

During 2007, there were no changes in estimation methods or assumptions that affected the allowance methodology. Significant variation can occur over time in the methodology's assessment of the adequacy of the allowance as a result of the credit performance of a small number of borrowers. The unallocated allowance at year-end 2007, when measured against the total allowance, was 0%, as it was in 2006. The total allowance at December 31, 2007, was within the desirable range under the Company's policy guidelines derived from the allowance methodology.

The allowance increased by \$5.6 million or 29% during 2007, which was the amount of the provision for 2007 coupled with the allowance acquired from acquisitions less the net charge-offs for the year. The required allowance for commercial real estate and other commercial loans increased by \$4.7 million, reflective of the significant growth in loan balances as a result of the Company's emphasis on commercial lending and recent acquisitions. The required allowance for consumer and residential loans increased \$0.7 million during the year, mainly due to an increase in residential mortgage loans.

At December 31, 2007, total non-performing loans and leases were \$34.4 million, or 1.51% of total loans and leases, compared to \$3.7 million, or 0.21% of total loans and leases, at December 31, 2006. The increase in non-performing loans and leases was due primarily to two commercial construction loans totaling \$18.9 million which management

believes are adequately reserved and four commercial real estate loans totaling \$5.8 million which are well secured by collateral. The allowance represented 73% of non-performing loans and leases at December 31, 2007, compared to coverage of 522% a year earlier. Significant variation in the coverage ratio may occur from year to year because the amount of non-performing loans and leases depends largely on the condition of a small number of individual credits and borrowers relative to the total loan and lease portfolio. Other real estate owned totaled \$0.5 million at December 31, 2007 and was \$0.2 at December 31, 2006.

The balance of impaired loans was \$21.9 million at December 31, 2007, with reserves of \$0.9 million against those loans, compared to \$0.3 million at December 31, 2006, with reserves of \$0.1 million.

The Company's borrowers are concentrated in six counties in Maryland and two counties in Virginia. Commercial and residential mortgages, including home equity loans and lines, represented 63% of total loans and leases at December 31, 2007, compared to 65% at December 31, 2006. Historically, the Company has experienced low loss levels with respect to such loans through various economic cycles and conditions. Risk inherent in this loan concentration is mitigated by the nature of real estate collateral, the Company's substantial experience in most of the markets served, and its lending practices.

Certain loan terms may create concentrations of credit risk and increase the lender's exposure to loss. These include terms that permit the deferral of principal payments or payments that are smaller than normal interest accruals (negative amortization); loans with high loan-to-value ratios; loans, such as option adjustable-rate mortgages, that may expose the borrower to future increases in repayments that are in excess of increases that would result solely from increases in market interest rates; and interest-only loans. The Company does not make loans that provide for negative amortization. The Company originates option adjustable-rate mortgages infrequently and sells all of them in the secondary market.

At December 31, 2007, the Company had a total of \$40.7 million in residential real estate loans and \$2.2 million in consumer loans with a loan to value ratio (“LTV”) greater than 90%. The Company also had an additional \$91.3 million in residential lot loans owned by individuals with an LTV greater than 75%. Commercial loans, with an LTV greater than 75% to 85%, depending on the type of property, totaled \$49.9 million at December 31, 2007. The Company had interest-only loans totaling \$100.1 million in its loan portfolio at December 31, 2007. In addition, virtually all of the Company’s equity lines of credit, \$217.9 million at December 31, 2007, which were included in the consumer loan portfolio, were made on an interest-only basis. The aggregate of all loans with these terms was \$502.1 million at December 31, 2007 which represented 22% of total loans and leases outstanding at that date. The Company is of the opinion that its loan underwriting procedures are structured to adequately mitigate any additional risk that the above types of loans might present.

**Table 9 – Summary of Loan and Lease Loss Experience**

<i>(In thousands)</i>	Years Ended December 31,				
	2007	2006	2005	2004	2003
Balance of loan and lease loss					
Allowance, January 1,	\$ 19,492	\$ 16,886	\$ 14,654	\$ 14,880	\$ 15,036
Provision for loan and lease losses	4,094	2,795	2,600	0	0
Allowance acquired from acquisitions	2,798	0	0	0	0
Loan and lease charge-offs:					
Residential real estate	0	0	0	(109)	(148)
Commercial loans and leases	(1,103)	(230)	(491)	(173)	(122)
Consumer	(341)	(85)	(44)	(214)	(87)
Total charge-offs	(1,444)	(315)	(535)	(496)	(357)
Loan and lease recoveries:					
Residential real estate	12	0	64	54	126
Commercial loans and leases	110	89	89	169	63
Consumer	30	37	14	47	12
Total recoveries	152	126	167	270	201
Net charge-offs	(1,292)	(189)	(368)	(226)	(156)
Balance of loan and lease allowance, December 31	\$ 25,092	\$ 19,492	\$ 16,886	\$ 14,654	\$ 14,880
Net charge-offs to average loans and leases	0.06%	0.01%	0.02%	0.02%	0.01%
Allowance to total loans and leases	1.10%	1.08%	1.00%	1.01%	1.29%

**Table 10 – Analysis of Credit Risk**

<i>(In thousands)</i>	Years Ended December 31,				
	2007	2006	2005	2004	2003
Non-accrual loans and leases <sup>(1)</sup>	\$ 23,040	\$ 1,910	\$ 437	\$ 746	\$ 522

Loans and leases 90 days past due	<b>11,362</b>	1,823	958	1,043	2,333
Restructured loans and leases	<b>0</b>	0	0	0	0
Total non-performing loans and leases <sup>(2)</sup>	<b>34,402</b>	3,733	1,395	1,789	2,855
Other real estate owned, net	<b>461</b>	182	0	0	77
Total non-performing assets	<b>\$ 34,863</b>	\$ 3,915	\$ 1,395	\$ 1,789	\$ 2,932
Non-performing loans and leases to total loans and leases	<b>1.51%</b>	0.21%	0.08%	0.12%	0.25%
Allowance for loan and lease losses to non-performing loans and leases	<b>73%</b>	522%	1,210%	819%	521%
Non-performing assets to total assets	<b>1.15%</b>	0.15%	0.06%	0.08%	0.13%

<sup>(1)</sup> Gross interest income that would have been recorded in 2007 if non-accrual loans and leases shown above had been current and in accordance with their original terms was \$1.1 million, while interest actually recorded on such loans was \$0. Please see Note 1 of the Notes to Consolidated Financial Statements for a description of the Company's policy for placing loans on non-accrual status.

<sup>(2)</sup> Performing loans considered potential problem loans, as defined and identified by management, amounted to \$3.0 million at December 31, 2007. Although these are loans where known information about the borrowers' possible credit problems causes management to have doubts as to the borrowers' ability to comply with the loan repayment terms, most are well collateralized and are not believed to present significant risk of loss. Loans classified for regulatory purposes not included in either non-performing or potential problem loans consist only of "other loans especially mentioned" and do not, in management's opinion, represent or result from trends or uncertainties reasonably expected to materially impact future operating results, liquidity or capital resources, or represent material credits where known information about the borrowers' possible credit problems causes management to have doubts as to the borrowers' ability to comply with the loan repayment terms.

## **Market Risk Management**

The Company's net income is largely dependent on its net interest income. Net interest income is susceptible to interest rate risk to the extent that interest-bearing liabilities mature or re-price on a different basis than interest-earning assets. When interest-bearing liabilities mature or re-price more quickly than interest-earning assets in a given period, a significant increase in market rates of interest could adversely affect net interest income. Similarly, when interest-earning assets mature or re-price more quickly than interest-bearing liabilities, falling interest rates could result in a decrease in net interest income. Net interest income is also affected by changes in the portion of interest-earning assets that are funded by interest-bearing liabilities rather than by other sources of funds, such as noninterest-bearing deposits and stockholders' equity.

The Company's interest rate risk management goals are (1) to increase net interest income at a growth rate consistent with the growth rate of total assets, and (2) to minimize fluctuations in net interest margin as a percentage of earning assets. Management attempts to achieve these goals by balancing, within policy limits, the volume of floating-rate liabilities with a similar volume of floating-rate assets; by keeping the average maturity of fixed-rate asset and liability contracts reasonably matched; by maintaining a pool of administered core deposits; and by adjusting pricing rates to market conditions on a continuing basis.

The Company's board of directors has established a comprehensive interest rate risk management policy, which is administered by management's Asset Liability Management Committee ("ALCO"). The policy establishes limits of risk, which are quantitative measures of the percentage change in net interest income (a measure of net interest income at risk) and the fair value of equity capital (a measure of economic value of equity or "EVE" at risk) resulting from a hypothetical change in U.S. Treasury interest rates for maturities from one day to thirty years. The Company measures the potential adverse impacts that changing interest rates may have on its short-term earnings, long-term value, and liquidity by employing simulation analysis through the use of computer modeling. The simulation model captures optionality factors such as call features and interest rate caps and floors imbedded in investment and loan portfolio contracts. As with any method of gauging interest rate risk, there are certain shortcomings inherent in the interest rate modeling methodology used by the Company. When interest rates change, actual movements in different categories of interest-earning assets and interest-bearing liabilities, loan prepayments, and withdrawals of time and other deposits, may deviate significantly from assumptions used in the model. Finally, the methodology does not measure or reflect the impact that higher rates may have on adjustable-rate loan customers' ability to service their debts, or the impact of rate changes on demand for loan, lease, and deposit products.

The Company prepares a current base case and eight alternative simulations at least once a quarter, and reports the analysis to the board of directors. In addition, more frequent forecasts are produced when interest rates are particularly uncertain or when other business conditions so dictate.

The balance sheet is subject to quarterly testing for eight alternative interest rate shock possibilities to indicate the inherent interest rate risk. Average interest rates are shocked by +/- 100, 200, 300, and 400 basis points ("bp"), although the Company may elect not to use particular scenarios that it determines are impractical in a current rate environment. It is management's goal to structure the balance sheet so that net interest earnings at risk over a twelve-month period and the economic value of equity at risk do not exceed policy guidelines at the various interest rate shock levels.

The Company augments its quarterly interest rate shock analysis with alternative external interest rate scenarios on a monthly basis. These alternative interest rate scenarios may include non-parallel rate ramps and non-parallel yield curve twists. If a measure of risk produced by the alternative simulations of the entire balance sheet violates policy guidelines, ALCO is required to develop a plan to restore the measure of risk to a level that complies with policy limits within two quarters.

## **Analysis**

Measures of net interest income at risk produced by simulation analysis are indicators of an institution's short-term performance in alternative rate environments. These measures are typically based upon a relatively brief period, usually one year. They do not necessarily indicate the long-term prospects or economic value of the institution.

**Table 11 - Estimated Changes in Net Interest Income**

<b>CHANGE IN INTEREST RATES:</b>	<b>+400 bp</b>	<b>+300 bp</b>	<b>+200 bp</b>	<b>+100 bp</b>	<b>-100 bp</b>	<b>-200 bp</b>	<b>-300 bp</b>	<b>-400 bp</b>
<b>POLICY LIMIT</b>	<b>25%</b>	<b>20%</b>	<b>17.5%</b>	<b>12.5%</b>	<b>12.5%</b>	<b>17.5%</b>	<b>20%</b>	<b>25%</b>
December 2007	-14.82	-10.47	-6.12	-1.91	-0.68	-1.01	-2.84	N/A
December 2006	-13.67	-10.94	-7.68	-3.12	0.37	-2.27	-5.37	-9.87

As shown above, measures of net interest income at risk decreased from December 31, 2006 at all interest rate shock levels except the +400 bp and -100bp levels. All measures remained well within prescribed policy limits. Although assumed to be unlikely, our largest exposure is at the +400 bp level, with a measure of -14.82%. This is also within our prescribed policy limit of 25%. The sensitivity of net interest income indicated by this analysis is consistent with management's decision to position the balance sheet in anticipation of the declining interest rate cycle expected over the coming year.



The measures of equity value at risk indicate the ongoing economic value of the Company by considering the effects of changes in interest rates on all of the Company's cash flows, and discounting the cash flows to estimate the present value of assets and liabilities. The difference between these discounted values of the assets and liabilities is the economic value of equity, which, in theory, approximates the fair value of the Company's net assets.

**Table 12 - Estimated Changes in Economic Value of Equity (EVE)**

<b>CHANGE IN</b>								
<b>INTEREST RATES:</b>	<b>+400 bp</b>	<b>+300 bp</b>	<b>+200 bp</b>	<b>+100 bp</b>	<b>-100 bp</b>	<b>-200 bp</b>	<b>-300 bp</b>	<b>-400 bp</b>
<b>POLICY LIMIT</b>	<b>40%</b>	<b>30%</b>	<b>22.5%</b>	<b>10%</b>	<b>12.5%</b>	<b>22.5%</b>	<b>30%</b>	<b>40%</b>
December 2007	-15.40	-9.09	-1.44	3.14	-3.57	-9.01	-13.26	N/A
December 2006	-17.78	-13.07	-7.18	-1.67	-6.09	-14.95	-24.51	-35.53

Measures of the economic value of equity (EVE) at risk decreased over year-end 2006 in all interest rate shock levels. The major contributor to the decreased risk position was the increase in core deposits resulting from the Potomac and County acquisitions. The economic value of equity exposure at +200 bp is now -1.44% compared to -7.18% at year-end 2006, and is well within the policy limit of 22.5%, as are measures at all other shock levels.

### **Liquidity**

Liquidity is measured by a financial institution's ability to raise funds through loan and lease repayments, maturing investments, deposit growth, borrowed funds, capital and the sale of highly marketable assets such as investment securities and residential mortgage loans. The Company's liquidity position, considering both internal and external sources available, exceeded anticipated short-term and long-term needs at December 31, 2007. Management considers core deposits, defined to include all deposits other than time deposits of \$100 thousand or more, to be a relatively stable funding source. Core deposits equaled 72% of total earning assets at December 31, 2007. In addition, loan and lease payments, maturities, calls and pay downs of securities, deposit growth and earnings contribute a flow of funds available to meet liquidity requirements. In assessing liquidity, management considers operating requirements, the seasonality of deposit flows, investment, loan and deposit maturities and calls, expected funding of loans and deposit withdrawals, and the market values of available-for-sale investments, so that sufficient funds are available on short notice to meet obligations as they arise and to ensure that the Company is able to pursue new business opportunities.

Liquidity is measured using an approach designed to take into account, in addition to factors already discussed above, the Company's growth and mortgage banking activities. Also considered are changes in the liquidity of the investment portfolio due to fluctuations in interest rates. Under this approach, implemented by the Funds Management Subcommittee of ALCO under formal policy guidelines, the Company's liquidity position is measured weekly, looking forward at thirty day intervals from thirty (30) to one hundred eighty (180) days. The measurement is based upon the projection of funds sold or purchased position, along with ratios and trends developed to measure dependence on purchased funds and core growth. Resulting projections as of December 31, 2007, show short-term investments exceeding short-term borrowings by \$49.0 million over the subsequent 180 days. This projected excess of liquidity versus requirements provides the Company with flexibility in how it funds loans and other earning assets.

The Company also has external sources of funds, which can be drawn upon when required. The main source of external liquidity is an available line of credit for \$887.3 million with the Federal Home Loan Bank of Atlanta, of which \$649.2 million was available for borrowing based on pledged collateral, with \$293.5 million borrowed against it as of December 31, 2007. Other external sources of liquidity available to the Company in the form of lines of credit granted by the Federal Reserve and correspondent banks totaled \$140.8 million at December 31, 2007, against which there were no outstanding borrowings. In addition, the Company had an unsecured line of credit with a correspondent bank of \$20.0 million as of December 31, 2007. Based upon its liquidity analysis, including external sources of liquidity available, management believes the liquidity position is appropriate at December 31, 2007.

The Company's time deposits of \$100 thousand or more represented 12.65% of total deposits at December 31, 2007, and are shown by maturity in the table below.

<i>(In thousands)</i>	Months to Maturity				TOTAL
	3 or Less	Over 3 to 6	Over 6 To 12	Over 12	
Time deposits—\$100 thousand or more	\$ 51,114	\$ 123,122	\$ 85,015	\$ 28,474	\$ 287,725

The Company has various contractual obligations that affect its cash flows and liquidity. For information regarding material contractual obligations, please see “Market Risk Management” above, “Contractual Obligations” below, and “Note 7-Premises and Equipment,” “Note 11-Long-term Borrowings,” “Note 14-Pension, Profit Sharing and Other Employee Benefit Plans,” “Note 18-Financial Instruments with Off-balance Sheet Risk and Derivatives,” and “Note 20-Fair Value of Financial Instruments” of the Notes to the Consolidated Financial Statements.

### Off-Balance Sheet Arrangements

With the exception of the Company's obligations in connection with its trust preferred securities, irrevocable letters of credit, and loan commitments, the Company has no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on the Company's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources, that is material to investors. The trust preferred securities were issued by Sandy Spring Capital Trust II (the "Trust"), a subsidiary of the Company created for the purpose of issuing the trust preferred securities and purchasing the Company's junior subordinated debentures, which are its sole assets. These long-term borrowings bear a maturity date of October 7, 2034, which may be shortened, subject to conditions, to a date no earlier than October 7, 2009. The Company owns all of the Trust's outstanding securities. The Company and the Trust believe that, taken together, the Company's obligations under the junior subordinated debentures, the Indenture, the Trust Agreement, and the Guarantee entered into in connection with the issuance of the trust preferred securities and the debentures, in the aggregate constitute a full, irrevocable and unconditional guarantee of the Trust's obligations. For additional information on off-balance sheet arrangements, please see "Note 18-Financial Instruments with Off-balance Sheet Risk and Derivatives" and "Note 11-Long-term Borrowings" of the Notes to the Consolidated Financial Statements, and "Capital Management" and "Securities".

### Contractual Obligations

The Company enters into contractual obligations in the normal course of business. Among these obligations are long-term FHLB advances, operating leases related to branch and administrative facilities, a long-term contract with a data processing provider and purchase contracts related to construction of new branch offices. Payments required under these obligations, are set forth in the table below as of December 31, 2007.

<i>(In thousands)</i>	<b>Total</b>	Payment Due by Period			
		Less than 1 year	1-3 Years	3-5 Years	More than 5 Years
Long-term debt obligations	\$ 17,553	\$ 0	\$ 6,794	\$ 700	\$ 10,059
Operating lease obligations	32,649	4,712	9,799	8,207	9,931
Purchase obligations <sup>(1)</sup>	5,213	2,941	2,272	0	0
<b>Total</b>	<b>\$ 55,415</b>	<b>\$ 7,653</b>	<b>\$ 18,865</b>	<b>\$ 8,907</b>	<b>\$ 19,990</b>

<sup>(1)</sup>Represents payments required under contract, based on average monthly charges for 2007 and assuming a growth rate of 3%, with the Company's current data processing service provider that expires in September 2009.

## CONTROLS AND PROCEDURES

### Disclosure Controls and Procedures

As required by SEC rules, the Company's management evaluated the effectiveness of the Company's disclosure controls and procedures as of December 31, 2007. The Company's chief executive officer and chief financial officer participated in the evaluation. Based on this evaluation, the Company's chief executive officer and chief financial officer concluded that the Company's disclosure controls and procedures were effective as of December 31, 2007.

### Internal Control Over Financial Reporting

#### Management's Report on Internal Control Over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting. As required by SEC rules, the Company's management evaluated the effectiveness of the Company's internal control over financial reporting as of December 31, 2007. The Company's chief executive officer and chief financial officer participated in the evaluation, which was based upon the criteria for effective internal control over financial

reporting included in the “Internal Control-Integrated Framework” issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, the Company’s chief executive officer and chief financial officer concluded that the Company’s internal control over financial reporting was effective as of December 31, 2007.

The attestation report by the Company’s independent registered public accounting firm, McGladrey & Pullen, LLP, on the Company’s internal control over financial reporting begins on the following page.

**Fourth Quarter 2007 Changes In Internal Controls Over Financial Reporting**

No change occurred during the fourth quarter of 2007 that has materially affected, or is reasonably likely to materially affect, the Company’s internal controls over financial reporting.

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

To the Board of Directors and Stockholders  
Sandy Spring Bancorp, Inc.

We have audited Sandy Spring Bancorp, Inc. and Subsidiaries' (the "Company") internal control over financial reporting as of December 31, 2007, based on the criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Sandy Spring Bancorp, Inc. and Subsidiaries' management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal controls over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Sandy Spring Bancorp, Inc. and Subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007 based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO").

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets as of December 31, 2007 and 2006, and the related consolidated statements of income, changes in stockholders' equity and cash flows for each of the three years in the period ended December 31, 2007 of Sandy Spring Bancorp, Inc. and Subsidiaries and our report dated February 29, 2008 expressed an unqualified opinion thereon.

Frederick, Maryland  
February 29, 2008



**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Stockholders  
Sandy Spring Bancorp, Inc.

We have audited the accompanying consolidated balance sheets of Sandy Spring Bancorp, Inc. and Subsidiaries as of December 31, 2007 and 2006, and the related consolidated statements of income, changes in stockholders' equity and cash flows for each of the three years in the period ended December 31, 2007. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provided a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sandy Spring Bancorp, Inc. and Subsidiaries as of December 31, 2007 and 2006, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2007 in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1 to the consolidated financial statements, in 2006 Sandy Spring Bancorp, Inc. and Subsidiaries adopted Statement of Financial Accounting Standards No. 123R, "Share-Based Payment," Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" and Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements in the Current Year Financial Statements."

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Sandy Spring Bancorp, Inc. and Subsidiaries' internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") and our report dated February 29, 2008 expressed an unqualified opinion on the effectiveness of Sandy Spring Bancorp, Inc. and Subsidiaries internal control over financial reporting.

Frederick, Maryland  
February 29, 2008

**SANDY SPRING BANCORP, INC. AND SUBSIDIARIES**  
**CONSOLIDATED BALANCE SHEETS**

(In thousands, except per share data)

	December 31,	
	2007	2006
<b>Assets</b>		
Cash and due from banks	\$ 63,432	\$ 54,945
Federal funds sold	22,055	48,978
Cash and cash equivalents	85,487	103,923
Interest-bearing deposits with banks	365	2,974
Residential mortgage loans held for sale	7,089	10,595
Investments available for sale (at fair value)	186,801	256,845
Investments held to maturity – fair value of \$240,995 (2007) and \$273,206 (2006)	234,706	267,344
Other equity securities	23,766	16,719
Total loans and leases	2,277,031	1,805,579
Less: allowance for loan and lease losses	(25,092)	(19,492)
Net loans and leases	2,251,939	1,786,087
Premises and equipment, net	54,457	47,756
Accrued interest receivable	14,955	15,200
Goodwill	76,585	12,494
Other intangible assets, net	16,630	10,653
Other assets	91,173	79,867
Total assets	\$ 3,043,953	\$ 2,610,457
<b>Liabilities</b>		
Noninterest-bearing deposits	\$ 434,053	\$ 394,662
Interest-bearing deposits	1,839,815	1,599,561
Total deposits	2,273,868	1,994,223
Short-term borrowings	373,972	314,732
Other long-term borrowings	17,553	1,808
Subordinated debentures	35,000	35,000
Accrued interest payable and other liabilities	27,920	26,917
Total liabilities	2,728,313	2,372,680
Commitments and contingencies (Notes 2, 7, 10, 11, 18 and 19)		
<b>Stockholders' Equity</b>		
Common stock-par value \$1.00; shares authorized 50,000,000; shares issued and outstanding 16,349,317 (2007) and 14,826,805 (2006)	16,349	14,827
Additional paid in capital	83,970	27,869
Retained earnings	216,376	199,102
Accumulated other comprehensive income (loss)	(1,055)	(4,021)
Total stockholders' equity	315,640	237,777
Total liabilities and stockholders' equity	\$ 3,043,953	\$ 2,610,457



*See Notes to Consolidated Financial Statements.*

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**SANDY SPRING BANCORP, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME**

(In thousands, except per share data)

	Years Ended December 31,		
	2007	2006	2005
<b>Interest income:</b>			
Interest and fees on loans and leases	\$ 152,723	\$ 125,813	\$ 94,562
Interest on loans held for sale	815	739	1,073
Interest on deposits with banks	1,123	123	63
<b>Interest and dividends on securities:</b>			
Taxable	13,989	14,132	12,327
Exempt from federal income taxes	10,168	11,555	13,416
Interest on federal funds sold	2,157	1,081	719
<b>Total interest income</b>	<b>180,975</b>	<b>153,443</b>	<b>122,160</b>
<b>Interest expense:</b>			
Interest on deposits	59,916	39,334	21,482
Interest on short-term borrowings	13,673	17,049	9,638
Interest on long-term borrowings	2,560	2,304	2,862
<b>Total interest expense</b>	<b>76,149</b>	<b>58,687</b>	<b>33,982</b>
<b>Net interest income</b>	<b>104,826</b>	<b>94,756</b>	<b>88,178</b>
Provision for loan and lease losses	4,094	2,795	2,600
<b>Net interest income after provision for loan and lease losses</b>	<b>100,732</b>	<b>91,961</b>	<b>85,578</b>
<b>Noninterest income:</b>			
Securities gains	43	1	3,262
Service charges on deposit accounts	11,148	7,903	7,688
Gains on sales of mortgage loans	2,739	2,978	3,757
Fees on sales of investment products	2,989	2,960	2,109
Trust and investment management fees	9,588	8,762	5,006
Insurance agency commissions	6,625	6,477	5,309
Income from bank owned life insurance	2,829	2,350	2,259
Visa check fees	2,784	2,381	2,167
Other income	5,544	5,083	5,352
<b>Total noninterest income</b>	<b>44,289</b>	<b>38,895</b>	<b>36,909</b>
<b>Noninterest expenses:</b>			
Salaries and employee benefits	55,207	50,518	47,013
Occupancy expense of premises	10,360	8,493	8,053
Equipment expenses	6,563	5,476	5,410
Marketing	2,237	2,583	1,225
Outside data services	3,967	3,203	2,940
Amortization of intangible assets	4,080	2,967	2,198
Other expenses	17,374	11,856	10,355
<b>Total noninterest expenses</b>	<b>99,788</b>	<b>85,096</b>	<b>77,194</b>
<b>Income before income taxes</b>	<b>45,233</b>	<b>45,760</b>	<b>45,293</b>
<b>Income tax expense</b>	<b>12,971</b>	<b>12,889</b>	<b>12,195</b>
<b>Net income</b>	<b>\$ 32,262</b>	<b>\$ 32,871</b>	<b>\$ 33,098</b>
<b>Basic net income per share</b>	<b>\$ 2.01</b>	<b>\$ 2.22</b>	<b>\$ 2.26</b>
<b>Diluted net income per share</b>	<b>\$ 2.01</b>	<b>\$ 2.20</b>	<b>\$ 2.24</b>
<b>Dividends declared per share</b>	<b>\$ 0.92</b>	<b>\$ 0.88</b>	<b>\$ 0.84</b>

*See Notes to Consolidated Financials Statements*

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**SANDY SPRING BANCORP, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

<i>(In thousands)</i>	Years Ended December 31,		
	2007	2006	2005
Cash flows from operating activities:			
Net income	\$ 32,262	\$ 32,871	\$ 33,098
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	10,648	8,859	6,836
Provision for loan and lease losses	4,094	2,795	2,600
Stock option expense	1,128	624	0
Deferred income taxes (benefits)	(2,721)	(986)	(2,755)
Origination of loans held for sale	(280,152)	(294,027)	(316,494)
Proceeds from sales of loans held for sale	286,398	296,916	326,022
Gains on sales of loans	(2,739)	(2,978)	(3,757)
Securities gains	(43)	(1)	(3,262)
Gains on sales of premises and equipment	(289)	0	(21)
Net decrease (increase) in accrued interest receivable	2,020	(2,056)	(1,470)
Net (increase) decrease in other assets	(4,931)	(3,913)	854
Net increase (decrease) in accrued interest payable and other liabilities	(2,913)	5,485	(354)
Other-net	1,078	(530)	1,078
Net cash provided by operating activities	43,840	43,059	42,375
Cash flows from investing activities:			
Net decrease (increase) in interest-bearing deposits with banks	2,609	(2,223)	(141)
Purchases of other equity securities	(4,548)	(1,506)	(1,301)
Purchases of investments available for sale	(83,440)	(94,984)	(107,244)
Proceeds from sales of investments available for sale	0	0	124,311
Proceeds from maturities, calls and principal payments of investments held to maturity	36,038	27,936	9,137
Proceeds from maturities, calls and principal payments of investments available for sale	208,555	95,396	70,978
Proceeds from sales of other real estate owned	(179)	0	108
Proceeds from sales of premises and equipment	650	0	0
Net increase in loans and leases receivable	(176,880)	(187,389)	(238,927)
Purchase of loans and leases	0	(2,148)	0
Proceeds from sale of loans and leases	0	68,087	0
Acquisition of business activity, net	(15,729)	(1,900)	(890)
Expenditures for premises and equipment	(4,780)	(6,674)	(8,442)
Net cash (used in) investing activities	(37,704)	(105,405)	(152,411)
Cash flows from financing activities:			
Net (decrease) increase in deposits	(57,031)	191,013	70,709
Net increase (decrease) in short-term borrowings	39,932	(65,838)	80,843
Net increase (decrease) in long-term borrowings	9,936	0	(25,000)
Common stock purchased and retired	(4,354)	(866)	(1,437)
Proceeds from issuance of common stock	1,823	1,424	1,498
Tax benefit from stock options exercised	110	121	0
Dividends paid	(14,988)	(13,028)	(12,329)

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Net cash provided by (used in) by financing activities	<b>(24,572)</b>		112,826		114,284
Net (decrease) increase in cash and cash equivalents	<b>(18,436)</b>		50,480		4,248
Cash and cash equivalents at beginning of year	<b>103,923</b>		53,443		49,195
Cash and cash equivalents at end of year	<b>\$ 85,487</b>	<b>\$</b>	103,923	<b>\$</b>	53,443
Supplemental Disclosures:					
Interest payments	<b>\$ 76,000</b>	<b>\$</b>	57,535	<b>\$</b>	33,638
Income tax payments	<b>14,149</b>		10,400		13,070
Non-cash Investing and Financing Activities:					
Transfers from loans to other real estate owned	<b>\$ 90</b>	<b>\$</b>	182	<b>\$</b>	73
Reclassification of borrowings from long-term to short-term	<b>808</b>		350		67,450
Details of acquisition:					
Fair value of assets acquired	<b>\$ 417,434</b>	<b>\$</b>	297	<b>\$</b>	939
Fair value of liabilities assumed	<b>(365,709)</b>		(287)		(1,275)
Stock issued for acquisition	<b>(58,916)</b>		0		(5,043)
Purchase price in excess of net assets acquired	<b>62,600</b>		1,890		6,269
Cash paid for acquisitions	<b>55,409</b>		1,900		890
Cash and cash equivalents acquired with acquisitions	<b>39,680</b>		0		0
Acquisition of business activity, net	<b>\$ 15,729</b>	<b>\$</b>	1,900	<b>\$</b>	890

*See Notes to Consolidated Financial Statements.*

**SANDY SPRING BANCORP, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**

(Dollars in thousands, except per share data)

	Common Stock	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income(Loss)	Total Stockholders' Equity
Balances at December 31, 2004	\$ 14,629	\$ 21,522	\$ 156,315	\$ 2,617	\$ 195,083
Comprehensive Income:					
Net income			33,098		33,098
Other comprehensive income (loss), net of tax effects of \$2,044 (unrealized losses on securities of \$1,993, adjusted for a reclassification adjustment for gains of \$3,262)				(3,211)	(3,211)
Total comprehensive income					29,887
Cash dividends-\$0.84 per share			(12,329)		(12,329)
Stock repurchases-45,500 shares	(46)	(1,391)			(1,437)
Common stock issued pursuant to:					
Stock option plan-42,478 shares	42	950			992
Employee stock purchase plan-21,272 shares	21	567			588
Director Stock Purchase Plan-1,693 shares	2	54			56
Acquisition of West Financial Services, Inc.					
145,534 shares	146	4,897			5,043
Balances at December 31, 2005, as previously reported	14,794	26,599	177,084	(594)	217,883
Adjustment to reflect adoption of SAB 108 effective January 1, 2006			2,175		2,175
Balance as of January 1, 2006 following adoption of SAB 108	14,794	26,599	179,259	(594)	220,058
Comprehensive Income:					
Net income			32,871		32,871
Other comprehensive income (loss), net of tax effects of \$243 (unrealized gains on securities of \$619, adjusted for a reclassification adjustment for gains of \$1)				375	375
Total comprehensive income					33,246
Cash dividends - \$0.88 per share			(13,028)		(13,028)
Stock Compensation expense		624			624
Stock repurchases - 25,000 shares	(25)	(841)			(866)
Common stock issued pursuant to:					
Stock option plan - 35,998 shares	36	824			860
Employee stock purchase plan - 19,439 shares	19	582			601
	3	81			84

Director Stock Purchase Plan - 2,381  
shares

Adjustment to initially apply FASB Statement No. 158, net of tax effects of \$2,487				(3,802)	(3,802)
Balances at December 31, 2006	14,827	27,869	199,102	(4,021)	237,777
<b>Comprehensive Income:</b>					
Net income			<b>32,262</b>		<b>32,262</b>
<b>Other comprehensive income (loss):</b>					
Unrealized gains on securities of \$2,141, adjusted for a reclassification adjustment for gains of \$43, net of tax effects of \$837				<b>1,261</b>	<b>1,261</b>
Change in funded status of defined benefit pension, net of tax effects of \$1,095				<b>1,705</b>	<b>1,705</b>
Total comprehensive income					<b>35,228</b>
Cash dividends - \$0.92 per share			<b>(14,988)</b>		<b>(14,988)</b>
Stock compensation expense		<b>1,128</b>			<b>1,128</b>
Stock repurchases - 156,249 shares	<b>(156)</b>	<b>(4,198)</b>			<b>(4,354)</b>
<b>Common stock issued pursuant to:</b>					
Acquisition of Potomac Bank - 886,989 shares	<b>887</b>	<b>32,190</b>			<b>33,077</b>
Acquisition of CN Bancorp, Inc - 690,047 shares	<b>690</b>	<b>25,149</b>			<b>25,839</b>
Stock option plan - 68,098 shares (78,264 shares issued less 10,166 shares retired)	<b>68</b>	<b>1,095</b>			<b>1,163</b>
Director Stock Purchase Plan - 2,402 shares	<b>2</b>	<b>75</b>			<b>77</b>
Employee Stock Purchase Plan - 25,147 shares	<b>25</b>	<b>662</b>			<b>687</b>
Restricted Stock - 6,078 shares	<b>6</b>				<b>6</b>
Balances at December 31, 2007	<b>\$ 16,349</b>	<b>\$ 83,970</b>	<b>\$ 216,376</b>	<b>\$(1,055)</b>	<b>\$ 315,640</b>

*See Notes to Consolidated Financial Statements.*

**SANDY SPRING BANCORP, INC. AND SUBSIDIARIES**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1 – Significant Accounting Policies**

The accounting and reporting policies of the Company, which include Sandy Spring Bancorp, Inc. and its wholly-owned subsidiary, Sandy Spring Bank (the "Bank"), together with the Bank's subsidiaries, Sandy Spring Insurance Corporation, The Equipment Leasing Company, and West Financial Services, Inc., conform to accounting principles generally accepted in the United States and to general practice within the financial services industry.

**Nature of Operations**

Through its subsidiary bank, the Company conducts a full-service commercial banking, mortgage banking and trust business. Services to individuals and businesses include accepting deposits, extending real estate, consumer and commercial loans and lines of credit, equipment leasing, general insurance, personal trust, and investment and wealth management services. The Company operates in the six Maryland counties of Anne Arundel, Carroll, Frederick, Howard, Montgomery, and Prince George's, and in Fairfax and Loudoun counties in Virginia. The Company offers investment and wealth management services through the Bank's subsidiary, West Financial Services Inc., located in McLean, Virginia. Insurance products are available to clients through Chesapeake Insurance Group, Wolfe & Reichelt, and Neff & Associates, which are agencies of Sandy Spring Insurance Corporation. The Equipment Leasing Company provides leasing for primarily technology-based equipment for retail businesses.

**Policy for Consolidation**

The consolidated financial statements include the accounts of Sandy Spring Bancorp, Inc. and the Bank. Consolidation has resulted in the elimination of all significant inter-company balances and transactions. The financial statements of Sandy Spring Bancorp, Inc. (Parent Only) include its investment in the Bank under the equity method of accounting.

**Use of Estimates**

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Assets Under Management**

Assets held for others under fiduciary and agency relationships are not included in the accompanying balance sheets since they are not assets of the Company or its subsidiaries. Trust department income and investment management fees are presented on an accrual basis.

**Cash Flows**

For purposes of reporting cash flows, cash and cash equivalents include cash and due from banks and federal funds sold (items with an original maturity of three months or less).

**Residential Mortgage Loans Held for Sale**

The Company engages in sales of residential mortgage loans originated by the Bank. Loans held for sale are carried at the lower of aggregate cost or fair value. Fair value is derived from secondary market quotations for similar instruments. Gains and losses on sales of these loans are recorded as a component of noninterest income in the Consolidated Statements of Income. The Company's current practice is to sell such loans on a servicing released basis.

During 2006, the Company sold \$68.6 million in residential mortgage loans from its loan portfolio on a servicing retained basis. The Company has recorded an intangible asset for the value of such servicing totaling \$0.4 million and \$0.6 million at December 31, 2007 and 2006, respectively.



Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. Purchased servicing rights are capitalized at the cost to acquire the rights. For sales of mortgage loans, a portion of the cost of originating the loan is allocated to the servicing right based on relative fair value. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses. Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights into tranches based on predominant characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that fair value is less than the capitalized amount for the tranches. If the Company later determines that all or a portion of the impairment no longer exists for a particular tranche, a reduction of the allowance may be recorded as an increase to income. Capitalized servicing rights are reported in other assets and are amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets.

Servicing fee income is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal and are recorded as income when earned. The amortization of mortgage servicing rights is netted against loan servicing fee income.

### **Derivative Financial Instruments**

#### **Derivative Loan Commitments**

Mortgage loan commitments are referred to as derivative loan commitments if the loan that will result from exercise of the commitment will be held for sale upon funding. Loan commitments that are derivatives are recognized at fair value on the consolidated balance sheet in other assets or other liabilities with changes in their fair values recorded in net gain on sale of loans.

The Company records a zero value for the loan commitment at inception (at the time the commitment is issued to a borrower (“the time of rate lock”), consistent with EITF 02-3, *Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities*, and SEC Staff Accounting Bulletin No. 105, *Application of Accounting Principles to Loan Commitments*, and, accordingly, does not recognize the value of the expected normal servicing rights until the underlying loan is sold. Subsequent to inception, changes in the fair value of the loan commitment are recognized based on changes in the fair value of the underlying mortgage loan due to interest rate changes, changes in the probability the derivative loan commitment will be exercised, and the passage of time. In estimating fair value, the Company assigns a probability to a loan commitment based on an expectation that it will be exercised and the loan will be funded.

#### **Forward Loan Sale Commitments**

The Company carefully evaluates all loan sales agreements to determine whether they meet the definition of a derivative under SFAS No. 133 as facts and circumstances may differ significantly. If agreements qualify, to protect against the price risk inherent in derivative loan commitments, the Company utilizes both “mandatory delivery” and “best efforts” forward loan sale commitments to mitigate the risk of potential decreases in the values of loans that would result from the exercise of the derivative loan commitments. Mandatory delivery contracts are accounted for as derivative instruments. Generally, the Company’s best efforts contracts also meet the definition of derivative instruments after the loan to the borrower has closed. Accordingly, forward loan sale commitments that economically hedge the closed loan inventory are recognized at fair value on the consolidated balance sheet in other assets and other liabilities with changes in their fair values recorded in net gain on sale of loans. The Company estimates the fair value of its forward loan sales commitments using a methodology similar to that used for derivative loan commitments.

#### **Interest Rate Swap Agreements**

Beginning in 2007, the Company entered into interest rate swaps (“swaps”) to facilitate customer transactions and meet their financing needs. The swaps are reported at fair value in other assets or other liabilities. The accounting for changes in the fair value of a swap depends on whether it has been designated and qualifies as part of a hedging relationship. The Company's swaps qualify as derivatives, but are not designated as hedging instruments, thus any gain or loss resulting from changes in the fair value is recognized in current net income. Further discussion of the Company's financial derivatives is set forth in Footnote 18 to the consolidated financial statements.

### **Investments Held to Maturity and Other Equity Securities**

Investments held to maturity are those securities which the Company has the ability and positive intent to hold until maturity. Securities so classified at the time of purchase are recorded at cost. The carrying values of securities held to maturity are adjusted for premium amortization to the earlier of the maturity or expected call date and discount accretion to the maturity date. Related interest and dividends are included in interest income. Declines in the fair value of individual held-to-maturity securities below their cost that are other than temporary result in write-downs of the individual securities to their fair value. Factors affecting the determination of whether an other-than-temporary impairment has occurred include a downgrading of the security by the rating agency, a significant deterioration in the

financial condition of the issuer, or that management would not have the ability to hold a security for a period of time sufficient to allow for any anticipated recovery in fair value. Other equity securities represent Federal Reserve Bank, Federal Home Loan Bank of Atlanta stock and Atlantic Central Banker's Bank stock which are considered restricted as to marketability and are recorded at cost.

**Investments Available for Sale**

Marketable equity securities and debt securities not classified as held to maturity or trading are classified as available for sale. Securities available for sale are acquired as part of the Company's asset/liability management strategy and may be sold in response to changes in interest rates, loan demand, changes in prepayment risk and other factors. Securities available for sale are carried at fair value, with unrealized gains or losses based on the difference between amortized cost and fair value, reported net of deferred tax, as accumulated other comprehensive income (loss), a separate component of stockholders' equity. The carrying values of securities available for sale are adjusted for premium amortization to the earlier of the maturity or expected call date and discount accretion to the maturity date. Realized gains and losses, using the specific identification method, are included as a separate component of noninterest income. Related interest and dividends are included in interest income. Declines in the fair value of individual available-for-sale securities below their cost that are other than temporary result in write-downs of the individual securities to their fair value. Factors affecting the determination of whether an other-than-temporary impairment has occurred include a downgrading of the security by a rating agency, a significant deterioration in the financial condition of the issuer, or that management would not have the intent and ability to hold a security for a period of time sufficient to allow for any anticipated recovery in fair value.

### **Loans and Leases**

Loans are stated at their principal balance outstanding net of any deferred fees and costs. Interest income on loans is accrued at the contractual rate based on the principal outstanding. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method. Lease financing assets, all of which are direct financing leases, include aggregate lease rentals, net of related unearned income. Leasing income is recognized on a basis that achieves a constant periodic rate of return on the outstanding lease financing balances over the lease terms. The Company generally places loans and leases, except for consumer loans, on non-accrual when any portion of the principal or interest is ninety days past due and collateral is insufficient to discharge the debt in full. Interest accrual may also be discontinued earlier if, in management's opinion, collection is unlikely. Generally, consumer installment loans are not placed on non-accrual, but are charged off when they are five months past due. All interest accrued but not collected for loans that are placed on non-accrual or charged-off is reversed against interest income. Interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual status. Loans are returned to accrual status when all principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Loans are considered impaired when, based on current information, it is probable that the Company will not collect all principal and interest payments according to contractual terms. Generally, loans are considered impaired once principal and interest payments are past due and they are placed on non-accrual. Management also considers the financial condition of the borrower, cash flows of the loan and the value of the related collateral. Impaired loans do not include large groups of smaller balance homogeneous credits such as residential real estate, consumer installment loans, and commercial leases, which are evaluated collectively for impairment. Loans specifically reviewed for impairment are not considered impaired during periods of "minimal delay" in payment (usually ninety days or less) provided eventual collection of all amounts due is expected. The impairment of a loan is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or the fair value of the collateral if repayment is expected to be provided by the collateral. Generally, the Company measures impairment on such loans by reference to the fair value of the collateral. Income on impaired loans is recognized similar to the method followed on nonaccrual loans.

### **Allowance for Loan and Lease Losses**

The allowance for loan and lease losses ("allowance") represents an amount which, in management's judgment, is adequate to absorb estimated losses on outstanding loans and leases. The allowance represents an estimation made pursuant to Statement of Financial Accounting Standards ("SFAS") No. 5, "Accounting for Contingencies," and SFAS No. 114, "Accounting by Creditors for Impairment of a Loan." The adequacy of the allowance is determined through careful and continuous evaluation of the loan and lease portfolio, and involves consideration of a number of factors, as outlined below, to establish a prudent level. Determination of the allowance is inherently subjective and requires significant estimates, including estimated losses on pools of homogeneous loans based on historical loss experience and consideration of current economic trends, which may be susceptible to significant change. Loans and leases deemed uncollectible are charged against the allowance, while recoveries are credited to the allowance. Management adjusts the level of the allowance through the provision for loan and lease losses, which is recorded as a current period operating expense. The Company's systematic methodology for assessing the appropriateness of the allowance includes: (1) the formula allowance reflecting historical losses, as adjusted, by credit category, and (2) the specific allowance for risk-rated credits on an individual or portfolio basis.

The formula allowance is based upon historical loss factors, as adjusted, and establishes allowances for the major loan categories based upon adjusted historical loss experience over the prior eight quarters, weighted so that losses realized in the most recent quarters have the greatest effect. The factors used to adjust the historical loss experience address various risk characteristics of the Company's loan portfolio including: (1) trends in delinquencies and other non-performing loans, (2) changes in the risk profile related to large loans in the portfolio, (3) changes in the categories of loans comprising the loan portfolio, (4) concentrations of loans to specific industry segments, (5) changes in economic conditions on both a local and national level, (6) changes in the Company's credit administration

and loan portfolio management processes, and (7) quality of the Company's credit risk identification processes.

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The specific allowance is used to allocate an allowance for internally risk-rated commercial loans where significant conditions or circumstances indicate that a loss may be imminent. Analysis resulting in specific allowances, including those on loans identified for evaluation of impairment, includes consideration of the borrower's overall financial condition, resources and payment record, support available from financial guarantors and the sufficiency of collateral. These factors are combined to estimate the probability and severity of potential losses. Then a specific allowance is established based on the Company's calculation of the potential loss imbedded in the individual loan. Allowances are also established by application of credit risk factors to other internally risk-rated loans, individual consumer and residential loans and commercial leases having reached non-accrual or 90-day past due status. Each risk rating category is assigned a credit risk factor based on management's estimate of the associated risk, complexity, and size of the individual loans within the category. Additional allowances may also be established in special circumstances involving a particular group of credits or portfolio within a risk category when management becomes aware that losses incurred may exceed those determined by application of the risk factor alone.

### **Premises and Equipment**

Premises and equipment are stated at cost, less accumulated depreciation and amortization, computed using the straight-line method. Premises and equipment are depreciated over the useful lives of the assets, which generally range from 3 to 10 years for furniture, fixtures and equipment, 3 to 5 years for computer software and hardware, and 10 to 40 years for buildings and building improvements. Leasehold improvements are amortized over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter. The costs of major renewals and betterments are capitalized, while the costs of ordinary maintenance and repairs are included in noninterest expense.

### **Other Real Estate Owned (OREO)**

OREO, which is included in other assets in the consolidated balance sheets, is comprised of properties acquired in partial or total satisfaction of problem loans. The properties are recorded at fair value less estimated costs of disposal, on the date acquired. Losses arising at the time of acquisition of such properties are charged against the allowance for loan and lease losses. Subsequent write-downs that may be required are added to a valuation reserve. Gains and losses realized from the sale of OREO, as well as valuation adjustments, are included in noninterest income. Expenses of operation are included in noninterest expense.

### **Goodwill and Other Intangible Assets**

Goodwill represents the excess of the cost of an acquisition over the fair value of the net assets acquired. Other intangible assets represent purchased assets that also lack physical substance but can be distinguished from goodwill because of contractual or other legal rights or because the asset is capable of being sold or exchanged either on its own or in combination with a related contract, asset, or liability. Under the provisions of Statement of Financial Accounting Standards ("SFAS") No. 142, "*Goodwill and Other Intangible Assets*", goodwill is not amortized over an estimated life, but rather is tested at least annually for impairment. Prior to adoption of SFAS No. 142, the Company's goodwill was amortized on a straight-line basis over varying periods not exceeding 10 years.

Intangible assets that have finite lives are amortized over their estimated useful lives and also continue to be subject to impairment testing. All of the Company's other intangible assets have finite lives and are being amortized on a straight-line basis over varying periods that initially did not exceed 15 years.

Note 8 includes a summary of the Company's goodwill and other intangible assets. The unidentifiable Intangible Assets Resulting from Branch Acquisitions resulted from two transactions: the purchase of a commercial bank in 1996 and the purchase of seven commercial bank branches in a single transaction in 1999. No goodwill was recorded as a result of these branch acquisitions. SFAS No. 147, "*Acquisitions of Certain Financial Institutions*" addresses unidentifiable intangible assets resulting from acquisitions of entire or less-than-whole financial institutions where the fair value of liabilities assumed exceeds the fair value of tangible and identifiable intangible assets acquired. The Statement provides for the recognition of goodwill where the transaction in which an unidentifiable intangible asset

arose was a business combination. The transitional provisions of SFAS No. 147 allow for the reclassification of unidentifiable intangible assets that meet certain criteria to goodwill and the restatement of earnings for any amortization of the reclassified goodwill that occurred since SFAS No. 142 was adopted. After completing its analysis of the transactions identified above, the Company determined that neither met the definition of a business for purposes of SFAS No. 147 under EITF 98-3, "*Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business.*" Accordingly, the Company has continued to amortize these unidentifiable intangible assets without change in method.

#### **Valuation of Long-Lived Assets**

The Company accounts for the valuation of long-lived assets under Statement of Financial Accounting Standards (SFAS) No. 144, "*Accounting for the Impairment or Disposal of Long-Lived Assets.*" SFAS No. 144 requires that long-lived assets and certain identifiable intangible assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of the long-lived asset is measured by a comparison of the carrying amount of the asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. Assets to be disposed of are reportable at the lower of the carrying amount or the fair value, less costs to sell.

### **Transfers of Financial Assets**

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

### **Insurance Commissions and Fees**

Commission revenue is recognized the date the customer is billed. The Company also receives contingent commissions from insurance companies as additional incentive for achieving specified premium volume goals and/or the loss experience of the insurance placed by the Company. Contingent commissions from insurance companies are recognized when determinable, which is generally when such commissions are received.

### **Advertising Costs**

Advertising costs are expensed as incurred and included in noninterest expenses.

### **Earnings per Common Share**

Basic earnings per share is derived by dividing net income available to common stockholders by the weighted-average number of common shares outstanding, and does not include the impact of any potentially dilutive common stock equivalents. The diluted earnings per share is derived by dividing net income by the weighted-average number of shares outstanding, adjusted for the dilutive effect of outstanding stock options as well as any adjustment to income that would result from the assumed issuance. The number of potential shares issued pursuant to the stock option plans was determined using the treasury stock method.

### **Income Taxes**

Income tax expense is based on the results of operations, adjusted for permanent differences between items of income or expense reported in the financial statements and those reported for tax purposes. Deferred income tax assets and liabilities are determined using the liability method. Under the liability method, deferred income taxes are determined based on the differences between the financial statement carrying amounts and the income tax bases of assets and liabilities and are measured at the enacted tax rates that will be in effect when these differences reverse.

### **Adopted Accounting Pronouncements**

In December 2004, the FASB issued SFAS No. 123 (revised), "Share-Based Payment" ("SFAS 123(R)"). SFAS 123(R) replaces SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"), and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). SFAS 123(R) requires compensation costs related to share-based payment transactions to be recognized in the financial statements over the period that an employee provides services in exchange for the award. Compensation cost is measured based on the fair value of the equity or liability instruments issued. The Company adopted SFAS 123R effective January 1, 2006, using the modified prospective method. Under the modified prospective method, the Company records compensation cost for new and modified awards, measured using the fair value of the award on the grant dates, over the related vesting period of such awards prospectively. Compensation cost related to any non-vested portion of awards outstanding as of that date, if any, would be based on the grant-date fair value as calculated under the original provisions of SFAS No. 123 since the Company was not required to re-measure any non-vested awards.

Effective January 1, 2006, the Company adopted the provisions of SFAS 123(R) thereby expensing employee stock-based compensation using the fair value method prospectively for all awards granted, modified, settled, or vesting on or after January 1, 2006. The fair value at date of grant of the stock option is estimated using a binomial pricing model. Prior to January 1, 2006, the Company, as permitted under SFAS 123, applied the intrinsic value recognition and measurement principles of APB 25, and related interpretations in accounting for its stock-based compensation plans. Therefore, no stock-based employee compensation cost was reflected in net income, as all



options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

In May 2005, the FASB issued Statement No. 154, (“SFAS No. 154”), “*Accounting Changes and Error Corrections -A Replacement of APB Opinion No. 20 and FASB Statement No. 3.*” Among other things, SFAS No. 154 requires that a voluntary change in accounting principle be applied retroactively with all prior period financial statements presented on the new accounting principle, unless it is impractical to do so. SFAS No. 154 also provides that (1) a change in method of depreciating or amortizing a long-lived nonfinancial asset be accounted for as a change in estimate (prospectively) that was effected by a change in accounting principle, and (2) correction of errors in previously issued financial statements should be termed a “restatement”. The new standard was effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The adoption of this Statement did not have a material impact on the Company’s financial position, results of operations or cash flows.

In February 2006, FASB issued SFAS 155, "*Accounting for Certain Hybrid Financial Instruments*", which permits, but does not require, fair value accounting for any hybrid financial instrument that contains an embedded derivative that would otherwise require bifurcation in accordance with SFAS 133, "*Accounting for Derivative Instruments and Hedging Activities*". The statement also subjects beneficial interests in securitized financial assets to the requirements of SFAS 133. This statement is effective for all financial instruments acquired, issued, or subject to re-measurement for fiscal years beginning after September 15, 2006. The adoption of this Statement did not have a material impact on the Company's financial position, results of operations or cash flows.

In March 2006, the FASB issued SFAS No. 156, "*Accounting for Servicing of Financial Assets, and an amendment of FASB Statement No. 140.*" The statement amends SFAS No. 140 by (1) requiring the separate accounting for servicing assets and servicing liabilities, which arise from the sale of financial assets; (2) requiring all separately recognized serving assets and servicing liabilities to be initially measured at fair value, if practicable; and (3) permitting an entity to choose between an amortization method or a fair value method for subsequent measurement for each class of separately recognized servicing assets and servicing liabilities. This statement is effective for fiscal years beginning after September 15, 2006, with earlier adoption permitted. The adoption of this Statement did not have a material impact on the Company's financial position, results of operations or cash flows.

In June 2006, the FASB issued FASB Interpretation No. 48 ("FIN 48"), "*Accounting for Uncertainty in Income Taxes.*" This interpretation applies to all tax positions accounted for in accordance with SFAS No. 109, "*Accounting for Income Taxes.*" FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109. 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. In addition, the Statement provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition for tax positions. This interpretation is effective for fiscal years beginning after December 15, 2006, with earlier adoption permitted. The adoption of this Statement did not have a material impact on the Company's financial position, results of operations or cash flows.

In June 2006, the EITF released Issue 06-05, "*Accounting for Purchases of Life Insurance-Determining the Amount That Could Be Realized in Accordance with FASB Technical Bulletin No. 85-4, 'Accounting for Purchases of Life Insurance'*". On September 7, 2006, the EITF concluded that a policyholder should consider any additional amounts included in the contractual terms of the policy in determining the amount that could be realized under the insurance contract. Amounts that are recoverable by the policyholder at the discretion of the insurance company should be excluded from the amount that could be realized. Amounts that are recoverable by the policyholder in periods beyond one year from the surrender of the policy should be discounted utilizing an appropriate rate of interest. The effective date of EITF 06-05 is for fiscal years beginning after December 15, 2006. The adoption of this Statement did not have a material impact on the Company's financial position, results of operations or cash flows.

In September 2006, the FASB issued Statement No. 158, ("SFAS No. 158"), "*Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88, 106 and 132(R).*" SFAS No. 158 requires a company that sponsors a postretirement benefit plan to fully recognize, as an asset or liability, the over-funded or under-funded status of its benefit plan in its balance sheet. The funded status is measured as the difference between the fair value of the plan's assets and its benefit obligation (projected benefit obligation for pension plans and accumulated postretirement benefit obligation for other postretirement benefit plans). In years prior to 2006, the funded status of such plans was reported in the notes to the financial statements. This provision is effective for public companies for fiscal years ending after December 15, 2006. In addition, SFAS No. 158 also requires a company to measure its plan assets and benefit obligations as of its year-end balance sheet date. Currently, a company is permitted to choose a measurement date up to three months prior to its year-end to measure the plan assets and obligations. This provision is now effective for all companies for fiscal years ending after December 15, 2008. The Company adopted SFAS No. 158 as of December 31, 2006. At December 31, 2006, the projected benefit obligation of its defined benefit pension plan exceeded the fair value of plan assets by \$1.9 million and such amount is included in

“Accrued interest payable and other liabilities” in the Consolidated Balance Sheet as of that date. Due primarily to a plan curtailment effective December 31, 2007, the fair value of plan assets exceeded the projected benefit obligation of the defined benefit plan by \$0.9 million at December 31, 2007. Accordingly, such amount is included in “Other Assets” in the Consolidated Balance Sheet as of December 31, 2007. The required disclosures related to the Company’s defined benefit pension plan are included in Note 14 to the Consolidated Financial Statements.

The Company has adopted SEC Staff Accounting Bulletin No. 108 (SAB 108), “*Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements.*” SAB 108 states that registrants must quantify the impact of correcting all misstatements, including both the carryover (iron curtain method) and reversing (rollover method) effects of prior-year misstatements on the current-year financial statements, and by evaluating the misstatements quantified under each method in light of quantitative and qualitative factors. In adopting the requirements of SAB 108, the Company adjusted Net Deferred Tax Assets, disclosed in Note 15, and included in Other Assets in the consolidated financial statements, which had been understated by \$2.2 million as of January 1, 2006. Such understatement resulted from the over accrual of income tax expense in years prior to 2002, which were previously evaluated as being immaterial under the rollover method. The Company has reported the cumulative effect of the initial application of SAB 108 by adjusting retained earnings as of January 1, 2006 with a credit of \$2.2 million. The adjustment of the quarterly consolidated financial results for 2006 was accomplished by adjusting the applicable financial statement line items when such information was next presented. Reports previously filed with the SEC will not be amended.

### **Pending Accounting Pronouncements**

In September 2006, the FASB issued SFAS No. 157, "*Fair Value Measurements*". This Statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. It clarifies that fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in the market in which the reporting entity transacts. This Statement does not require any new fair value measurements, but rather, it provides enhanced guidance to other pronouncements that require or permit assets or liabilities to be measured at fair value. This Statement is effective for fiscal years beginning after November 15, 2007, with earlier adoption permitted. In February 2008, the FASB issued FASB Staff Position ("FSP") No. FAS 157-2, "*Effective Date of FASB Statement No.157*". This FSP defers the effective date of SFAS No.157 for nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually), to years beginning after November 15, 2008, and interim periods within those fiscal years. The Company does not expect that the adoption of this Statement will have a material impact on its financial position, results of operations or cash flows.

At its September 2006 meeting, the Emerging Issues Task Force ("EITF") reached a final consensus on Issue 06-04, "*Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*." The consensus stipulates that an agreement by an employer to share a portion of the proceeds of a life insurance policy with an employee during the postretirement period is a postretirement benefit arrangement required to be accounted for under SFAS No. 106, "*Employers' Accounting for Postretirement Benefits Other Than Pensions*" or Accounting Principles Board Opinion ("APB") No. 12, "*Omnibus Opinion - 1967*." The consensus concludes that the purchase of a split-dollar life insurance policy does not constitute a settlement under SFAS No. 106 and, therefore, a liability for the postretirement obligation must be recognized under SFAS No. 106 if the benefit is offered under an arrangement that constitutes a plan or under APB No. 12, if it is not part of a plan. Issue 06-04 is effective for annual or interim reporting periods beginning after December 15, 2007. The Company has endorsement split-dollar life insurance policies totaling \$20.9 million as of December 31, 2007 and will record a liability and a corresponding reduction of retained earnings of \$1.6 million on January 1, 2008 to reflect the effect of this consensus.

In March 2007, the FASB ratified the consensus of the EITF and released Issue 06-10, "*Accounting for Deferred Compensation and Postretirement Benefit Aspects of Collateral Assignment Split-Dollar Life Insurance Arrangements*". This Issue addresses questions raised about whether the consensus reached in Issue 06-4 should apply to collateral assignment split-dollar life insurance arrangements and the recognition and measurement of the employer's asset in such arrangements. The EITF concluded that an employer should recognize a liability for the postretirement benefit related to a collateral assignment split-dollar life insurance arrangement in accordance with either SFAS No. 106 or APB No. 12 based on the substantive agreement with the employee. In addition the EITF reached a conclusion that an employer should recognize and measure an asset based on the nature and substance of the collateral assignment split-dollar arrangement based on what future cash flows the employer is entitled to, if any, as well as the employee's obligation and ability to repay the employer. The effective date of EITF 06-10 is for fiscal years beginning after December 15, 2007. The Company had no collateral assignment split dollar life insurance policies as of December 31, 2007 and does not expect that the implementation of EITF 06-10 will have a material impact on its financial position, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159, "*The Fair Value Option for Financial Assets and Financial Liabilities*". This Statement permits companies to elect to follow fair value accounting for certain financial assets and liabilities in an effort to mitigate volatility in earnings without having to apply complex hedge accounting provisions. The Statement also establishes presentation and disclosure requirements designed to facilitate comparison between entities that choose different measurement attributes for similar types of assets and liabilities. The effective date of SFAS No. 159 is for fiscal years beginning after November 15, 2007. The Company does not expect that the adoption of this Statement will have a material impact on its financial position, results of operations or cash flows.



In December 2007, the FASB issued SFAS No. 141 (revised 2007), “*Business Combinations*” (“SFAS 141(R)”). This Statement replaces SFAS No. 141, “*Business Combinations*” (“SFAS 141”). SFAS No.141(R), among other things, establishes principles and requirements for how the acquirer in a business combination (i) recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquired business, (ii) recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase, and (iii) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. The Company is required to adopt SFAS No. 141(R) for all business combinations for which the acquisition date is on or after January 1, 2009. Earlier adoption is prohibited. The Statement will change the Company’s accounting treatment for business combinations on a prospective basis.

In December 2007, the FASB issued SFAS No. 160, “*Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB No. 51.*” This Statement establishes accounting and reporting standards for noncontrolling interests in a subsidiary and for the deconsolidation of a subsidiary. Minority interests will be recharacterized as noncontrolling interests and classified as a component of equity. The Statement also establishes a single method of accounting for changes in a parent’s ownership interest in a subsidiary and requires expanded disclosures. This Statement is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008 with earlier adoption prohibited. The Company does not expect that the adoption of this Statement will have a material impact on its financial position, results of operations or cash flows.

#### **Reclassifications**

Certain amounts in the accompanying consolidated financial statements have been reclassified to conform with the 2007 presentation.

#### **Note 2 – Acquisitions**

In October 2005, the Company completed the acquisition of West Financial Services, Inc. (“WFS”) located in McLean, Virginia, an asset management and financial planning company with approximately \$576 million in assets under management at the date of the acquisition. Under the terms of the acquisition agreement, the Company purchased WFS with a combination of stock and cash totaling approximately \$5.9 million. Additional contingent payments may be made and recorded in 2008 based on the financial results attained by WFS.

In the transaction, \$0.9 million of assets were acquired, primarily accounts receivable, and \$1.3 million of liabilities were assumed, primarily operating payables. The acquisition, including a 2007 contingent payment of \$1.4 million, resulted in the recognition of \$5.1 million of goodwill, which will not be amortized, and \$4.6 million of identified intangible assets which will be amortized on a straight-line basis over periods ranging from 4 to 10 years. This acquisition was considered immaterial and, accordingly, no pro forma results of operations are provided for the pre-acquisition periods.

In January 2006, the Company completed the acquisition of Neff & Associates (“Neff”), an insurance agency located in Ocean City, Maryland. Under the terms of the acquisition agreement, the Company purchased Neff for cash totaling approximately \$1.9 million. Additional contingent payments may be made and recorded in 2008 based on the financial results attained by Neff in that year.

In the transaction, \$0.3 million of assets were acquired, primarily accounts receivable, and \$0.3 million of liabilities were assumed, primarily operating payables. The acquisition resulted in the recognition of \$0.5 million of goodwill, which will not be amortized, and \$1.4 million of identified intangible assets which will be amortized on a straight-line basis over a period of 5 to 10 years. This acquisition was considered immaterial and, accordingly, no pro forma results of operations are provided for the pre-acquisition periods.

On February 15, 2007, the Company completed the acquisition of Potomac Bank of Virginia (“Potomac”), a bank headquartered in Fairfax, Virginia. Potomac operated five branch offices in the Northern Virginia metropolitan market at the time of the acquisition. The primary reason for the merger with Potomac was to gain entry into the northern Virginia high growth market. The total consideration paid to Potomac shareholders and related merger costs in connection with the acquisition was \$68.2 million. The results of Potomac’s operations have been included in the Company’s consolidated financial results subsequent to February 15, 2007. The assets and liabilities of Potomac were recorded on the Consolidated Balance Sheet at their respective fair values. The fair values were determined as of February 15, 2007 and are not subject to further refinements. The transaction resulted in total assets acquired as of February 15, 2007 of \$252.5 million, including approximately \$196.0 million of loans and leases; liabilities assumed were \$224.3 million, including \$197.0 million of deposits. Additionally, the Company recorded \$40.0 million of goodwill, \$5.1 million of core deposit intangibles (“CDI”) and \$0.3 million of other intangibles. CDI’s are subject to amortization and are being amortized over seven years on a straight-line basis.

On May 31, 2007, the Company completed the acquisition of CN Bancorp Inc. (“CNB”) and its wholly owned subsidiary, County National Bank (“County”). County was headquartered in Glen Burnie, Maryland, and had four full-service branches located in Anne Arundel County, Maryland at the time of the acquisition. The total consideration paid to CNB shareholder’s and related merger costs in connection with the acquisition was \$46.1 million. The results of CNB’s operations have been included in the Company’s consolidated financial results subsequent to May 31, 2007. The assets and liabilities of CNB were recorded on the Consolidated Balance Sheet at their respective fair values. The fair values were determined as of May 31, 2007 and are not subject to further refinements. The transaction resulted in total assets acquired as of May 31, 2007 of \$164.9 million, including approximately \$98.7 million of loans; liabilities assumed were \$141.4 million, including \$138.4 million of deposits. Additionally, the Company recorded \$22.6 million of goodwill, \$4.6 million of CDI’s and \$0.1 million of other intangibles. CDI’s are subject to amortization and are being amortized over seven years on a straight-line basis.

The acquisitions of Potomac and CNB, individually and in the aggregate, are considered immaterial for purposes of the pro forma disclosures required by SFAS No. 141, “*Business Combinations*.”

### Note 3 – Cash and Due from Banks

Regulation D of the Federal Reserve Act requires that banks maintain reserve balances with the Federal Reserve Bank based principally on the type and amount of their deposits. At its option, the Company maintains additional balances to compensate for clearing and safekeeping services. The average balance maintained in 2007 was \$2.1 million and in 2006 was \$2.3 million.

### Note 4 – Investments Available for Sale

The amortized cost and estimated fair values of investments available for sale at December 31 are as follows:

	2007				2006			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
(In thousands)								
U.S. Treasury	\$ 2,953	\$ 20	\$ 0	\$ 2,973	\$ 600	\$ 0	\$ (3)	\$ 597
U.S. Agencies and Corporations	139,057	352	(99)	139,310	244,688	32	(1,631)	243,089
State and municipal	2,660	101	0	2,761	2,303	87	0	2,390
Mortgage-backed	32,160	243	(47)	32,356	1,533	48	(4)	1,577
Trust preferred	7,887	1,164	0	9,051	7,885	1,107	0	8,992
Total debt securities	184,717	1,880	(146)	186,451	257,009	1,274	(1,638)	256,645
Marketable equity securities	350	0	0	350	200	0	0	200
Total investments available for sale	\$ 185,067	\$ 1,880	\$ (146)	\$ 186,801	\$ 257,209	\$ 1,274	\$ (1,638)	\$ 256,845

Gross unrealized losses and fair value by length of time that the individual available-for-sale securities have been in a continuous unrealized loss position at December 31, 2007 and 2006 are as follows:

(In thousands)	Continuous unrealized losses existing for:				Total Unrealized Losses
	Number Of securities	Fair Value	Less than 12 months	More than 12 months	
Available for sale as of December 31, 2007					



U.S. Agencies and Corporations	2	\$	20,925	\$	0	\$	99	\$	99
Mortgage-backed	14		12,554		43		4		47
	16	\$	33,479	\$	43	\$	103	\$	146

(In thousands)

Continuous unrealized losses existing for:

Available for sale as of December 31, 2006	Number of securities	Fair Value	Less than 12 months	More than 12 months	Total Unrealized Losses
U.S. Agencies and Corporations	26	\$ 194,521	\$ 57	\$ 1,574	\$ 1,631
U.S. Treasury	1	597	0	3	3
Mortgage-backed	5	300	0	4	4
	32	\$ 195,418	\$ 57	\$ 1,581	\$ 1,638

Approximately 100% of the bonds carried in the available-for-sale investment portfolio experiencing continuous losses as of December 31, 2007 and 2006 are rated AAA. The securities representing the unrealized losses in the available-for-sale portfolio as of December 31, 2007 and 2006 all have modest duration risk (1.14 years in 2007 and 2006), low credit risk, and minimal loss (approximately .43% in 2007 and .83% in 2006) when compared to book value. The unrealized losses that exist are the result of changes in market interest rates since the original purchase. These factors coupled with the fact that the Company has both the intent and ability to hold these investments for a period of time sufficient to allow for any anticipated recovery in fair value substantiates that the unrealized losses in the available-for-sale portfolio are temporary.

The amortized cost, and estimated fair values, of debt securities available for sale at December 31 by contractual maturity are shown below. The Company has allocated mortgage-backed securities into the four maturity groupings shown using the expected average life of the individual securities based upon statistics provided by independent third party industry sources. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

<i>(In thousands)</i>	2007		2006	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	\$ 145,952	\$ 146,531	\$ 236,789	\$ 235,667
Due after one year through five years	32,990	34,095	19,216	19,943
Due after five years through ten years	5,775	5,825	351	357
Due after ten years	0	0	653	678
Total debt securities available for sale	\$ 184,717	\$ 186,451	\$ 257,009	\$ 256,645

Sales of investments available for sale during 2007, 2006 and 2005 resulted in the following:

<i>(In thousands)</i>	2007	2006	2005
Proceeds	\$ 0	\$ 0	\$ 124,311
Gross gains	0	0	3,968
Gross losses	0	0	706

At December 31, 2007 and 2006, investments available for sale with a book value of \$173.9 million and \$237.3 million, respectively, were pledged as collateral for certain government deposits and for other purposes as required or permitted by law. The outstanding balance of no single issuer, except for U.S. Agencies and Corporations securities, exceeded ten percent of stockholders' equity at December 31, 2007 and 2006.

#### Note 5 – Investments Held to Maturity and Other Equity Securities

The amortized cost and estimated fair values of investments held to maturity at December 31 are as follows:

<i>(In thousands)</i>	2007				2006			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U.S. Agencies and Corporations	\$ 34,419	\$ 74	\$ 0	\$ 34,493	\$ 34,408	\$ 0	\$ (787)	\$ 33,621
Mortgage-backed	860	14	0	874	0	0	0	0

State and municipal	199,427	6,233	(32)	205,628	232,936	6,731	(82)	239,585
Total investments held to maturity	\$ 234,706	\$ 6,321	\$ (32)	\$ 240,995	\$ 267,344	\$ 6,731	\$ (869)	\$ 273,206

Gross unrealized losses and fair value by length of time that the individual held-to-maturity securities have been in a continuous unrealized loss position at December 31, 2007 and 2006 are as follows:

<i>(In thousands)</i>	Continuous unrealized losses existing for:				
	Number of securities	Fair Value	Less than 12 months	More than 12 months	Total Unrealized Losses
Held to Maturity as of December 31, 2007					
State and municipal	7	\$ 3,340	1	\$ 31	\$ 32
	7	\$ 3,340	1	\$ 31	\$ 32

*(In thousands)*

Held to Maturity as of December 31, 2006	Number of securities	Continuous unrealized losses existing for:			
		Fair Value	Less than 12 months	More than 12 months	Total Unrealized Losses
U.S. Agencies and Corporations	4	\$ 33,621	\$ 0	\$ 787	\$ 787
State and municipal	16	14,247	6	76	82
	20	\$ 47,868	\$ 6	\$ 863	\$ 869

Approximately 92% and 96% of the bonds carried in the held-to-maturity investment portfolio experiencing continuous unrealized losses as of December 31, 2007 and 2006, respectively, are rated AAA and 8% and 4% as of December 31, 2007 and 2006 respectively, are rated AA1. The securities representing the unrealized losses in the held-to-maturity portfolio all have modest duration risk (4.69 years in 2007 and 4.46 years in 2006), low credit risk, and minimal losses (approximately 1% in 2007 and 2% in 2006) when compared to book value. The unrealized losses that exist are the result of changes in market interest rates since the original purchase. These factors coupled with the Company's intent and ability to hold these investments for a period of time sufficient to allow for any anticipated recovery in fair value substantiates that the unrealized losses in the held-to-maturity portfolio are temporary.

The amortized cost and estimated fair values of debt securities held to maturity at December 31 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

<i>(In thousands)</i>	2007		2006	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	\$ 79,970	\$ 80,493	\$ 76,800	\$ 76,316
Due after one year through five years	136,614	141,547	146,014	150,408
Due after five years through ten years	11,757	12,108	38,234	39,782
Due after ten years	6,365	6,847	6,296	6,700
Total debt securities held to maturity	\$ 234,706	\$ 240,995	\$ 267,344	\$ 273,206

At December 31, 2007 and 2006, investments held to maturity with a book value of \$166.3 million and \$128.8 million, respectively, were pledged as collateral for certain government deposits and for other purposes as required or permitted by law. The outstanding balance of no single issuer, except for U.S. Agency and Corporations securities, exceeded ten percent of stockholders' equity at December 31, 2007 or 2006.

Other equity securities at December 31 are as follows:

<i>(In thousands)</i>	2007	2006
Federal Reserve Bank stock	\$ 5,033	\$ 2,027
Federal Home Loan Bank of Atlanta stock	18,658	14,692
Atlantic Central Bank stock	75	0
Total	\$ 23,766	\$ 16,719

#### Note 6 – Loans and Leases

Major categories at December 31 are presented below:

<i>(In thousands)</i>	2007	2006
Residential real estate:		
Residential mortgages	\$ 456,305	\$ 390,852
Residential construction	166,981	151,399
Commercial loans and leases:		
Commercial real estate	662,837	509,726
Commercial construction	262,840	192,547
Leases	35,722	34,079
Other commercial	316,051	182,159
Consumer	376,295	344,817
Total loans and leases	2,277,031	1,805,579
Less: allowance for loan and lease losses	(25,092)	(19,492)
Net loans and leases	\$ 2,251,939	\$ 1,786,087

Certain loan terms may create concentrations of credit risk and increase the lender's exposure to loss. These include terms that permit the deferral of principal payments or payments that are smaller than normal interest accruals (negative amortization); loans with high loan-to-value ratios; loans, such as option adjustable-rate mortgages, that may expose the borrower to future increases in repayments that are in excess of increases that would result solely from increases in market interest rates; and interest-only loans. The Company does not make loans that provide for negative amortization. The Company originates option adjustable-rate mortgages infrequently and sells all of them in the secondary market.

At December 31, 2007, the Company had a total of \$40.7 million in residential real estate loans and \$2.2 million in consumer loans with a loan to value ratio ("LTV") greater than 90%. The Company also had an additional \$91.3 million in residential lot loans owned by individuals with an LTV greater than 75%. Commercial loans, with an LTV greater than 75% to 85%, depending on the type of property, totaled \$49.9 million at December 31, 2007. The Company had interest-only loans totaling \$100.1 million in its loan portfolio at December 31, 2007. In addition, virtually all of the Company's equity lines of credit, \$217.9 million at December 31, 2007, which were included in the consumer loan portfolio, were made on an interest-only basis. The aggregate of all loans with these terms was \$502.1 million at December 31, 2007 which represented 22% of total loans and leases outstanding at that date. The Company is of the opinion that its loan underwriting procedures are structured to adequately mitigate any additional risk that the above types of loans might present.

Activity in the allowance for loan and lease losses for the preceding three years ended December 31 is shown below:

<i>(In thousands)</i>	2007	2006	2005
Balance at beginning of year	\$ 19,492	\$ 16,886	\$ 14,654
Allowance acquired with acquisition of other institutions	2,798	0	0
Provision for loan and lease losses	4,094	2,795	2,600
Loan and lease charge-offs	(1,444)	(315)	(535)
Loan and lease recoveries	152	126	167
Net charge-offs	(1,292)	(189)	(368)
Balance at year end	\$ 25,092	\$ 19,492	\$ 16,886

Information regarding impaired loans at December 31, and for the respective years then ended, is as follows:

<i>(In thousands)</i>	2007	2006	2005
Impaired loans with a valuation allowance	\$ 5,710	\$ 286	\$ 200
Impaired loans without a valuation allowance	16,174	0	209
Total impaired loans	\$ 21,884	\$ 286	\$ 409
Allowance for loan and lease losses related to impaired loans	\$ 936	\$ 118	\$ 31
Allowance for loan and lease losses related to other than impaired loans	24,156	19,374	16,855
Total allowance for loan and lease losses	\$ 25,092	\$ 19,492	\$ 16,886
Average impaired loans for the year	\$ 14,496	\$ 250	\$ 656
Interest income on impaired loans recognized on a cash basis	\$ 0	\$ 0	\$ 0

Non-accrual loans and leases including the impaired loans reflected in the preceding table, totaled \$23.0 million and \$1.9 million at December 31, 2007 and 2006 respectively. Gross interest income that would have been recorded in

2007 if non-accrual loans and leases had been current and, in accordance with their original terms, was \$1.1 million, while interest actually recorded on such loans was \$0. The Company's policy is to continue accrual of interest on loans over 90 days delinquent unless the specific circumstances of the loan dictate otherwise. In those cases, such loans are then classified as non-accrual loans. At December 31, 2007 such loans 90 days past due and still accruing interest totaled \$11.3 million.

Other real estate owned totaled \$0.5 million at December 31, 2007 and \$0.2 million at December 31, 2006.

**Note 7 – Premises and Equipment**

Premises and equipment at December 31 consist of:

<i>(In thousands)</i>	<b>2007</b>	<b>2006</b>
Land	\$ <b>9,954</b>	\$ 8,356
Buildings and leasehold improvements	<b>56,582</b>	49,897
Equipment	<b>33,839</b>	27,687
Total premises and equipment	<b>100,375</b>	85,940
Less: accumulated depreciation and amortization	<b>(45,918)</b>	(38,184)
Net premises and equipment	\$ <b>54,457</b>	\$ 47,756

Depreciation and amortization expense for premises and equipment amounted to \$4.9 million for 2007, \$4.2 million for 2006 and \$4.6 million for 2005. There were no contractual commitments at December 31, 2007 to construct branch facilities.

Total rental expense (net of rental income) of premises and equipment for the three years ended December 31 was \$5.7 million (2007), \$4.5 million (2006) and \$4.1 million (2005). Lease commitments entered into by the Company bear initial terms varying from 3 to 15 years, or they are 20-year ground leases, and are associated with premises.

Future minimum lease payments as of December 31, 2007 for all non-cancelable operating leases are:

<i>(In thousands)</i>	Operating Leases
2008	\$ 4,712
2009	4,902
2010	4,897
2011	4,470
2012	3,737
Thereafter	9,931
Total minimum lease payments	\$ 32,649

#### Note 8 – Goodwill and Other Intangible Assets

Goodwill is tested for impairment annually or more frequently if events or circumstances indicate a possible impairment. Under the provisions of SFAS No. 144, the acquired intangible assets apart from goodwill are reviewed for impairment annually and are being amortized over their remaining estimated lives.

The significant components of goodwill and acquired intangible assets are as follows:

<i>(Dollars in thousands)</i>	Unidentifiable Intangible Assets Resulting From	Other Identifiable Intangibles	Core Deposit Intangible Assets	Total
<b>2007</b>				
Gross carrying amount	\$ 13,603	\$ 17,854	\$ 7,959	\$ 39,416
Purchase price adjustment	1,491	0	0	1,491
Acquired during the year	62,600	0	342	72,658
Accumulated amortization	(1,109)	(14,809)	(3,408)	(20,350)
Net carrying amount	\$ 76,585	\$ 3,045	\$ 4,893	\$ 93,215
Weighted average remaining life		1.7	5.9	6.3
<b>2006</b>				
Gross carrying amount	\$ 13,151	\$ 17,854	\$ 6,557	\$ 37,562
Purchase price adjustment	(8)	0	(38)	(46)
Acquired during the year	460	0	1,440	1,900
Accumulated amortization	(1,109)	(13,069)	(2,091)	(16,269)
Net carrying amount	\$ 12,494	\$ 4,785	\$ 5,868	\$ 23,147
Weighted average remaining life		2.7	5.1	



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The changes in the carrying amount of goodwill by reportable segment for the twelve months ended December 31, 2007 and 2006 are as follows:

<i>(Dollars in thousands)</i>	Community		Investment		Total
	Banking	Insurance	Leasing	Management	
Balance January 1, 2006	\$ 130	\$ 4,265	\$ 4,159	\$ 3,488	\$ 12,042
Purchase price adjustment	0	(102)	0	94	(8)
Acquired during the year	0	460	0	0	460
Balance December 31, 2006	130	4,623	4,159	3,582	12,494
Purchase price adjustment	0	0	0	1,491	1,491
Acquired during the year	62,600	0	0	0	62,600
Balance December 31, 2007	\$ 62,730	\$ 4,623	\$ 4,159	\$ 5,073	\$ 76,585

Future estimated annual amortization expense is presented below:

(In thousands)

Year	Amount
2008	\$ 4,439
2009	3,654
2010	1,959
2011	1,845
2012	1,845
Later years	2,888

### Note 9 – Deposits

Deposits outstanding at December 31 consist of:

(In thousands)	2007	2006
Noninterest-bearing deposits	\$ 434,053	\$ 394,662
Interest-bearing deposits:		
Demand	254,878	233,841
Money market savings	726,647	518,146
Regular savings	153,964	160,035
Time deposits of less than \$100,000	416,601	406,910
Time deposits of \$100,000 or more	287,725	280,629
Total interest-bearing deposits	1,839,815	1,599,561
Total deposits	\$ 2,273,868	\$ 1,994,223

Interest expense on time deposits of \$100 thousand or more amounted to \$14.8 million, \$11.1 million and \$6.6 million for 2007, 2006, and 2005, respectively.

The following is a maturity schedule for time deposits maturing within years ending December 31:

(In thousands)

Year	Amount
2008	\$ 626,867
2009	54,668
2010	13,797
2011	3,731
2012	5,263
Total	\$ 704,326

### Note 10 – Short-term Borrowings

Information relating to short-term borrowings is as follows for the years ended December 31:

(Dollars in thousands)	2007		2006		2005	
At Year End:	Amount	Rate	Amount	Rate	Amount	Rate
Federal Home Loan Bank advances	\$ 275,957	4.25%	\$ 215,350	4.35%	\$ 192,450	3.98%
Retail repurchase agreements	98,015	3.00	99,382	4.25	170,769	3.45

Other short-term borrowings	<b>0</b>	<b>0.00</b>	0	0.00	17,000	4.31
Total	<b>\$ 373,972</b>	<b>3.92</b>	\$ 314,732	4.32%	\$ 380,219	3.76%
Average for the Year:						
Federal Home Loan Bank advances	<b>\$ 209,974</b>	<b>4.47%</b>	\$ 237,145	4.10%	\$ 121,813	3.87%
Retail repurchase agreements	<b>109,353</b>	<b>3.92</b>	174,150	4.11	146,887	2.54
Other short-term borrowings	<b>92</b>	<b>5.58</b>	2,979	5.34	26,761	4.15
Maximum Month-end Balance:						
Federal Home Loan Bank advances	<b>\$ 275,957</b>		\$ 252,350		\$ 192,450	
Retail repurchase agreements	<b>122,130</b>		236,427		186,760	
Other short-term borrowings	<b>0</b>		5,300		27,000	

The Company pledges U.S. Agencies and Corporations securities, based upon their market values, as collateral for 102.5% of the principal and accrued interest of its repurchase agreements.

The Company has an available line of credit for \$887.3 million with the Federal Home Loan Bank of Atlanta (the "FHLB") under which its borrowings are limited to \$649.2 million based on pledged collateral at interest rates based upon current market conditions, of which \$293.5 million was outstanding at December 31, 2007. At December 31, 2006, such line of credit totaled \$779.1 million under which \$543.9 million was available based on pledged collateral of which \$217.2 million was outstanding. Both short-term and long-term FHLB advances are fully collateralized by pledges of loans and U.S. Agency securities. The Company has pledged, under a blanket lien, qualifying residential mortgage loans amounting to \$282.6 million, commercial loans amounting to \$639.6 million, and home equity lines of credit ("HELOC") amounting to \$287.2 million at December 31, 2007 as collateral under the borrowing agreement with the FHLB. At December 31, 2006 the Company had pledged collateral of qualifying mortgage loans of \$262.0 million and HELOC loans amounting to \$251.4 million under the above borrowing agreement. The Company also had lines of credit available from the Federal Reserve and correspondent banks of \$140.8 million at December 31, 2007, and \$136.6 million at December 31, 2006, collateralized by state and municipal securities. In addition, the Company had an unsecured line of credit with a correspondent bank of \$20.0 million at December 31, 2007 and 2006. There were no borrowings outstanding against this unsecured line at December 31, 2007 or 2006.

**Note 11 – Long-term Borrowings**

The Company formed Sandy Spring Capital Trust II (“Capital Trust”) to facilitate completion of a pooled placement issuance of \$35.0 million of trust preferred securities on August 10, 2004. Subordinated debentures on the accompanying balance sheets reflect the subordinated debt instruments the Company issued to Capital Trust and bear a 6.35% rate of interest until July 7, 2009 at which time the interest rate becomes a variable rate, adjusted quarterly, equal to 225 basis points over the three month Libor. These obligations of the Company are subordinated to all other debt except other trust preferred subordinated, to which it may have equal subordination. The borrowing has a maturity date of October 7, 2034, and may be called by the Company no earlier than October 7, 2009.

The Company had other long-term borrowings at December 31 as follows:

<i>(In thousands)</i>	2007	2006
FHLB 4.13% Advance due 2013	\$ 1,458	\$ 1,808
FHLB 3.36% Advance due 2009	10,000	0
FHLB 4.34% Advance due 2010	2,094	0
FHLB 5.16% Advance due 2010	4,001	0
Total other long-term borrowings	\$ 17,553	\$ 1,808

The 4.13%, 4.34% and 5.16% advances are principal reducing with payments of approximately \$30 thousand, \$65 thousand and \$83 thousand, respectively, all paid monthly. Expected maturities may differ from contractual maturities because the Company may elect to prepay obligations.

The following is a maturity schedule for long-term borrowings within the years ending December 31:

Year	Maturities <i>(in thousands)</i>
2008	\$ 0
2009	968
2010	5,826
2011	350
2012	350
Future Years	10,059
Total	\$ 17,553

**Note 12 – Stockholders’ Equity**

The Company’s Articles of Incorporation authorize 50,000,000 shares of capital stock (par value \$1.00 per share). Issued shares have been classified as common stock. The Articles of Incorporation provide that remaining unissued shares may later be designated as either common or preferred stock.

The Company has a director stock purchase plan (the “Director Plan”) which commenced on May 1, 2004. Under the Director Plan, members of the Board of Directors may elect to use a portion (minimum 50%) of their annual retainer fee to purchase shares of Company stock. The Company has reserved 15,000 authorized but unissued shares of common stock for purchase under the plan. Purchases are made at the fair market value of the stock on the purchase date. At December 31, 2007, there were 7,404 shares available for issuance under the plan.

The Company has an employee stock purchase plan (the "Purchase Plan") which commenced on July 1, 2001, with consecutive monthly offering periods thereafter. The Company has reserved 450,000 authorized but unissued shares of common stock for purchase under the plan. Shares are purchased at 85% of the fair market value on the exercise date through monthly payroll deductions of not less than 1% or more than 10% of cash compensation paid in the month. The Purchase Plan is administered by a committee of at least three directors appointed by the Board of Directors. At December 31, 2007, there were 328,341 shares available for issuance under this plan.

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In 2007, the Company's Board of Directors renewed a Stock Repurchase Plan by authorizing the repurchase of up to 5% or approximately 786,000 shares of the Company's outstanding common stock, par value \$1.00 per share, in connection with shares expected to be issued under the Company's stock option and employee benefit plans, and for other corporate purposes. The share repurchases are expected to be made primarily on the open market periodically until March 31, 2009, or earlier termination of the repurchase program by the board. Repurchases will be made at the discretion of management based upon market, business, legal, accounting and other factors. The Company purchased the equivalent of 70,500 shares of its common stock under a prior share repurchase program, which expired on March 31, 2007. No shares were repurchased under that plan during 2007. The Company has purchased 156,249 shares under the current share repurchase program through December 31, 2007.

The Company has an Investors Choice Plan (the "Plan"), which is sponsored and administered by the American Stock Transfer and Trust Company ("AST") as independent agent, which enables current shareholders as well as first-time buyers to purchase and sell common stock of Sandy Spring Bancorp, Inc. directly through AST at low commissions. Participants may reinvest cash dividends and make periodic supplemental cash payments to purchase additional shares. Share purchases pursuant to the Plan are made in the open market. The Plan also allows participants to deposit their stock certificates with AST for safekeeping or sale.

Bank and holding company regulations, as well as Maryland law, impose certain restrictions on dividend payments by the Bank, as well as restricting extensions of credit and transfers of assets between the Bank and the Company. At December 31, 2007, the Bank could have paid additional dividends of \$14.6 million to its parent company without regulatory approval. In conjunction with the Company's long-term borrowing from Capital Trust, the Bank issued a note to Bancorp for \$35.0 million which was outstanding at December 31, 2007. There were no other loans outstanding between the Bank and the Company at December 31, 2007 or December 31, 2006.

### **Note 13 – Stock Based Compensation**

At December 31, 2007, the Company had three stock-based compensation plans in existence, the 1992 and 1999 stock option plans (both expired but having outstanding options that may still be exercised) and the 2005 Omnibus Stock Plan, which is described below.

The Company's 2005 Omnibus Stock Plan ("Omnibus Plan") provides for the granting of non-qualifying stock options and restricted stock to the Company's directors, and incentive and non-qualifying stock options, stock appreciation rights and restricted stock grants to selected key employees on a periodic basis at the discretion of the board. The Omnibus Plan authorizes the issuance of up to 1,800,000 shares of common stock of which 1,365,708 are available for issuance at December 31, 2007. It has a term of ten years, and is administered by a committee of at least three independent directors. Options granted under the plan have an exercise price which may not be less than 100% of the fair market value of the common stock on the date of the grant and must be exercised within seven to ten years from the date of grant. The exercise price of stock options must be paid for in full in cash or shares of common stock, or a combination of both. The Stock Option Committee has the discretion, when making a grant of stock options, to impose restrictions on the shares to be purchased in exercise of such options. Outstanding options granted under the expired 1992 and 1999 stock option plans will continue until exercise or expiration.

Options awarded prior to December 15, 2005 vest in equal increments over a two-year period, with one third vesting immediately upon grant. Effective October 19, 2005, the Board of Directors approved the acceleration, by one year, of the vesting of the then outstanding options to purchase approximately 66,000 shares of the Company's common stock granted in December 2004. These included options held by certain members of senior management. This effectively reduced the two-year vesting period on these options to one year. The amount that would have been expensed for such unvested options in 2006 had the Company not accelerated the vesting would have been approximately \$0.4 million. Additionally, stock options granted in 2004 have a ten year life. The other terms of the option grants remain unchanged.

The board of directors approved the granting of stock options totaling 3,750 shares in 2007 and 105,623 shares in 2006. The options are subject to a three year vesting schedule with one third of the options vesting each year on the anniversary date of the respective grants. In addition, the board of directors granted restricted shares totaling 750 shares in 2007 and 31,483 shares in 2006. The restricted shares are subject to three year and five year vesting schedules, respectively, with one third and one fifth, respectively, of the shares vesting each year on the anniversary date of the respective grants. Compensation expense is recognized on a straight-line basis over the stock option or restricted stock vesting period. The fair value based method for expense recognition of employee awards resulted in expense of approximately \$1.1 million and \$0.5 million, net of a tax benefits of approximately \$0.6 million and \$0.1 million for the years ended December 31, 2007 and 2006, respectively.

Had the compensation cost for the Company's stock-based compensation plan been determined under the fair value recognition provisions in SFAS No. 123 prior to the date of adopting SFAS No. 123R, the Company's net income and earnings per share would have been adjusted to the pro forma amounts below for the year ended December 31, 2005:

<i>(In thousands, except per share data)</i>	2005
Net income, as reported	\$ 33,098
Basic earnings per share	2.26
Diluted earnings per share	2.24
Stock-based compensation cost, net of related tax effects	0
Information calculated as if fair value method had been applied to all awards:	
Net income, as reported	\$ 33,098
Add: Stock-based compensation expense recognized during the period, net of related tax effects	0
Less: Stock-based compensation expense determined under the fair value-based method, net of tax effects	(2,107)
Pro forma net income	\$ 30,991
Basic earnings per share – as reported	\$ 2.26
Basic earnings per share – pro forma	\$ 2.11
Diluted earnings per share – as reported	\$ 2.24
Diluted earnings per share – pro forma	\$ 2.10

The fair values of all of the options granted during the last three years have been estimated using a binomial option-pricing model with the following weighted-average assumptions as of December 31:

	2007	2006	2005
Dividend yield	3.12%	2.43%	2.48%
Weighted average expected volatility	26.71%	19.12%	21.27%
Weighted average risk-free interest rate	4.35%	4.75%	4.34%
Weighted average expected lives (in years)	7	6	5
Weighted average grant-date fair value	\$ 7.50	\$ 8.14	\$ 6.72

The dividend yield is based on estimated future dividend yields. The risk-free rate for periods within the contractual term of the share option is based on the U.S. Treasury yield curve in effect at the time of the grant. Expected volatilities are generally based on historical volatilities. The expected term of share options granted is generally derived from historical experience.

The total intrinsic value of options exercised during the year ended December 31, 2007 and 2006 was \$1.1 million and \$0.6 million, respectively. The number of options, exercise prices, and fair values has been retroactively restated for all stock dividends, if any, occurring since the date the options were granted. The Company generally issues authorized but previously unissued shares to satisfy option exercises.

The total of unrecognized compensation cost related to stock options was approximately \$0.4 million as of December 31, 2007. That cost is expected to be recognized over a weighted average period of approximately 2.0 years.

The following is a summary of changes in shares under option for the years ended December 31:



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	2007		2006		2005		
	Aggregate Intrinsic Value	Number Of Shares	Weighted Average Exercise Price	Number Of Shares	Weighted Average Exercise Price	Number Of Shares	Weighted Average Exercise Price
Balance, beginning of year		<b>1,032,585</b>	<b>\$ 33.77</b>	1,004,473	\$ 33.08	824,192	\$ 31.04
Options (at fair value) related to option plans of acquired companies		<b>77,811</b>	<b>18.87</b>	—	—	—	—
Granted		<b>3,750</b>	<b>28.87</b>	105,623	37.40	249,061	38.13
Forfeited or Expired		<b>(39,517)</b>	<b>36.58</b>	(41,510)	37.73	(26,302)	36.69
Exercised		<b>(78,264)</b>	<b>17.48</b>	(36,001)	20.53	(42,478)	21.00
Balance, end of year	<b>\$ 1,588,288</b>	<b>996,365</b>	<b>\$ 33.72</b>	1,032,585	\$ 33.77	1,004,473	\$ 33.08
Options exercisable at year-end	<b>\$ 1,588,288</b>	<b>924,144</b>	<b>\$ 33.47</b>				
Weighted average fair value of options granted during the year			<b>\$ 7.50</b>		<b>\$ 8.14</b>		<b>\$ 6.72</b>

The following table summarizes information about options outstanding at December 31, 2007:

Range of Exercise Price	Options Outstanding			Exercisable Options	
	Outstanding Number	Weighted Average Remaining Contracted Life (in years)	Weighted Average Exercise Price	Exercisable Number	Weighted Average Exercise Price
\$11.78-\$21.78	145,172	3.6	\$ 16.88	145,172	\$ 16.88
\$28.59-\$32.25	202,231	4.7	31.58	198,481	31.64
\$37.40-\$38.91	648,962	5.9	38.15	580,491	38.24
	996,365	5.3	33.72	924,144	33.47

A summary of the status of the Company's restricted stock as of December 31, 2007, is presented below:

	Number Of Shares	Weighted Average Grant-Date Fair Value
Restricted stock at January 1, 2007	31,483	\$ 37.40
Granted	750	28.87
Vested	(6,078)	37.40
Forfeited	(1,409)	37.40
Restricted stock at December 31, 2007	24,746	37.14

The total of unrecognized compensation cost related to restricted stock was approximately \$0.7 million as of December 31, 2007. That cost is expected to be recognized over a weighted period of approximately 4.0 years.

#### Note 14 – Pension, Profit Sharing, and Other Employee Benefit Plans

##### Defined Benefit Pension Plan

The Company has a qualified, noncontributory, defined benefit pension plan covering substantially all employees. Benefits after January 1, 2005, are based on the benefit earned as of December 31, 2004, plus benefits earned in future years of service based on the employee's compensation during each such year. On November 14, 2007, the Company informed employees that the plan would be frozen for new and existing entrants after December 31, 2007. All benefit accruals for employees were frozen as of December 31, 2007 based on past service and thus future salary increases will no longer affect the defined benefit provided by the plan although additional vesting may continue to occur.

The Company's funding policy is to contribute amounts to the plan sufficient to meet the minimum funding requirements of the Employee Retirement Income Security Act of 1974 ("ERISA"), as amended. In addition, the Company contributes additional amounts as it deems appropriate based on benefits attributed to service prior to the date of the plan freeze. The Plan invests primarily in a diversified portfolio of managed fixed income and equity funds.

The Plan's funded status as of December 31 is as follows:

<i>(In thousands)</i>	2007	2006
<b>Reconciliation of Projected Benefit Obligation:</b>		
Projected obligation at January 1	\$ 22,055	\$ 21,201
Service cost	1,315	1,105
Interest cost	1,337	1,230
Actuarial loss	734	153
Curtailment	(2,322)	
Increase/(decrease) due to amendments during the year	0	(782)
Increase/(decrease) due to discount rate change	0	(164)
Benefit payments	(177)	(688)
Projected obligation at December 31	22,942	22,055
<b>Reconciliation of Fair Value of Plan Assets:</b>		
Fair value of plan assets at January 1	20,192	18,431
Actual return on plan assets	2,384	1,449
Employer contributions	1,400	1,000
Benefit payments	(177)	(688)
Fair value of plan assets at December 31	23,799	20,192
<b>Funded Status:</b>		
Funded status at December 31	857	(1,863)
Unrecognized prior service cost (benefit)	(1,589)	(1,764)
Unrecognized net actuarial loss	5,078	8,053
Net periodic benefit cost not yet recognized	(3,489)	(6,289)
Prepaid (unfunded) pension cost	\$ 857	\$ (1,863)
Accumulated benefit obligation at December 31	\$ 22,942	\$ 19,936

Net periodic benefit cost for the previous three years includes the following components:

<i>(In thousands)</i>	2007	2006	2005
Service cost for benefits earned	\$ 1,315	\$ 1,105	\$ 1,622
Interest cost on projected benefit obligation	1,337	1,230	1,094
Expected return on plan assets	(1,508)	(1,377)	(1,179)
Amortization of prior service cost	(175)	(175)	(63)
Recognized net actuarial loss	512	445	335
Net periodic benefit cost	\$ 1,481	\$ 1,228	\$ 1,809

The following shows the amounts recognized in accumulated other comprehensive income as of the beginning of the fiscal year, the amount arising during the year, the adjustment due to being recognized as a component of net periodic benefit cost during the year, and the amount remaining to be recognized and therefore a part of accumulated other comprehensive income (loss) as of December 31, 2007:

<i>(In thousands)</i>	Prior Service Cost	Net Gain/(Loss)
Included in accumulated other comprehensive income (loss) as of January 1, 2006	\$ (1,157)	\$ 8,581
Additions during the year	(782)	(83)
Reclassifications due to recognition as net periodic pension cost	175	(445)
	(1,764)	8,053

Included in accumulated other comprehensive income (loss) as of December 31, 2006

Net gain due to plan curtailment	0	(2,322)
Additions during the year	0	(142)
Reclassifications due to recognition as net periodic pension cost	175	(511)
Included in accumulated other comprehensive income (loss) as of December 31, 2007	\$ (1,589)	\$ 5,078
Applicable tax effect	633	(2,024)
Included in accumulated other comprehensive income(loss) net of tax effect as of December 31, 2007	\$ (956)	\$ 3,054
Amount expected to be recognized as part of net periodic pension cost in the next fiscal year	\$ (174)	\$ 272

There are no plan assets expected to be returned to the employer in the next twelve months.

The following items have not yet been recognized as a component of net periodic benefit cost as December 31, 2007 and 2008, respectively:

<i>(In thousands):</i>	2008	2007	2006
Prior service cost	\$ 1,415	\$ 1,589	\$ 1,764
Net actuarial loss	(4,806)	(5,078)	(8,053)
Net periodic benefit cost not yet recognized	\$ (3,391)	\$ (3,489)	\$ (6,289)

#### **Additional Information**

Weighted-average assumptions used to determine benefit obligations at December 31 are as follows:

	2007	2006	2005
Discount rate	6.00%	6.00%	6.00%
Rate of compensation increase	4.00%	4.00%	4.50%

Weighted-average assumptions used to determine net periodic benefit cost for years ended December 31 are as follows:

	2007	2006	2005
Discount rate	6.00%	6.00%	6.50%
Expected return on plan assets	7.50%	7.50%	8.00%
Rate of compensation increase	4.00%	4.00%	4.50%

The expected rate of return on assets of 7.50% reflects the Plan's predominant investment of assets in equity type securities and an analysis of the average rate of return of the S&P 500 index and the Lehman Brothers Gov't/Corp. index over the past 10 years weighted by 66.7% and 33.3%, respectively.

#### **Plan Assets**

The Company's pension plan weighted-average allocations at December 31, 2007 and 2006, by asset category are as follows:

Asset Category	2007	2006
Equity securities	47.9%	71.3%
Debt securities	27.6%	23.4%
Cash, other	24.5%	5.3%
Total	100.0%	100.0%

The Company has a written investment policy approved by the Board of Directors that governs the investment of the defined benefit pension fund trust portfolio. The investment policy is designed to provide limits on risk that is undertaken by the investment managers both in terms of market volatility of the portfolio and the quality of the individual assets that are held in the portfolio. The investment policy statement focuses on the following areas of concern: preservation of capital, diversification, risk tolerance, investment duration, rate of return, liquidity and investment management costs. Market volatility risk is controlled by limiting the asset allocation of the most volatile asset class, equities, to no more than 70% of the portfolio; and ensuring that there is sufficient liquidity to meet distribution requirements from the portfolio without disrupting long-term assets. Diversification of the equity portion of the portfolio is controlled by limiting the value of any initial acquisition so that it does not exceed 5% of the market value of the portfolio when purchased. The policy requires the sale of any portion of an equity position when its value exceeds 10% of the portfolio. Fixed income market volatility risk is managed by limiting the term of fixed income investments to five years. Fixed income investments must carry an "A" or better rating by a recognized credit rating agency. Corporate debt of a single issuer may not exceed 10% of the market value of the portfolio. The investment in

derivative instruments such as “naked” call options, futures, commodities, and short selling is prohibited. Investment in equity index funds and the writing of “covered” call options (a conservative strategy to increase portfolio income) are permitted. Foreign currencies denominated debt instruments are not permitted. Investment performance is measured against industry accepted benchmarks. The risk tolerance and asset allocation limitations imposed by the policy are consistent with attaining the rate of return assumptions used in the actuarial funding calculations. A Retirement Plan Investment Committee meets quarterly to review the activities of the investment managers to ensure adherence with the investment policy statement.

**Contributions**

The Company, with input from its actuaries, estimates that the 2008 contribution will be approximately \$1.0 million.

**Estimated Future Benefit Payments**

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

Year	Pension Benefits (in thousands)
2008	\$ 323
2009	387
2010	433
2011	511
2012	655
2013-2017	5,818

**Cash and Deferred Profit Sharing Plan**

The Sandy Spring Bancorp, Inc. Cash and Deferred Profit Sharing Plan includes a 401(k) provision with a Company match. Effective January 1, 2007 the Company revised the Plan to eliminate the deferral option and require an all-cash payout of any profit sharing distributions beginning in 2007. The 401(k) provision is voluntary and covers all eligible employees after ninety days of service. Employees contributing to the 401(k) provision receive a matching contribution of 100% of the first 3% of compensation and 50% of the next 2% of compensation subject to employee contribution limitations. The Company match vests immediately. The Plan permits employees to purchase shares of Sandy Spring Bancorp, Inc. common stock with their 401(k) contributions, Company match, and other contributions under the Plan. Profit sharing contributions and Company match are included in noninterest expenses and totaled \$1.5 million in 2007, \$1.4 million in 2006, and \$2.3 million in 2005.

The Company also had a performance based compensation benefit in 2007 that at one time was integrated with the Cash and Deferred Profit Sharing Plan and provided incentives to employees based on the Company's financial results as measured against key performance indicator goals set by management. Payments were made annually and amounts included in noninterest expense under the plan amounted to \$0.2 million in 2007, \$2.3 million in 2006, and \$2.7 million in 2005. For 2008, this incentive plan has been replaced with a new short-term incentive plan named the Sandy Spring Leadership Incentive Plan. It will provide a cash bonus to key members of management based on the Company's financial results using a weighted formula.

**Supplemental Executive Retirements Agreements**

In past years, the Company had Supplemental Executive Retirement Agreements ("SERAs") with its executive officers providing for retirement income benefits as well as pre-retirement death benefits. Retirement benefits payable under the SERAs, if any, were integrated with other pension plan and Social Security retirement benefits expected to be received by the executive. The Company accrued the present value of these benefits over the remaining number of years to the executives' retirement dates. Effective January 1, 2008, these agreements were replaced with a defined contribution plan, the "Executive Incentive Retirement Plan" or "the Plan". Benefits under the SERAs were reduced to a fixed amount as of December 31, 2007, and those amounts accrued were transferred to the new plan on behalf of each participant. Additionally, under the new Plan, officers designated by the board of directors earn a deferral bonus which is accrued annually based on the Company's financial performance compared to a selected group of peer banks. For current participants, accruals after January 1, 2008 vest immediately. Amounts transferred to the plan from the SERAs on behalf of each participant continue to vest based on years of service. Benefit costs included in noninterest expenses for 2007, 2006 and 2005 were \$0.9 million, \$1.0 million, and \$0.6 million, respectively.

**Executive Health Insurance Plan**

In past years, the Company had an Executive Health Insurance Plan that provided for payment of defined medical and dental expenses not otherwise covered by insurance for selected executives and their families. Benefits, which were paid during both employment and retirement, were subject to a \$6,500 limitation for each executive per year. Effective January 1, 2008 this plan was eliminated with respect to all active executives and liabilities accrued for such payments upon retirement by such executives were reversed which resulted in income in 2007 of \$0.4 million. Currently retired executives that formerly retired under the Plan will continue to receive this benefit. Expenses under the Plan, covering insurance premiums and out-of-pocket expense reimbursement benefits, totaled \$35 thousand in 2006, and (\$72 thousand) in 2005.



**Note 15 – Income Taxes**

Income tax expense for the years ended December 31 consists of:

<i>(In thousands)</i>	2007	2006	2005
<b>Current Income Taxes:</b>			
Federal	\$ 13,178	\$ 11,793	\$ 11,979
State	2,514	2,082	2,971
Total current	15,692	13,875	14,950
<b>Deferred Income Taxes (benefits):</b>			
Federal	(2,003)	(845)	(2,052)
State	(718)	(141)	(703)
Total deferred	(2,721)	(986)	(2,755)
Total income tax expense	\$ 12,971	\$ 12,889	\$ 12,195

Temporary differences between the amounts reported in the financial statements and the tax bases of assets and liabilities result in deferred taxes. Deferred tax assets and liabilities, shown as the sum of the appropriate tax effect for each significant type of temporary difference, are presented below for the years ended December 31:

<i>(In thousands)</i>	2007	2006
<b>Deferred Tax Assets:</b>		
Allowance for loan and lease losses	\$ 10,009	\$ 7,709
Loan and deposit premium/discount	997	389
Intangible assets	0	573
Employee benefits	3,002	2,573
Pension plan costs	0	737
Unrealized losses on investments available for sale	0	144
Non-qualified stock option expense	149	88
Other	424	289
Gross deferred tax assets	14,581	12,502
<b>Deferred Tax Liabilities:</b>		
Depreciation	(953)	(1,230)
Intangible assets	(2,777)	0
Deferred loan fees and costs	(1,098)	(1,494)
Unrealized gains on investments available for sale	(691)	0
Bond accretion	(396)	(299)
Pension plan costs	(342)	0
Other	(3)	(1)
Gross deferred tax liabilities	(6,260)	(3,024)
Net deferred tax (liabilities) assets	\$ 8,321	\$ 9,478

No valuation allowance exists with respect to deferred tax items.

A three-year reconciliation of the difference between the statutory federal income tax rate and the effective tax rate for the Company is as follows:

	2007	2006	2005
Federal income tax rate	35.0%	35.0%	35.0%
Increase (decrease) resulting from:			
Tax exempt income, net	(9.1)	(9.7)	(11.4)

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State income taxes, net of federal income tax benefits	<b>3.0</b>	2.9	3.3
State tax rate change on deferred tax assets	<b>(0.4)</b>	0	0
Other, net	<b>0.2</b>	0	0
Effective tax rate	<b>28.7%</b>	28.2%	26.9%

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**Note 16 – Net Income per Common Share**

The calculation of net income per common share for the years ended December 31 is as follows:

<i>(In thousands, except per share data)</i>	2007		2006		2005	
<b>Basic:</b>						
Net income available to common stockholders	\$	32,262	\$	32,871	\$	33,098
Average common shares outstanding		16,015		14,801		14,664
Basic net income per share	\$	2.01	\$	2.22	\$	2.26
<b>Diluted:</b>						
Net income available to common stockholders	\$	32,262	\$	32,871	\$	33,098
Average common shares outstanding		16,015		14,801		14,664
Stock option adjustment		72		126		103
Average common shares outstanding-diluted		16,087		14,927		14,767
Diluted net income per share	\$	2.01	\$	2.20	\$	2.24

As of December 31, 2007 options for 733,482 shares of common stock were not included in computing diluted net income per share because their effects were anti-dilutive.

**Note 17 – Related Party Transactions**

Certain directors and executive officers have loan transactions with the Company. Such loans were made in the ordinary course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with outsiders. The following schedule summarizes changes in amounts of loans outstanding, both direct and indirect, to these persons during the years indicated.

<i>(In thousands)</i>	2007		2006	
Balance at January 1	\$	38,342	\$	40,295
Additions		3,300		6,852
Repayments		(15,934)		(8,805)
Balance at December 31	\$	25,708	\$	38,342

**Note 18 – Financial Instruments with Off-balance Sheet Risk and Derivatives**

In the normal course of business, the Company has various outstanding credit commitments that are properly not reflected in the financial statements. These commitments are made to satisfy the financing needs of the Company's clients. The associated credit risk is controlled by subjecting such activity to the same credit and quality controls as exist for the Company's lending and investing activities. The commitments involve diverse business and consumer customers and are generally well collateralized. Collateral held varies, but may include residential real estate, commercial real estate, property and equipment, inventory and accounts receivable. Management does not anticipate that losses, if any, which may occur as a result of these commitments, would materially affect the stockholders' equity of the Company. Since a portion of the commitments have some likelihood of not being exercised, the amounts do not necessarily represent future cash requirements. A summary of the financial instruments with off-balance sheet credit risk is as follows at December 31:

<i>(In thousands)</i>	2007		2006	
<b>Commitments to extend credit and available credit lines:</b>				
Commercial	\$	98,930	\$	93,614
Real estate-development and construction		82,498		70,159
Real estate-residential mortgage		2,955		11,529
Lines of credit, principally home equity and business lines		665,778		566,877
Standby letters of credit		55,280		42,443
	\$	905,441	\$	784,622

Beginning in 2007, the Company entered into interest rate swaps (“swaps”) to facilitate customer transactions and meet their financing needs. These swaps qualify as derivatives, but are not designated as hedging instruments. Interest rate swap contracts involve the risk of dealing with counterparties and their ability to meet contractual terms. When the fair value of a derivative instrument contract is positive, this generally indicates that the counterparty or customer owes the Company, and results in credit risk to the Company. When the fair value of a derivative instrument contract is negative, the Company owes the customer or counterparty and therefore, has no credit risk.

A summary of the Company's interest rate swaps is included in the following table:

<i>(in thousands)</i>	As of December 31, 2007					Pay Rate
	Notional Amount	Estimated Fair Value	Years to Maturity	Receive Rate	Weighted Average	
Interest Rate Swap Agreements:						
Pay Fixed/Receive Variable \$ Swaps	3,153	\$ 74	2.7	7.00%	7.47%	
Pay Variable/Receive Fixed Swaps	3,153	(74)	2.7	7.47	7.00	
Total Swaps	\$ 6,306	\$ 0	2.7	7.24%	7.24%	

### Note 19 – Litigation

In the normal course of business, the Company becomes involved in litigation arising from the banking, financial, and other activities it conducts. Management, after consultation with legal counsel, does not anticipate that the ultimate liability, if any, arising out of these matters will have a material effect on the Company's financial condition, operating results or liquidity.

### Note 20 – Fair Value of Financial Instruments

The Company discloses fair value information about financial instruments for which it is practicable to estimate the value, whether or not such financial instruments are recognized on the balance sheet. Financial instruments have been defined broadly to encompass 94.0% of the Company's assets and 99.0% of its liabilities at December 31, 2007 and 97.0% of its assets and 99.0% of its liabilities at December 31, 2006. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by a quoted market price, if one exists.

Quoted market prices, where available, are shown as estimates of fair market values. Because no quoted market prices are available for a significant part of the Company's financial instruments, the fair value of such instruments has been derived based on the amount and timing of future cash flows and estimated discount rates.

Present value techniques used in estimating the fair value of many of the Company's financial instruments are significantly affected by the assumptions used. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate cash settlement of the instrument. Additionally, the accompanying estimates of fair values are only representative of the fair values of the individual financial assets and liabilities, and should not be considered an indication of the fair value of the Company.

The estimated fair values of the Company's financial instruments at December 31 are as follows:

<i>(In thousands)</i>	2007		2006	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial Assets				
Cash and temporary investments <sup>(1)</sup>	\$ 92,941	\$ 93,028	\$ 117,492	\$ 117,591
Investments available for sale	186,801	186,801	256,845	256,845
Investments held to maturity and other equity securities	258,472	264,761	284,063	289,925

Loans, net of allowances	<b>2,251,939</b>	<b>2,261,950</b>	1,786,087	1,788,214
Accrued interest receivable and other assets <sup>(2)</sup>	<b>85,759</b>	<b>85,759</b>	76,810	76,810

#### Financial Liabilities

Deposits	<b>\$ 2,273,868</b>	<b>\$ 2,274,872</b>	\$ 1,994,223	\$ 1,990,623
Short-term borrowings	<b>373,972</b>	<b>395,302</b>	314,732	318,189
Long-term borrowings	<b>52,553</b>	<b>57,311</b>	36,808	39,298
Accrued interest payable and other liabilities <sup>(2)</sup>	<b>3,552</b>	<b>3,552</b>	3,426	3,426

<sup>(1)</sup>Temporary investments include federal funds sold, interest-bearing deposits with banks and residential mortgage loans held for sale.

<sup>(2)</sup>Only financial instruments as defined in SFAS No. 107, "Disclosure about Fair Value of Financial Instruments," are included in other assets and other liabilities.

The following methods and assumptions were used to estimate the fair value of each category of financial instruments for which it is practicable to estimate that value:

**Cash and Temporary Investments:**

**Cash and due from banks, federal funds sold and interest-bearing deposits with banks.** The carrying amount approximated the fair value.

**Residential mortgage loans held for sale.** The fair value of residential mortgage loans held for sale was derived from secondary market quotations for similar instruments.

**Investments.** The fair value for U.S. Treasury, U.S. Agency, state and municipal, corporate debt and trust preferred securities was based upon quoted market bids; for mortgage-backed securities upon bid prices for similar pools of fixed and variable rate assets, considering current market spreads and prepayment speeds; and, for equity securities upon quoted market prices.

**Loans.** The fair value was estimated by computing the discounted value of estimated cash flows, adjusted for potential loan and lease losses, for pools of loans having similar characteristics. The discount rate was based upon the current loan origination rate for a similar loan. Non-performing loans have an assumed interest rate of 0%.

**Accrued interest receivable.** The carrying amount approximated the fair value of accrued interest, considering the short-term nature of the receivable and its expected collection.

**Other assets.** The carrying amount approximated the fair value considering their short-term nature.

**Deposits.** The fair value of demand, money market savings and regular savings deposits, which have no stated maturity, were considered equal to their carrying amount, representing the amount payable on demand. While management believes that the Bank's core deposit relationships provide a relatively stable, low-cost funding source that has a substantial intangible value separate from the value of the deposit balances, these estimated fair values do not include the intangible value of core deposit relationships, which comprise a significant portion of the Bank's deposit base.

The fair value of time deposits was based upon the discounted value of contractual cash flows at current rates for deposits of similar remaining maturity.

**Short-term borrowings.** The carrying amount approximated the fair value of repurchase agreements due to their variable interest rates. The fair value of Federal Home Loan Bank of Atlanta advances was estimated by computing the discounted value of contractual cash flows payable at current interest rates for obligations with similar remaining terms.

**Long-term borrowings.** The fair value of the Federal Home Loan Bank of Atlanta advances and subordinated debentures was estimated by computing the discounted value of contractual cash flows payable at current interest rates for obligations with similar remaining terms.

**Accrued interest payable and other liabilities.** The carrying amount approximated the fair value of accrued interest payable, accrued dividends and premiums payable, considering their short-term nature and expected payment.

**Note 21 – Parent Company Financial Information**

The condensed financial statements for Sandy Spring Bancorp, Inc. (Parent Only) pertaining to the periods covered by the Company's consolidated financial statements are presented below:

**Balance Sheets**

<i>(In thousands)</i>	December 31,	
	2007	2006
<b>Assets</b>		
Cash and cash equivalents	\$ 6,601	\$ 2,870
Investments available for sale (at fair value)	350	200
Investment in subsidiary	302,980	235,346
Loan to subsidiary	35,000	35,000
Other assets	6,994	556
<b>Total assets</b>	<b>\$ 351,925</b>	<b>\$ 273,972</b>
<b>Liabilities</b>		
Subordinated debentures	\$ 35,000	\$ 35,000
Accrued expenses and other liabilities	1,285	1,195
<b>Total liabilities</b>	<b>36,285</b>	<b>36,195</b>
<b>Stockholders' Equity</b>		
Common stock	16,349	14,827
Additional paid in capital	83,970	27,869
Retained earnings	216,376	199,102
Accumulated other comprehensive income(loss)	(1,055)	(4,021)
<b>Total stockholders' equity</b>	<b>315,640</b>	<b>237,777</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 351,925</b>	<b>\$ 273,972</b>

**Statements of Income**

<i>(In thousands)</i>	Years Ended December 31,		
	2007	2006	2005
<b>Income:</b>			
Cash dividends from subsidiary	\$ 68,880	\$ 13,073	\$ 2,952
Securities gains	0	0	1,758
Other income, principally interest	2,802	2,269	2,324
<b>Total income</b>	<b>71,682</b>	<b>15,342</b>	<b>7,034</b>
<b>Expenses:</b>			
Interest	2,223	2,223	2,223
Other expenses	1,972	1,555	695
<b>Total expenses</b>	<b>4,195</b>	<b>3,778</b>	<b>2,918</b>
Income before income taxes and equity in undistributed income of subsidiary	67,487	11,564	4,116
Income tax expense (benefit)	(309)	(471)	437
Income before equity in undistributed income of subsidiary	67,796	12,035	3,679
Equity in undistributed (excess distributions) income of subsidiary	(35,534)	20,836	29,419
<b>Net income</b>	<b>\$ 32,262</b>	<b>\$ 32,871</b>	<b>\$ 33,098</b>





**Statements of Cash Flows**

<i>(In thousands)</i>	Years Ended December 31,		
	2007	2006	2005
<b>Cash Flows from Operating Activities:</b>			
Net income	\$ 32,262	\$ 32,871	\$ 33,098
Adjustments to reconcile net income to net cash provided by operating activities:			
Excess distributions of (equity in undistributed) income-subsiary	35,534	(20,836)	(29,419)
Investment in subsidiary	(41,176)	0	0
Securities gains	0	0	(1,758)
Stock compensation expense	1,128	624	0
Net change in other liabilities	(142)	(959)	(90)
Other-net	(295)	(91)	(49)
Net cash provided by operating activities	27,311	11,609	1,782
<b>Cash Flows from Investing Activities:</b>			
Net increase in loans receivable	(6,171)	0	0
Proceeds from sales of investments available for sale	0	0	4,249
Increase in note receivable from subsidiary	0	0	(1,435)
Net cash (used) provided by investing activities	(6,171)	0	2,814
<b>Cash Flows from Financing Activities:</b>			
Common stock purchased and retired	(4,354)	(866)	(1,437)
Proceeds from issuance of common stock	1,823	1,424	1,498
Tax benefit from stock options exercised	110	121	0
Dividends paid	(14,988)	(13,028)	(12,329)
Net cash used by financing activities	(17,409)	(12,349)	(12,268)
Net increase (decrease) in cash and cash equivalents	3,731	(740)	(7,672)
Cash and cash equivalents at beginning of year	2,870	3,610	11,282
Cash and cash equivalents at end of year	\$ 6,601	\$ 2,870	\$ 3,610

**Note 22 – Regulatory Matters**

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

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). As of December 31, 2007 and 2006, the capital levels of the Company and the Bank substantially exceeded all capital adequacy requirements to which they are subject.

As of December 31, 2007, the most recent notification from the Bank's primary regulator categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized the Bank must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the table

below. There are no conditions or events since that notification that management believes have changed the Bank's category.

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The Company's and the Bank's actual capital amounts and ratios are also presented in the table:

<i>(Dollars in thousands)</i>	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2007:						
Total Capital (to risk weighted assets):						
Company	\$ 283,571	11.28%	\$ 201,123	8.00%	N/A	
Sandy Spring Bank	269,828	10.77	200,480	8.00	\$ 250,601	10.00%
Tier 1 Capital (to risk weighted assets):						
Company	258,479	10.28	100,561	4.00	N/A	
Sandy Spring Bank	209,737	8.37	100,240	4.00	150,360	6.00
Tier 1 Capital (to average assets):						
Company	258,479	8.87	87,386	3.00	N/A	
Sandy Spring Bank	209,737	7.22	87,156	3.00	145,260	5.00
As of December 31, 2006:						
Total Capital (to risk weighted assets):						
Company	\$ 273,143	13.62%	\$ 160,482	8.00%	N/A	
Sandy Spring Bank	269,629	13.45	160,369	8.00	\$ 200,461	10.00%
Tier 1 Capital (to risk weighted assets):						
Company	253,651	12.64	80,241	4.00	N/A	
Sandy Spring Bank	215,137	10.73	80,185	4.00	120,277	6.00
Tier 1 Capital (to average assets):						
Company	253,651	9.81	77,595	3.00	N/A	
Sandy Spring Bank	215,137	8.32	77,555	3.00	129,258	5.00

### Note 23 - Segment Reporting

The Company operates in four operating segments—Community Banking, Insurance, Leasing and Investment Management. Only Community Banking presently meets the threshold for reportable segment reporting; however, the Company is disclosing separate information for all four operating segments. Each of the operating segments is a strategic business unit that offers different products and services. The Insurance, Leasing and Investment Management segments were businesses that were acquired in separate transactions where management at the time of acquisition was retained. The accounting policies of the segments are the same as those described in Note 1 to the consolidated financial statements. However, the segment data reflect inter-segment transactions and balances.

The Community Banking segment is conducted through Sandy Spring Bank and involves delivering a broad range of financial products and services, including various loan and deposit products to both individuals and businesses. Parent company income is included in the Community Banking segment, as the majority of effort of these functions is related to this segment. Major revenue sources include net interest income, gains on sales of mortgage loans, trust income, fees on sales of investment products and service charges on deposit accounts. Expenses include personnel, occupancy, marketing, equipment and other expenses. Included in Community Banking expenses are non-cash charges associated with amortization of intangibles related to acquired entities totaling \$2.9 million in 2007, \$1.8 million in 2006 and 2005.

The Insurance segment is conducted through Sandy Spring Insurance Corporation, a subsidiary of the Bank, and offers annuities as an alternative to traditional deposit accounts. Sandy Spring Insurance Corporation operates the Chesapeake Insurance Group and Wolfe and Reichelt Insurance Agency, general insurance agencies located in Annapolis, Maryland, and Neff and Associates, located in Ocean City, Maryland. Major sources of revenue are insurance commissions from commercial lines, personal lines, and medical liability lines. Expenses include personnel and support charges. Included in insurance expenses are non-cash charges associated with amortization of intangibles related to acquired entities totaling \$0.4 million in 2007 and 2006 and \$0.2 million in 2005.

The Leasing segment is conducted through The Equipment Leasing Company, a subsidiary of the Bank that provides leases for essential commercial equipment used by small to medium sized businesses. Equipment leasing is conducted through vendor relations and direct solicitation to end-users located primarily in states along the east coast from New Jersey to Florida. The typical lease is categorized as a financing lease and is characterized as a "small ticket" by industry standards, averaging less than \$100 thousand, with individual leases generally not exceeding \$500 thousand. Major revenue sources include interest income. Expenses include personnel and support charges.

The Investment Management segment is conducted through West Financial Services, Inc., a subsidiary of the Bank that was acquired in October 2005. This asset management and financial planning firm, located in McLean, Virginia, provides comprehensive investment management and financial planning to individuals, families, small businesses and associations including cash flow analysis, investment review, tax planning, retirement planning, insurance analysis and estate planning. West Financial currently has approximately \$711 million in assets under management. Major revenue sources include noninterest income earned on the above services. Expenses include personnel and support charges. Included in investment management expenses are non-cash charges associated with amortization of intangibles related to acquired entities totaling \$0.8 million in 2007 and 2006 and \$0.2 million in 2005.

Information about operating segments and reconciliation of such information to the consolidated financial statements follows:

<i>(In thousands)</i>	Community Banking	Insurance	Leasing	Investment Mgmt.	Inter-Segment Elimination	Total
<b>Year ended December 31, 2007</b>						
Interest income	\$ 179,364	\$ 104	\$ 2,759	\$ 70	\$ (1,322)	\$ 180,975
Interest expense	76,319	0	1,152	0	(1,322)	76,149
Provision for loan and lease losses	4,094	0	0	0	0	4,094
Noninterest income	34,680	7,097	818	4,588	(2,894)	44,289
Noninterest expenses	89,930	5,515	1,068	3,848	(573)	99,788
Income before income taxes	43,701	1,686	1,357	810	(2,321)	45,233
Income tax expense	11,439	676	539	317	0	12,971
Net income	\$ 32,262	\$ 1,010	\$ 818	\$ 493	\$ (2,321)	\$ 32,262
Assets	\$ 3,045,055	\$ 12,073	\$ 36,151	\$ 10,037	\$ (59,363)	\$ 3,043,953
<b>Year ended December 31, 2006</b>						
Interest income	\$ 151,982	\$ 68	\$ 2,277	\$ 27	\$ (911)	\$ 153,443
Interest expense	58,780	0	818	0	(911)	58,687
Provision for loan and lease losses	2,795	0	0	0	0	2,795
Noninterest income	29,480	7,452	884	4,115	(3,036)	38,895
Noninterest expense	75,618	5,690	994	3,588	(794)	85,096
Income before income taxes	44,269	1,830	1,349	554	(2,242)	45,760
Income tax expense	11,398	724	554	213	0	12,889
Net income	\$ 32,871	\$ 1,106	\$ 795	\$ 341	\$ (2,242)	\$ 32,871
Assets	\$ 2,608,392	\$ 11,146	\$ 32,843	\$ 8,015	\$ (49,939)	\$ 2,610,457
<b>Year ended December 31, 2005</b>						
Interest income	\$ 120,842	\$ 40	\$ 1,828	\$ 1	\$ (551)	\$ 122,160

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Interest expense	34,023	0	510	0	(551)	33,982
Provision for loan and lease losses	2,600	0	0	0	0	2,600
Noninterest income	31,526	5,916	1,049	866	(2,448)	36,909
Noninterest expense	71,556	4,654	928	795	(739)	77,194
Income before income taxes	44,189	1,302	1,439	72	(1,709)	45,293
Income tax expense	11,091	516	560	28	0	12,195
Net income	\$ 33,098	\$ 786	\$ 879	\$ 44	\$ (1,709)	\$ 33,098
Assets	\$ 2,459,292	\$ 9,274	\$ 26,281	\$ 6,940	\$ (42,171)	\$ 2,459,616

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**Note 24 – Quarterly Financial Results (unaudited)**

A summary of selected consolidated quarterly financial data for the two years ended December 31, 2007 is reported in the following table.

<i>(In thousands, except per share data)</i>	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
<b>2007</b>				
Interest income	\$ 41,894	\$ 46,014	\$ 46,958	\$ 46,109
Net interest income	24,015	26,199	27,212	27,400
Provision for loan and lease losses	839	780	750	1,725
Income before income taxes	10,468	11,333	11,693	11,739
Net income	7,545	8,169	8,181	8,367
Basic net income per share	\$ 0.49	\$ 0.51	\$ 0.50	\$ 0.51
Diluted net income per share	0.49	0.51	0.50	0.51
<b>2006</b>				
Interest income	\$ 35,177	\$ 37,873	\$ 40,018	\$ 40,375
Net interest income	23,177	23,852	24,122	23,605
Provision for loan and lease losses	950	1,045	550	250
Income before income taxes	11,717	11,374	11,468	11,201
Net income	8,340	8,095	8,122	8,314
Basic net income per share	\$ 0.56	\$ 0.55	\$ 0.55	\$ 0.56
Diluted net income per share	0.56	0.54	0.55	0.55

**OTHER MATERIAL REQUIRED BY FORM 10-K****DESCRIPTION OF BUSINESS****General**

Sandy Spring Bancorp, Inc. (the "Company") is the one-bank holding company for Sandy Spring Bank (the "Bank"). The Company is registered as a bank holding company pursuant to the Bank Holding Company Act of 1956, as amended (the "Holding Company Act"). As such, the Company is subject to supervision and regulation by the Board of Governors of the Federal Reserve System (the "Federal Reserve"). The Company began operating in 1988. The Bank was founded in 1868, and is the oldest banking business based in Montgomery County, Maryland. The Bank is independent, community oriented, and conducts a full-service commercial banking business through 42 community offices located in Anne Arundel, Carroll, Frederick, Howard, Montgomery and Prince George's counties in Maryland, and Fairfax and Loudoun counties in Virginia. The Bank is a state chartered bank subject to supervision and regulation by the Federal Reserve and the state of Maryland. The Bank's deposit accounts are insured by the Deposit Insurance Fund administered by the Federal Deposit Insurance Corporation (the "FDIC") to the maximum permitted by law. The Bank is a member of the Federal Reserve System and is an Equal Housing Lender. The Company, the Bank, and its other subsidiaries are Affirmative Action/Equal Opportunity Employers.

The Bank experiences substantial competition both in attracting and retaining deposits and in making loans. Direct competition for deposits comes from other commercial banks, savings associations, and credit unions located in the



Bank's primary market area of Anne Arundel, Carroll, Frederick, Howard, Montgomery and Prince George's counties in Maryland, and Fairfax and Loudoun counties in Virginia. Additional significant competition for deposits comes from mutual funds and corporate and government debt securities. Sandy Spring Insurance Corporation ("SSIC"), a wholly-owned subsidiary of the Bank, offers annuities as an alternative to traditional deposit accounts. SSIC also operates the Chesapeake Insurance Group, a general insurance agency located in Annapolis, Maryland, which faces competition primarily from other insurance agencies and insurance companies. In October 2005, the Company acquired West Financial Services, Inc. ("WFS"), an asset management and financial planning company located in McLean, Virginia. WFS faces competition primarily from other financial planners, banks, and financial management companies. In January 2006, the Company acquired Neff & Associates ("Neff"), an insurance agency located in Ocean City, Maryland. Neff faces competition primarily from other insurance agencies and insurance companies. The primary factors in competing for loans are interest rates, loan origination fees, and the range of services offered by lenders. Competitors for loan originations include other commercial banks, mortgage bankers, mortgage brokers, savings associations, and insurance companies. Equipment leasing through the equipment leasing subsidiary basically involves the same competitive factors as lending, with competition from other equipment leasing companies. Management believes the Bank is able to compete effectively in its primary market area.

The Company's and the Bank's principal executive office is located at 17801 Georgia Avenue, Olney, Maryland 20832, and its telephone number is 301-774-6400. The Company's Web site is located at [www.sandyspringbank.com](http://www.sandyspringbank.com).

### **Loan and Lease Products**

**Residential Real Estate Loans.** The residential real estate category contains loans principally to consumers secured by residential real estate. The Company's residential real estate lending policy requires each loan to have viable repayment sources. Residential real estate loans are evaluated for the adequacy of these repayment sources at the time of approval, based upon measures including credit scores, debt-to-income ratios, and collateral values. Credit risk for residential real estate loans arises from borrowers lacking the ability or willingness to repay the loan, and by a shortfall in the value of the residential real estate in relation to the outstanding loan balance in the event of a default and subsequent liquidation of the real estate collateral. The residential real estate portfolio includes both conforming and nonconforming mortgage loans. Conforming mortgage loans represent loans originated in accordance with underwriting standards set forth by the government-sponsored entities ("GSEs"), including the Federal National Mortgage Association ("Fannie Mae"), the Federal Home Loan Mortgage Corporation ("Freddie Mac"), and the Government National Mortgage Association ("Ginnie Mae"), which serve as the primary purchasers of loans sold in the secondary mortgage market by mortgage lenders. These loans are generally collateralized by one-to-four-family residential real estate, have loan-to-collateral value ratios of 80% or less or have mortgage insurance to insure down to 80%, and are made to borrowers in good credit standing. Substantially all fixed-rate conforming loans originated are sold in the secondary mortgage market. For any loans retained by the Company, title insurance insuring the priority of its mortgage lien, as well as fire and extended coverage casualty insurance protecting the properties securing the loans are required. Borrowers may be required to advance funds, with each monthly payment of principal and interest, to a loan escrow account from which the Company makes disbursements for items such as real estate taxes and mortgage insurance premiums. Appraisers approved by the Company appraise the properties securing substantially all of the Company's residential mortgage loans.

Nonconforming mortgage loans represent loans that generally are not saleable in the secondary market to the GSEs for inclusion in conventional mortgage-backed securities due to the credit characteristics of the borrower, the underlying documentation, the loan-to-value ratio, or the size of the loan, among other factors. The Company originates nonconforming loans for its own portfolio and for sale to third-party investors, usually large mortgage companies, under commitments by them to purchase subject to compliance with pre-established investor criteria. These nonconforming loans generated for sale include some residential mortgage credits that may be categorized as sub-prime under federal banking regulations. Such sub-prime credits typically remain on the Company's consolidated books after funding for thirty days or less, and are included in residential mortgages held for sale on the face of the balance sheet. The Company also holds occasional, isolated credits that inadvertently failed to meet GSE or other third-party investor criteria, or that were originated and managed in the ordinary course of business (rather than in any sub-prime lending program) and may have characteristics that could cause them to be categorized as sub-prime. The Company's current practice is to sell all such sub-prime loans to third-party investors. The Company believes that the sub-prime credits it originates or holds and the risks they entail are not significant to its financial condition, results of operations, liquidity, or capital resources.

The Company engages in sales of residential mortgage loans originated by the Bank. The Company's current practice is to sell loans on a servicing released basis.

The Company makes residential real estate development and construction loans generally to provide interim financing on property during the development and construction period. Borrowers include builders, developers and persons who will ultimately occupy the single-family dwelling. Residential real estate development and construction loan funds are disbursed periodically as pre-specified stages of completion are attained based upon site inspections. Interest rates on these loans are usually adjustable. Loans to individuals for the construction of primary personal residences are typically secured by the property under construction, frequently include additional collateral (such as a second

mortgage on the borrower's present home), and commonly have maturities of six to twelve months. The Company attempts to obtain the permanent mortgage loan under terms, conditions and documentation standards that permit the sale of the mortgage loan in the secondary mortgage loan market. The Company's practice is to immediately sell substantially all fixed-rate residential mortgage loans in the secondary market with servicing released.

Commercial Loans and Leases. The Company devotes significant resources and attention to seeking and then serving commercial clients. Included in this category are commercial real estate loans, commercial construction loans, leases and other commercial loans. Over the years, the Company's commercial loan clients have come to represent a diverse cross-section of small to mid-size local businesses, whose owners and employees are often established Bank customers. Such banking relationships are a natural business for the Company, with its long-standing community roots and extensive experience in serving and lending to this market segment.

Commercial loans are evaluated for the adequacy of repayment sources at the time of approval and are regularly reviewed for any possible deterioration in the ability of the borrower to repay the loan. Collateral generally is required to provide the Company with an additional source of repayment in the event of default by a commercial borrower. The structure of the collateral package, including the type and amount of the collateral, varies from loan to loan depending on the financial strength of the borrower, the amount and terms of the loan, and the collateral available to be pledged by the borrower, but generally may include real estate, accounts receivable, inventory, equipment or other assets. Loans also may be supported by personal guarantees from the principals of the commercial loan borrowers. The financial condition and cash flow of commercial borrowers are closely monitored by the submission of corporate financial statements, personal financial statements and income tax returns. The frequency of submissions of required information depends upon the size and complexity of the credit and the collateral that secures the loan. Credit risk for commercial loans arises from borrowers lacking the ability or willingness to repay the loan, and in the case of secured loans, by a shortfall in the collateral value in relation to the outstanding loan balance in the event of a default and subsequent liquidation of collateral. The Company has no commercial loans to borrowers in similar industries that exceed 10% of total loans.

Included in commercial loans are credits directly originated by the Company and syndicated transactions or loan participations that are originated by other lenders. The Corporation's commercial lending policy requires each loan, regardless of whether it is directly originated or is purchased, to have viable repayment sources. The risks associated with syndicated loans or purchased participations are similar to those of directly originated commercial loans, although additional risk may arise from the limited ability to control actions of the primary lender. Shared National Credits (SNC), as defined by the banking regulatory agencies, represent syndicated lending arrangements with three or more participating financial institutions and credit exceeding \$20.0 million in the aggregate. As of December 31, 2007, the Company had \$48.1 million in SNC purchased outstanding and no SNC sold outstanding. The Company also sells participations in loans it originates to other financial institutions in order to build long-term customer relationships or limit loan concentration. Strict policies are in place governing the degree of risk assumed and volume of loans held. At December 31, 2007, other financial institutions had \$10.8 million in outstanding commercial and commercial real estate loan participations sold by the Company, and the Company had \$39.4 million in outstanding commercial and commercial real estate loan participations purchased from other lenders, excluding SNC.

The Company's commercial real estate loans consist of loans secured by owner occupied properties where an established banking relationship exists and involves investment properties for warehouse, retail, and office space with a history of occupancy and cash flow. The commercial real estate category contains mortgage loans to developers and owners of commercial real estate. Commercial real estate loans are governed by the same lending policies and subject to credit risk as previously described for commercial loans. Although terms and amortization periods vary, the Company's commercial mortgages generally have maturities or repricing opportunities of five years or less. The Company seeks to reduce the risks associated with commercial mortgage lending by generally lending in its market area, using conservative loan-to-value ratios and obtaining periodic financial statements and tax returns from borrowers to perform annual loan reviews. It is also the Company's general policy to obtain personal guarantees from the principals of the borrowers and to underwrite the business entity from a cash flow perspective.

Commercial real estate loans secured by owner occupied properties are based upon the borrower's financial health and the ability of the borrower and the business to repay. Whenever appropriate and available, the Bank seeks governmental loan guarantees, such as the Small Business Administration loan programs, to reduce risks. All borrowers are required to forward annual corporate, partnership and personal financial statements. Interest rate risks are mitigated by using either floating interest rates or by fixing rates for a short period of time, generally less than three years. While loan amortizations may be approved for up to 300 months, each loan generally has a call provision (maturity date) of five years or less. A risk rating system is used to determine loss exposure.

The Company lends for commercial construction in markets it knows and understands, works selectively with local, top-quality builders and developers, and requires substantial equity from its borrowers. The underwriting process is

designed to confirm that the project will be economically feasible and financially viable; it is generally evaluated as though the Company will provide permanent financing. The Company's portfolio growth objectives do not include speculative commercial construction projects or projects lacking reasonable proportionate sharing of risk. The Company has limited loan losses in this area of lending through monitoring of development and construction loans with on-site inspections and control of disbursements on loans in process. Development and construction loans are secured by the properties under development or construction and personal guarantees are typically obtained. Further, to assure that reliance is not placed solely upon the value of the underlying collateral, the Company considers the financial condition and reputation of the borrower and any guarantors, the amount of the borrower's equity in the project, independent appraisals, cost estimates and pre-construction sales information.

Residential construction loans to residential builders are generally made for the construction of residential homes for which a binding sales contract exists and the prospective buyers had been pre-qualified for permanent mortgage financing by either third-party lenders (mortgage companies or other financial institutions) or the Company. Loans for the development of residential land are extended when evidence is provided that the lots under development will be or have been sold to builders satisfactory to the Company. These loans are generally extended for a period of time sufficient to allow for the clearing and grading of the land and the installation of water, sewer and roads, typically a minimum of eighteen months to three years. In addition, residential land development loans generally carry a loan-to-value ratio not to exceed 75% of the value of the project as completed.

The Company's equipment leasing business is, for the most part, technology based, consisting of a portfolio of leases for essential commercial equipment used by small to medium sized businesses. Equipment leasing is conducted through vendor relations and direct solicitation to end-users located primarily in east coast states from New Jersey to Florida. The typical lease is "small ticket" by industry standards, averaging less than \$100 thousand, with individual leases generally not exceeding \$500 thousand. Terms generally are fixed payment for up to five years. Leases are extended based primarily upon the ability of the borrower to pay rather than the value of the leased property.

The Company makes other commercial loans. Commercial term loans are made to provide funds for equipment and general corporate needs. This loan category is designed to support borrowers who have a proven ability to service debt over a term generally not to exceed 84 months. The Company generally requires a first lien position on all collateral and requires guarantees from owners having at least a 20% interest in the involved business. Interest rates on commercial term loans are generally floating or fixed for a term not to exceed five years. Management carefully monitors industry and collateral concentrations to avoid loan exposures to a large group of similar industries or similar collateral. Commercial loans are evaluated for historical and projected cash flow attributes, balance sheet strength, and primary and alternate resources of personal guarantors. Commercial term loan documents require borrowers to forward regular financial information on both the business and personal guarantors. Loan covenants require at least annual submission of complete financial information and in certain cases this information is required monthly, quarterly or semi-annually depending on the degree to which the Company desires information resources for monitoring a borrower's financial condition and compliance with loan covenants. Examples of properly margined collateral for loans, as required by bank policy, would be a 75% advance on the lesser of appraisal or recent sales price on commercial property, an 80% or less advance on eligible receivables, a 50% or less advance on eligible inventory and an 80% advance on appraised residential property. Collateral borrowing certificates may be required to monitor certain collateral categories on a monthly or quarterly basis. Loans may require personal guarantees. Key person life insurance may be required as appropriate and as necessary to mitigate the risk of loss of a primary owner or manager.

Commercial lines of credit are granted to finance a business borrower's short-term credit needs and/or to finance a percentage of eligible receivables and inventory. In addition to the risks inherent in term loan facilities, line of credit borrowers typically require additional monitoring to protect the lender against increasing loan volumes and diminishing collateral values. Commercial lines of credit are generally revolving in nature and require close scrutiny. The Company generally requires at least an annual out of debt period (for seasonal borrowers) or regular financial information (monthly or quarterly financial statements, borrowing base certificates, etc.) for borrowers with more growth and greater permanent working capital financing needs. Advances against collateral value are limited. Lines of credit and term loans to the same borrowers generally are cross-defaulted and cross-collateralized. Interest rate charges on this group of loans generally float at a factor at or above the prime lending rate.

**Consumer Lending.** Consumer lending continues to be very important to the Company's full-service, community banking business. This category of loans includes primarily home equity loans and lines, installment loans, personal lines of credit, marine loans and student loans.

The home equity category consists mainly of revolving lines of credit to consumers which are secured by residential real estate. Home equity lines of credit and other home equity loans are originated by the Company for typically up to 90% of the appraised value, less the amount of any existing prior liens on the property. While home equity loans have maximum terms of up to twenty years and interest rates are generally fixed, home equity lines of credit have maximum terms of up to ten years for draws and thirty years for repayment, and interest rates are generally adjustable. The Company secures these loans with mortgages on the homes (typically a second mortgage). Purchase money second mortgage loans originated by the Company have maximum terms ranging from ten to thirty years. These loans generally carry a fixed rate of interest for the entire term or a fixed rate of interest for the first five years, repricing every five years thereafter at a predetermined spread to the prime rate of interest. Home equity lines are generally governed by the same lending policies and subject to credit risk as described above for residential real estate loans.

Other consumer loans include installment loans used by customers to purchase automobiles, boats, recreational vehicles, and student loans. These consumer loans are generally governed by the same overall lending policies as described for residential real estate. Credit risk for consumer loans arises from borrowers lacking the ability or willingness to repay the loan, and in the case of secured loans, by a shortfall in the value of the collateral in relation to the outstanding loan balance in the event of a default and subsequent liquidation of collateral.

Consumer installment loans are generally offered for terms of up to five years at fixed interest rates. The Company makes loans for automobiles, recreational vehicles, and marine craft, both new and used, directly to the borrowers. Automobile loans can be for up to 100% of the purchase price or the retail value listed by the National Automobile Dealers Association. The terms of the loans are determined by the age and condition of the collateral. Collision insurance policies are required on all these loans, unless the borrower has substantial other assets and income. The Company's student loans are made in amounts of up to \$20,500 per year. The Company offers a variety of graduate and undergraduate loan programs under the Federal Family Education Loan Program. Interest is capitalized annually until the student leaves school and amortization over a ten-year period then begins. It is the Company's practice to sell all such loans in the secondary market when the student leaves school. The Company also makes other consumer loans, which may or may not be secured. The term of the loans usually depends on the collateral. Unsecured loans usually do not exceed \$50 thousand and have a term of no longer than 36 months.

### **Availability of Filings Through the Company's Website**

The Company provides internet access to annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, ownership reports on Forms 3, 4, and 5, and amendments to those reports, through the Investor Relations area of the Company's Web site, at [www.sandyspringbank.com](http://www.sandyspringbank.com). Access to these reports is provided by means of a link to a third-party vendor that maintains a database of such filings. In general, the Company intends that these reports be available as soon as reasonably practicable after they are filed with or furnished to the SEC. However, technical and other operational obstacles or delays caused by the vendor may delay their availability. The SEC maintains a Web site ([www.sec.gov](http://www.sec.gov)) where these filings also are available through the SEC's EDGAR system. There is no charge for access to these filings through either the Company's site or the SEC's site.

### **Regulation, Supervision, and Governmental Policy**

Following is a brief summary of certain statutes and regulations that significantly affect the Company and the Bank. A number of other statutes and regulations affect the Company and the Bank but are not summarized below.

Bank Holding Company Regulation. The Company is registered as a bank holding company under the Holding Company Act and, as such, is subject to supervision and regulation by the Federal Reserve. As a bank holding company, the Company is required to furnish to the Federal Reserve annual and quarterly reports of its operations and additional information and reports. The Company is also subject to regular examination by the Federal Reserve.

Under the Holding Company Act, a bank holding company must obtain the prior approval of the Federal Reserve before (1) acquiring direct or indirect ownership or control of any class of voting securities of any bank or bank holding company if, after the acquisition, the bank holding company would directly or indirectly own or control more than 5% of the class; (2) acquiring all or substantially all of the assets of another bank or bank holding company; or (3) merging or consolidating with another bank holding company.

Under the Holding Company Act, any company must obtain approval of the Federal Reserve prior to acquiring control of the Company or the Bank. For purposes of the Holding Company Act, "control" is defined as ownership of 25% or more of any class of voting securities of the Company or the Bank, the ability to control the election of a majority of the directors, or the exercise of a controlling influence over management or policies of the Company or the Bank.

The Change in Bank Control Act and the related regulations of the Federal Reserve require any person or persons acting in concert (except for companies required to make application under the Holding Company Act), to file a written notice with the Federal Reserve before the person or persons acquire control of the Company or the Bank. The Change in Bank Control Act defines "control" as the direct or indirect power to vote 25% or more of any class of voting securities or to direct the management or policies of a bank holding company or an insured bank.

The Holding Company Act also limits the investments and activities of bank holding companies. In general, a bank holding company is prohibited from acquiring direct or indirect ownership or control of more than 5% of the voting shares of a company that is not a bank or a bank holding company or from engaging directly or indirectly in activities other than those of banking, managing or controlling banks, providing services for its subsidiaries, non-bank activities that are closely related to banking, and other financially related activities. The activities of the Company are subject to these legal and regulatory limitations under the Holding Company Act and Federal Reserve regulations.

In general, bank holding companies that qualify as financial holding companies under federal banking law may engage in an expanded list of non-bank activities. Non-bank and financially related activities of bank holding companies, including companies that become financial holding companies, also may be subject to regulation and oversight by regulators other than the Federal Reserve. The Company is not a financial holding company, but may choose to become one in the future.



The Federal Reserve has the power to order a holding company or its subsidiaries to terminate any activity, or to terminate its ownership or control of any subsidiary, when it has reasonable cause to believe that the continuation of such activity or such ownership or control constitutes a serious risk to the financial safety, soundness, or stability of any bank subsidiary of that holding company.

The Federal Reserve has adopted guidelines regarding the capital adequacy of bank holding companies, which require bank holding companies to maintain specified minimum ratios of capital to total assets and capital to risk-weighted assets. See "Regulatory Capital Requirements."

The Federal Reserve has the power to prohibit dividends by bank holding companies if their actions constitute unsafe or unsound practices. The Federal Reserve has issued a policy statement on the payment of cash dividends by bank holding companies, which expresses the Federal Reserve's view that a bank holding company should pay cash dividends only to the extent that the company's net income for the past year is sufficient to cover both the cash dividends and a rate of earnings retention that is consistent with the company's capital needs, asset quality, and overall financial condition.

Bank Regulation. On September 21, 2001, the Bank's application to the Maryland State Commissioner of Financial Regulation to become a state chartered bank and trust company was approved and the Bank began operations as such. The Bank previously was a national bank regulated by the United States Comptroller of the Currency. The Bank is a member of the Federal Reserve System and is subject to supervision by the Federal Reserve and the State of Maryland. Deposits of the Bank are insured by the FDIC to the legal maximum of \$100 thousand for each insured depositor. Deposits, reserves, investments, loans, consumer law compliance, issuance of securities, payment of dividends, establishment of branches, mergers and acquisitions, corporate activities, changes in control, electronic funds transfers, responsiveness to community needs, management practices, compensation policies, and other aspects of operations are subject to regulation by the appropriate federal and state supervisory authorities. In addition, the Bank is subject to numerous federal, state and local laws and regulations which set forth specific restrictions and procedural requirements with respect to extensions of credit (including to insiders), credit practices, disclosure of credit terms and discrimination in credit transactions.

The Federal Reserve regularly examines the operations and condition of the Bank, including, but not limited to, its capital adequacy, reserves, loans, investments, and management practices. These examinations are for the protection of the Bank's depositors and the Deposit Insurance Fund. In addition, the Bank is required to furnish quarterly and annual reports to the Federal Reserve. The Federal Reserve's enforcement authority includes the power to remove officers and directors and the authority to issue cease-and-desist orders to prevent a bank from engaging in unsafe or unsound practices or violating laws or regulations governing its business.

The Federal Reserve has adopted regulations regarding capital adequacy, which require member banks to maintain specified minimum ratios of capital to total assets and capital to risk-weighted assets. See "Regulatory Capital Requirements." Federal Reserve and State regulations limit the amount of dividends that the Bank may pay to the Company. See "Note 12 - Stockholders' Equity" of the Notes to the Consolidated Financial Statements.

The Bank is subject to restrictions imposed by federal law on extensions of credit to, and certain other transactions with, the Company and other affiliates, and on investments in their stock or other securities. These restrictions prevent the Company and the Bank's other affiliates from borrowing from the Bank unless the loans are secured by specified collateral, and require those transactions to have terms comparable to terms of arms-length transactions with third persons. In addition, secured loans and other transactions and investments by the Bank are generally limited in amount as to the Company and as to any other affiliate to 10% of the Bank's capital and surplus and as to the Company and all other affiliates together to an aggregate of 20% of the Bank's capital and surplus. Certain exemptions to these limitations apply to extensions of credit and other transactions between the Bank and its subsidiaries. These regulations and restrictions may limit the Company's ability to obtain funds from the Bank for its cash needs, including funds for acquisitions and for payment of dividends, interest, and operating expenses.

Under Federal Reserve regulations, banks must adopt and maintain written policies that establish appropriate limits and standards for extensions of credit secured by liens or interests in real estate or are made for the purpose of financing permanent improvements to real estate. These policies must establish loan portfolio diversification

standards; prudent underwriting standards, including loan-to-value limits, that are clear and measurable; loan administration procedures; and documentation, approval, and reporting requirements. A bank's real estate lending policy must reflect consideration of the Interagency Guidelines for Real Estate Lending Policies (the "Interagency Guidelines") adopted by the federal bank regulators. The Interagency Guidelines, among other things, call for internal loan-to-value limits for real estate loans that are not in excess of the limits specified in the Guidelines. The Interagency Guidelines state, however, that it may be appropriate in individual cases to originate or purchase loans with loan-to-value ratios in excess of the supervisory loan-to-value limits.

The FDIC has established a risk-based deposit insurance premium assessment system for insured depository institutions. Under the current system, insured institutions are assigned to one of four risk categories based on supervisory evaluations, regulatory capital levels and certain other factors. An institution's assessment rate depends upon the category to which it is assigned. Risk category I, which contains the least risky depository institutions, is expected to include more than 90% of all institutions. Unlike the other categories, Risk Category I contains further risk differentiation based on the FDIC's analysis of financial ratios, examination component ratings and other information. Assessment rates are determined by the FDIC and currently range from five to seven basis points for the healthiest institutions (Risk Category I) to 43 basis points of assessable deposits for the riskiest (Risk Category IV). The FDIC may adjust rates uniformly from one quarter to the next, except that no single adjustment can exceed three basis points. No institution may pay a dividend if in default of its FDIC assessment.

Regulatory Capital Requirements. The Federal Reserve has established guidelines for maintenance of appropriate levels of capital by bank holding companies and member banks. The regulations impose two sets of capital adequacy requirements: minimum leverage rules, which require bank holding companies and banks to maintain a specified minimum ratio of capital to total assets, and risk-based capital rules, which require the maintenance of specified minimum ratios of capital to risk-weighted assets. These capital regulations are subject to change.

The regulations of the Federal Reserve require bank holding companies and member banks to maintain a minimum leverage ratio of "Tier 1 capital" (as defined in the risk-based capital guidelines discussed in the following paragraphs) to total assets of 3.0%. The capital regulations state, however, that only the strongest bank holding companies and banks, with composite examination ratings of 1 under the rating system used by the federal bank regulators, would be permitted to operate at or near this minimum level of capital. All other bank holding companies and banks are expected to maintain a leverage ratio of at least 1% to 2% above the minimum ratio, depending on the assessment of an individual organization's capital adequacy by its primary regulator. A bank or bank holding company experiencing or anticipating significant growth is expected to maintain capital well above the minimum levels. In addition, the Federal Reserve has indicated that it also may consider the level of an organization's ratio of tangible Tier 1 capital (after deducting all intangibles) to total assets in making an overall assessment of capital.

The risk-based capital rules of the Federal Reserve require bank holding companies and member banks to maintain minimum regulatory capital levels based upon a weighting of their assets and off-balance sheet obligations according to risk. The risk-based capital rules have two basic components: a core capital (Tier 1) requirement and a supplementary capital (Tier 2) requirement. Core capital consists primarily of common stockholders' equity, certain perpetual preferred stock (noncumulative perpetual preferred stock with respect to banks), and minority interests in the equity accounts of consolidated subsidiaries; less all intangible assets, except for certain mortgage servicing rights and purchased credit card relationships. Supplementary capital elements include, subject to certain limitations, the allowance for losses on loans and leases; perpetual preferred stock that does not qualify as Tier 1 capital; long-term preferred stock with an original maturity of at least 20 years from issuance; hybrid capital instruments, including perpetual debt and mandatory convertible securities; subordinated debt, intermediate-term preferred stock, and up to 45% of pre-tax net unrealized gains on available-for-sale equity securities.

The risk-based capital regulations assign balance sheet assets and credit equivalent amounts of off-balance sheet obligations to one of four broad risk categories based principally on the degree of credit risk associated with the obligor. The assets and off-balance sheet items in the four risk categories are weighted at 0%, 20%, 50% and 100%. These computations result in the total risk-weighted assets.

The risk-based capital regulations require all commercial banks and bank holding companies to maintain a minimum ratio of total capital to total risk-weighted assets of 8%, with at least 4% as core capital. For the purpose of calculating these ratios: (i) supplementary capital is limited to no more than 100% of core capital; and (ii) the aggregate amount of certain types of supplementary capital is limited. In addition, the risk-based capital regulations limit the allowance for credit losses that may be included in capital to 1.25% of total risk-weighted assets.

The federal bank regulatory agencies have established a joint policy regarding the evaluation of commercial banks' capital adequacy for interest rate risk. Under the policy, the Federal Reserve's assessment of a bank's capital adequacy includes an assessment of the bank's exposure to adverse changes in interest rates. The Federal Reserve has determined to rely on its examination process for such evaluations rather than on standardized measurement systems or formulas. The Federal Reserve may require banks that are found to have a high level of interest rate risk exposure or weak interest rate risk management systems to take corrective actions. Management believes its interest rate risk management systems and its capital relative to its interest rate risk are adequate.

Federal banking regulations also require banks with significant trading assets or liabilities to maintain supplemental risk-based capital based upon their levels of market risk. The Bank did not have significant levels of trading assets or

liabilities during 2007, and was not required to maintain such supplemental capital.

Well-capitalized institutions are not subject to limitations on brokered deposits, while an adequately capitalized institution is able to accept, renew, or rollover brokered deposits only with a waiver from the FDIC and subject to certain restrictions on the yield paid on such deposits. Undercapitalized institutions are not permitted to accept brokered deposits.

The Federal Reserve has established regulations that classify banks by capital levels and provide for the Federal Reserve to take various "prompt corrective actions" to resolve the problems of any bank that fails to satisfy the capital standards. Under these regulations, a well-capitalized bank is one that is not subject to any regulatory order or directive to meet any specific capital level and that has a total risk-based capital ratio of 10% or more, a Tier 1 risk-based capital ratio of 6% or more, and a leverage ratio of 5% or more. An adequately capitalized bank is one that does not qualify as well-capitalized but meets or exceeds the following capital requirements: a total risk-based capital ratio of 8%, a Tier 1 risk-based capital ratio of 4%, and a leverage ratio of either (i) 4% or (ii) 3% if the bank has the highest composite examination rating. A bank that does not meet these standards is categorized as undercapitalized, significantly undercapitalized, or critically undercapitalized, depending on its capital levels. A bank that falls within any of the three undercapitalized categories established by the prompt corrective action regulation is subject to severe regulatory sanctions. As of December 31, 2007, the Bank was well-capitalized as defined in the Federal Reserve's regulations.

For information regarding the Company's and the Bank's compliance with their respective regulatory capital requirements, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Capital Management" of this report, and "Note 11-Long-term Borrowings," and "Note 22 – Regulatory Matters" of the Notes to the Consolidated Financial Statements of this report.

### **Supervision and Regulation of Mortgage Banking Operations**

The Company's mortgage banking business is subject to the rules and regulations of the U.S. Department of Housing and Urban Development ("HUD"), the Federal Housing Administration ("FHA"), the Veterans' Administration ("VA"), and the Fannie Mae with respect to originating, processing, selling and servicing mortgage loans. Those rules and regulations, among other things, prohibit discrimination and establish underwriting guidelines, which include provisions for inspections and appraisals, require credit reports on prospective borrowers, and fix maximum loan amounts. Lenders such as the Company are required annually to submit audited financial statements to Fannie Mae, FHA and VA. Each of these regulatory entities has its own financial requirements. The Company's affairs are also subject to examination by the Federal Reserve, Fannie Mae, FHA and VA at all times to assure compliance with the applicable regulations, policies and procedures. Mortgage origination activities are subject to, among others, the Equal Credit Opportunity Act, Federal Truth-in-Lending Act, Fair Housing Act, Fair Credit Reporting Act, the National Flood Insurance Act and the Real Estate Settlement Procedures Act and related regulations that prohibit discrimination and require the disclosure of certain basic information to mortgagors concerning credit terms and settlement costs. The Company's mortgage banking operations also are affected by various state and local laws and regulations and the requirements of various private mortgage investors.

### **Community Reinvestment**

Under the Community Reinvestment Act ("CRA"), a financial institution has a continuing and affirmative obligation to help meet the credit needs of the entire community, including low and moderate income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions, or limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community. However, institutions are rated on their performance in meeting the needs of their communities. Performance is tested in three areas: (a) lending, to evaluate the institution's record of making loans in its assessment areas; (b) investment, to evaluate the institution's record of investing in community development projects, affordable housing, and programs benefiting low or moderate income individuals and businesses; and (c) service, to evaluate the institution's delivery of services through its branches, ATMs and other offices. The CRA requires each federal banking agency, in connection with its examination of a financial institution, to assess and assign one of four ratings to the institution's record of meeting the credit needs of the community and to take such record into account in its evaluation of certain applications by the institution, including applications for charters, branches and other deposit facilities, relocations, mergers, consolidations, acquisitions of assets or assumptions of liabilities, and savings and loan holding company acquisitions. The CRA also requires that all institutions make public, disclosure of their CRA ratings. The Bank was assigned a "satisfactory" rating as a result of its last CRA examination.

### **Bank Secrecy Act**

Under the Bank Secrecy Act ("BSA"), a financial institution is required to have systems in place to detect certain transactions, based on the size and nature of the transaction. Financial institutions are generally required to report cash transactions involving more than \$10,000 to the United States Treasury. In addition, financial institutions are required to file suspicious activity reports for transactions that involve more than \$5,000 and which the financial institution knows, suspects, or has reason to suspect involves illegal funds, is designed to evade the requirements of the BSA, or has no lawful purpose. The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act, commonly referred to as the "USA Patriot Act" or the "Patriot Act", enacted in response to the September 11, 2001, terrorist attacks, enacted prohibitions against specified financial transactions and account relationships, as well as enhanced due diligence standards intended to prevent the use of the United States financial system for money laundering and terrorist financing activities. The Patriot Act requires banks and other depository institutions, brokers, dealers and certain other businesses involved in the transfer of money to establish anti-money

laundering programs, including employee training and independent audit requirements meeting minimum standards specified by the act, to follow standards for customer identification and maintenance of customer identification records, and to compare customer lists against lists of suspected terrorists, terrorist organizations and money launderers. The Patriot Act also requires federal bank regulators to evaluate the effectiveness of an applicant in combating money laundering in determining whether to approve a proposed bank acquisition.

### **Sarbanes-Oxley Act of 2002**

The Sarbanes-Oxley Act of 2002 (“Sarbanes-Oxley”) established a broad range of corporate governance and accounting measures intended to increase corporate responsibility and protect investors by improving the accuracy and reliability of disclosures under federal securities laws. The Company is subject to Sarbanes-Oxley because it is required to file periodic reports with the SEC under the Securities and Exchange Act of 1934. Among other things, Sarbanes-Oxley, its implementing regulations and related Nasdaq Stock Market rules have established membership requirements and additional responsibilities for the Company’s audit committee, imposed restrictions on the relationship between the Company and its outside auditors (including restrictions on the types of non-audit services our auditors may provide to us), imposed additional financial statement certification responsibilities for the Company’s chief executive officer and chief financial officer, expanded the disclosure requirements for corporate insiders, required management to evaluate the Company’s disclosure controls and procedures and its internal control over financial reporting, and required the Company’s auditors to issue a report on our internal control over financial reporting.

### **Other Laws and Regulations**

Some of the aspects of the lending and deposit business of the Bank that are subject to regulation by the Federal Reserve and the FDIC include reserve requirements and disclosure requirements in connection with personal and mortgage loans and deposit accounts. The Bank’s federal student lending activities are subject to regulation and examination by the United States Department of Education. In addition, the Bank is subject to numerous federal and state laws and regulations that include specific restrictions and procedural requirements with respect to the establishment of branches, investments, interest rates on loans, credit practices, the disclosure of credit terms, and discrimination in credit transactions.

### **Enforcement Actions**

Federal statutes and regulations provide financial institution regulatory agencies with great flexibility to undertake an enforcement action against an institution that fails to comply with regulatory requirements. Possible enforcement actions range from the imposition of a capital plan and capital directive to civil money penalties, cease-and-desist orders, receivership, conservatorship, or the termination of the deposit insurance.

## **RISK FACTORS**

Investing in our common stock involves risks. You should carefully consider the following risk factors before you decide to make an investment decision regarding our stock. The risk factors may cause our future earnings to be lower or our financial condition to be less favorable than we expect. In addition, other risks of which we are not aware, or which we do not believe are material, may cause earnings to be lower, or may hurt our financial condition. You should also consider the other information in this Annual Report on Form 10-K, as well as in the documents incorporated by reference into it.

***Changes in interest rates and other factors beyond our control may adversely affect our earnings and financial condition.***

Our net income depends to a great extent upon the level of our net interest income. Changes in interest rates can increase or decrease net interest income and net income. Net interest income is the difference between the interest income we earn on loans, investments, and other interest-earning assets, and the interest we pay on interest-bearing liabilities, such as deposits and borrowings. Net interest income is affected by changes in market interest rates, because different types of assets and liabilities may react differently, and at different times, to market interest rate changes. When interest-bearing liabilities mature or reprice more quickly than interest-earning assets in a period, an increase in market rates of interest could reduce net interest income. Similarly, when interest-earning assets mature or reprice more quickly than interest-bearing liabilities, falling interest rates could reduce net interest income.



Changes in market interest rates are affected by many factors beyond our control, including inflation, unemployment, money supply, international events, and events in world financial markets. We attempt to manage our risk from changes in market interest rates by adjusting the rates, maturity, repricing, and balances of the different types of interest-earning assets and interest-bearing liabilities, but interest rate risk management techniques are not exact. As a result, a rapid increase or decrease in interest rates could have an adverse effect on our net interest margin and results of operations. Changes in the market interest rates for types of products and services in our various markets also may vary significantly from location to location and over time based upon competition and local or regional economic factors. At December 31, 2007, our interest rate sensitivity simulation model projected that net interest income would decrease by 1.01% if interest rates immediately fell by 200 basis points and would decrease by 6.12% if interest rates immediately rose by 200 basis points. The results of our interest rate sensitivity simulation model depend upon a number of assumptions which may not prove to be accurate. There can be no assurance that we will be able to successfully manage our interest rate risk. Please see "Market Risk Management" on page 22 of this report.

***Changes in local economic conditions could adversely affect our business.***

Our commercial and commercial real estate lending operations are concentrated in Anne Arundel, Frederick, Howard, Montgomery, and Prince George's counties in Maryland, and Fairfax and Loudoun counties in Virginia. Our success depends in part upon economic conditions in these markets. Adverse changes in economic conditions in these markets could reduce our growth in loans and deposits, impair our ability to collect our loans, increase our problem loans and charge-offs, and otherwise negatively affect our performance and financial condition.

***Our allowance for loan and lease losses may not be adequate to cover our actual loan and lease losses, which could adversely affect our earnings.***

We maintain an allowance for loan and lease losses in an amount that we believe is adequate to provide for probable losses in the portfolio. While we strive to carefully monitor credit quality and to identify loans and leases that may become nonperforming, at any time there are loans and leases included in the portfolio that will result in losses, but that have not been identified as nonperforming or potential problem credits. We cannot be sure that we will be able to identify deteriorating credits before they become nonperforming assets, or that we will be able to limit losses on those loans and leases that are identified. As a result, future additions to the allowance may be necessary. Additionally, future additions may be required based on changes in the loans and leases comprising the portfolio and changes in the financial condition of borrowers, such as may result from changes in economic conditions, or as a result of incorrect assumptions by management in determining the allowance. Additionally, federal banking regulators, as an integral part of their supervisory function, periodically review our allowance for loan and lease losses. These regulatory agencies may require us to increase our provision for loan and lease losses or to recognize further loan or lease charge-offs based upon their judgments, which may be different from ours. Any increase in the allowance for loan and lease losses could have a negative effect on our financial condition and results of operations.

***We rely on our management and other key personnel, and the loss of any of them may adversely affect our operations.***

We are and will continue to be dependent upon the services of our executive management team. In addition, we will continue to depend on our ability to retain and recruit key client relationship managers. The unexpected loss of services of any key management personnel, or the inability to recruit and retain qualified personnel in the future, could have an adverse effect on our business and financial condition.

***The market price for our common stock may be volatile.***

The market price for our common stock has fluctuated, ranging between \$25.60 and \$38.97 per share during the 12 months ended December 31, 2007. The overall market and the price of our common stock may continue to be volatile. There may be a significant impact on the market price for our common stock due to, among other things:

- Variations in our anticipated or actual operating results or the results of our competitors;
- Changes in investors' or analysts' perceptions of the risks and conditions of our business;
- The size of the public float of our common stock;
- Regulatory developments;
- The announcement of acquisitions or new branch locations by us or our competitors;
- Market conditions; and
- General economic conditions.

Additionally, the average daily trading volume for our common stock as reported on the Nasdaq Market was 46,447 shares during the twelve months ended December 31, 2007, with daily volume ranging from a low of 8,900 shares to a high of 172,100 shares. There can be no assurance that a more active or consistent trading market in our common

stock will develop. As a result, relatively small trades could have a significant impact on the price of our common stock.

*We may fail to realize the cost savings we estimate for mergers and acquisitions.*

The success of our mergers and acquisitions may depend, in part, on our ability to realize the estimated cost savings from combining the businesses. It is possible that the potential cost savings could turn out to be more difficult to achieve than we anticipated. Our cost savings estimates also depend on our ability to combine the businesses in a manner that permits those cost savings to be realized. If our estimates turn out to be incorrect or we are not able to combine successfully, the anticipated cost savings may not be realized fully or at all, or may take longer to realize than expected.

***Combining acquired businesses with Sandy Spring may be more difficult, costly, or time-consuming than we expect, or could result in the loss of customers.***

It is possible that the process of merger integration of acquired companies could result in the loss of key employees, the disruption of ongoing business or inconsistencies in standards, controls, procedures and policies that adversely affect the ability to maintain relationships with clients and employees or to achieve the anticipated benefits of the merger or acquisition. There also may be disruptions that cause us to lose customers or cause customers to withdraw their deposits. Customers may not readily accept changes to their banking arrangements or other customer relationships after the merger or acquisition.

***Competition may decrease our growth or profits.***

We compete for loans, deposits, and investment dollars with other banks and other financial institutions and enterprises, such as securities firms, insurance companies, savings associations, credit unions, mortgage brokers, and private lenders, many of which have substantially greater resources than ours. Credit unions have federal tax exemptions, which may allow them to offer lower rates on loans and higher rates on deposits than taxpaying financial institutions such as commercial banks. In addition, non-depository institution competitors are generally not subject to the extensive regulation applicable to institutions that offer federally insured deposits. Other institutions may have other competitive advantages in particular markets or may be willing to accept lower profit margins on certain products. These differences in resources, regulation, competitive advantages, and business strategy may decrease our net interest margin, increase our operating costs, and may make it harder for us to compete profitably.

***Government regulation significantly affects our business.***

The banking industry is heavily regulated. Banking regulations are primarily intended to protect the federal deposit insurance funds and depositors, not shareholders. Sandy Spring Bank is subject to regulation and supervision by the Board of Governors of the Federal Reserve System and by Maryland banking authorities. Sandy Spring Bancorp is subject to regulation and supervision by the Board of Governors of the Federal Reserve System. The burdens imposed by federal and state regulations put banks at a competitive disadvantage compared to less regulated competitors such as finance companies, mortgage banking companies, and leasing companies. Changes in the laws, regulations, and regulatory practices affecting the banking industry may increase our costs of doing business or otherwise adversely affect us and create competitive advantages for others. Regulations affecting banks and financial services companies undergo continuous change, and we cannot predict the ultimate effect of these changes, which could have a material adverse effect on our profitability or financial condition. Federal economic and monetary policy may also affect our ability to attract deposits and other funding sources, make loans and investments, and achieve satisfactory interest spreads.

***Our ability to pay dividends is limited by law and contract.***

Our ability to pay dividends to our shareholders largely depends on Sandy Spring Bancorp's receipt of dividends from Sandy Spring Bank. The amount of dividends that Sandy Spring Bank may pay to Sandy Spring Bancorp is limited by federal laws and regulations. We also may decide to limit the payment of dividends even when we have the legal ability to pay them in order to retain earnings for use in our business. We also are prohibited from paying dividends on our common stock if the required payments on our subordinated debentures have not been made.

***Restrictions on unfriendly acquisitions could prevent a takeover.***

Our articles of incorporation and bylaws contain provisions that could discourage takeover attempts that are not approved by the board of directors. The Maryland General Corporation Law includes provisions that make an acquisition of Sandy Spring Bancorp more difficult. These provisions may prevent a future takeover attempt in which

our shareholders otherwise might receive a substantial premium for their shares over then-current market prices.

These provisions include supermajority provisions for the approval of certain business combinations and certain provisions relating to meetings of shareholders. Our certificate of incorporation also authorizes the issuance of additional shares without shareholder approval on terms or in circumstances that could deter a future takeover attempt.

***Future sales of our common stock or other securities may dilute the value of our common stock.***

In many situations, our board of directors has the authority, without any vote of our shareholders, to issue shares of our authorized but unissued stock, including shares authorized and unissued under our omnibus stock plan. In the future, we may issue additional securities, through public or private offerings, in order to raise additional capital. Any such issuance would dilute the percentage of ownership interest of existing shareholders and may dilute the per share book value of the common stock. In addition, option holders may exercise their options at a time when we would otherwise be able to obtain additional equity capital on more favorable terms.

***We may not attain the revenue increases or expense reduction goals targeted by Project LIFT.***

The Company's results in the coming year may depend, in part, on our ability to realize the estimated revenue increases and expense reductions from *Project LIFT*. It is possible that the potential revenue increases or expense savings could turn out to be more difficult to achieve than we anticipated. Our estimates also depend on our ability to execute on a number of expense reduction initiatives. If our estimates turn out to be incorrect the anticipated revenue increases or cost savings may not be realized fully or at all, or may take longer to realize than expected.

## **COMPETITION**

The Bank's principal competitors for deposits are other financial institutions, including other banks, credit unions, and savings institutions. Competition among these institutions is based primarily on interest rates and other terms offered, service charges imposed on deposit accounts, the quality of services rendered, and the convenience of banking facilities. Additional competition for depositors' funds comes from U.S. Government securities, private issuers of debt obligations and suppliers of other investment alternatives for depositors, such as securities firms. Competition from credit unions has intensified in recent years as historical federal limits on membership have been relaxed. Because federal law subsidizes credit unions by giving them a general exemption from federal income taxes, credit unions have a significant cost advantage over banks and savings associations, which are fully subject to federal income taxes. Credit unions may use this advantage to offer rates that are highly competitive with those offered by banks and thrifts.

The banking business in Maryland generally, and the Bank's primary service areas specifically, are highly competitive with respect to both loans and deposits. As noted above, the Bank competes with many larger banking organizations that have offices over a wide geographic area. These larger institutions have certain inherent advantages, such as the ability to finance wide-ranging advertising campaigns and promotions and to allocate their investment assets to regions offering the highest yield and demand. They also offer services, such as international banking, that are not offered directly by the Bank (but are available indirectly through correspondent institutions), and, by virtue of their larger total capitalization, such banks have substantially higher legal lending limits, which are based on bank capital, than does the Bank. The Bank can arrange loans in excess of its lending limit, or in excess of the level of risk it desires to take, by arranging participations with other banks. Other entities, both governmental and in private industry, raise capital through the issuance and sale of debt and equity securities and indirectly compete with the Bank in the acquisition of deposits.

In addition to competing with other commercial banks, credit unions and savings associations, commercial banks such as the Bank compete with non-bank institutions for funds. For instance, yields on corporate and government debt and equity securities affect the ability of commercial banks to attract and hold deposits. Mutual funds also provide substantial competition to banks for deposits.

The Holding Company Act permits the Federal Reserve to approve an application of an adequately capitalized and adequately managed bank holding company to acquire control of, or acquire all or substantially all of the assets of, a bank located in a state other than that holding company's home state. The Federal Reserve may not approve the acquisition of a bank that has not been in existence for the minimum time period (not exceeding five years) specified by the statutory law of the host state. The Holding Company Act also prohibits the Federal Reserve from approving an application if the applicant (and its depository institution affiliates) controls or would control more than 10% of the insured deposits in the United States or 30% or more of the deposits in the target bank's home state or in any state in which the target bank maintains a branch. The Holding Company Act does not affect the authority of states to limit the percentage of total insured deposits in the state which may be held or controlled by a bank or bank holding company to the extent such limitation does not discriminate against out-of-state banks or bank holding companies. The State of Maryland allows out-of-state financial institutions to merge with Maryland banks and to establish branches in Maryland, subject to certain limitations.

Financial holding companies may engage in banking as well as types of securities, insurance, and other financial activities that historically had been prohibited for bank holding companies under prior law. Banks with or without holding companies also may establish and operate financial subsidiaries that may engage in most financial activities in which financial holding companies may engage. Competition may increase as bank holding companies and other large financial services companies take advantage of the ability to engage in new activities and provide a wider array of products.

## EMPLOYEES

The Company and the Bank employed 749 persons, including executive officers, loan and other banking and trust officers, branch personnel, and others at December 31, 2007. None of the Company's or the Bank's employees is represented by a union or covered under a collective bargaining agreement. Management of the Company and the Bank consider their employee relations to be excellent.

## EXECUTIVE OFFICERS

The following listing sets forth the name, age (as of February 27, 2008), principal position and business experience of each executive officer that is not a director for at least the last five years are set forth below:

R. Louis Caceres, 45, Executive Vice President of the Bank. Mr. Caceres was made Executive Vice President of the Bank in 2002. Prior to that, Mr. Caceres was a Senior Vice President of the Bank.

Ronald E. Kuykendall, 55, became Executive Vice President, General Counsel and Secretary of the Company and the Bank in 2002. Prior to that, Mr. Kuykendall was General Counsel and Secretary of Bancorp and Senior Vice President of the Bank.

Philip J. Mantua, CPA, 49, became Executive Vice President and Chief Financial Officer of the Company and the Bank in 2004. Prior to that, Mr. Mantua was Senior Vice President of Managerial Accounting.

Joseph J. O'Brien, Jr., 44, joined the Bank in July 2007 as Executive Vice President. On January 1, 2008 he became president of the Potomac Bank Division. Prior to joining the Bank Mr. O'Brien was Executive Vice President and senior lender for a local banking institution.

Daniel J. Schrider, 43, became Executive Vice President and Chief Credit Officer effective January 1, 2003. Prior to that, Mr. Schrider served as a Senior Vice President of the Bank.

Frank H. Small, 61, became an Executive Vice President of the Company and the Bank in 2001 and Chief Operating Officer of the Bank in 2002. Prior to that, Mr. Small was an Executive Vice President of the Bank.

Sara E. Watkins, 51, became an Executive Vice President of the Bank in 2002. Prior to that, Ms. Watkins was a Senior Vice President of the Bank.

## PROPERTIES

The locations of Sandy Spring Bancorp, Inc. and its subsidiaries are shown below.

### COMMUNITY BANKING OFFICES

40 West – Rockledge Plaza* 1100 West Patrick St, Unit A Frederick, MD 21702	Bedford Court 3701 International Drive Silver Spring, MD 20906	Colesville* 13300 New Hampshire Avenue Silver Spring, MD 20904
Airpark* 7653 Lindbergh Drive Gaithersburg, MD 20879	Bethesda* 7126 Wisconsin Avenue Bethesda, MD 20814	Damascus* 26250 Ridge Road Damascus, MD 20872
Ashton*	Burtonsville*	East Gude Drive*



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1 Ashton Road  
Ashton, MD 20861

3535 Spencerville Road  
Burtonsville, MD 20866

1601 East Gude Drive  
Rockville, MD 20850

Asbury\*  
409 Russell Avenue  
Gaithersburg MD 20877

Clarksville\*  
12276 Clarksville Pike  
Clarksville, MD 21029

Eastport\*  
1013 Bay Ridge Avenue  
Annapolis, MD 21403

Ballenger Creek\*  
6560 Mercantile Drive  
Frederick, MD 21703

Chantilly\*  
14231 Willard Road, Suite  
100  
Chantilly, VA 20151

Edgewater\*  
116 Mitchells Chance Road  
Edgewater, MD 21037

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Fairfax* 9910 Main Street Fairfax, VA 22031	Lisbon* 704 Lisbon Centre Drive Woodbine, MD 21797	Potomac* 9822 Falls Road Potomac, MD 20854
Fulton-Cherry Tree Crossing* 8315 Ice Crystal Drive Laurel, MD 20723	Merrifield* 8501 Arlington Blvd Fairfax, VA 22031	Rockville* 611 Rockville Pike Rockville, MD 20852
Gaithersburg Square* 484 North Frederick Avenue Gaithersburg, MD 20877	Milestone Center* 20930 Frederick Avenue Germantown, MD 20876	Sandy Spring 908 Olney-Sandy Spring Road Sandy Spring, MD 20860
Glen Burnie* 7405 Ritchie Highway Glen Burnie, MD 21061	Millersville* 8310 Veterans Highway Millersville, MD 21108	Silver Spring* 8677 Georgia Avenue Silver Spring, MD 20910
Jennifer Road* 166 Jennifer Road Annapolis, MD 21401	Montgomery Village* 9921 Stedwick Road Montgomery Village, MD 20886	Urbana* 8921 Fingerboard Road Frederick, MD 21704
Laurel Lakes* 14404 Baltimore Avenue Laurel, MD 20707	Mt. Airy Shopping Center* 425 East Ridgeville Blvd. Mt. Airy, MD 21771	Vienna* 414 Maple Ave N.E. Vienna, VA 22180
Lansdowne* 19460 golf Vista Plaza Lansdowne, VA 20175	Odenton* 8759 Piney Orchard Parkway Odenton, MD 21090	Wildwood* 10329 Old Georgetown Road Bethesda, MD 20814
Layhill* 14241 Layhill Road Silver Spring, MD 20906	Olney* 17801 Georgia Avenue Olney, MD 20832	* ATM Available
Leisure World Plaza* 3801 International Drive, Suite 100 Silver Spring, MD 20906	Pasadena* 4001 Mountain Road  Pasadena, MD 21122	
Linthicum* 504 S. Camp Meade Road Linthicum, MD 21090	Patrick Street* 14 West Patrick Street Frederick, MD 21701	

OTHER PROPERTIES

Administrative Offices 17735 Georgia Avenue Olney, MD 20832	The Equipment Leasing Company 53 Loveton Circle, Suite	Sandy Spring Mortgage and Columbia Center
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100 9112  
Sparks, MD Guilford  
21152 Road  
Columbia,  
MD 21046

Sandy Spring Financial Center 148 Jennifer Road Annapolis, MD 21401	Sandy Spring Insurance Corp. T/A Chesapeake Insurance Group 151 West Street, Suite 300 Annapolis, MD 21401	West Financial Services, Inc. 1355 Beverly Road, Suite 250 McLean, Virginia 22101
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Neff &  
Associates  
9921 Stephen  
Decatur  
Highway  
Suite C5  
Ocean City, MD  
21842

**EXHIBITS, FINANCIAL STATEMENT SCHEDULES**

The following financial statements are filed as a part of this report:

- Consolidated Balance Sheets at December 31, 2007 and 2006
- Consolidated Statements of Income for the years ended December 31, 2007, 2006, and 2005
- Consolidated Statements of Cash Flows for the years ended December 31, 2007, 2006, and 2005
- Consolidated Statements of Changes in Stockholders' Equity for the years ended December 31, 2007, 2006, and 2005
- Notes to the Consolidated Financial Statements
- Reports of Registered Public Accounting Firm

All financial statement schedules have been omitted, as the required information is either not applicable or included in the Consolidated Financial Statements or related Notes.

The following exhibits are filed as a part of this report:

Exhibit No.	Description	Incorporated by Reference to:
3(a)	Articles of Incorporation of Sandy Spring Bancorp, Inc., as Amended	Exhibit 3.1 to Form 10-Q for the quarter ended June 30, 1996, SEC File No. 0-19065.
3(b)	Bylaws of Sandy Spring Bancorp, Inc.	Exhibit 3.2 to Form 8-K dated May 13, 1992, SEC File No. 0-19065.
4	No long-term debt instrument issued by the Company exceeds 10% of consolidated assets or is registered. In accordance with paragraph 4(iii) of Item 601(b) of Regulation S-K, the Company will furnish the SEC copies of all long-term debt instruments and related agreements upon request.	
10(a)*	Amended and Restated Sandy Spring Bancorp, Inc., Cash and Deferred Profit Sharing Plan and Trust	Exhibit 10(a) to Form 10-Q for the quarter ended September 30, 1997, SEC File No. 0-19065.
10(b)*	Sandy Spring Bancorp, Inc. 2005 Omnibus Stock Plan	Exhibit 10.1 to Form 8-K dated June 27, 2005, Commission File No. 0-19065.
10(c)*	Sandy Spring Bancorp, Inc. 1992 Stock Option Plan	Exhibit 10(i) to Form 10-K for the year ended December 31, 1991, SEC File No. 0-19065.
10(d)*	Sandy Spring Bancorp, Inc. Amended and Restated Stock Option Plan for Employees of Annapolis	Exhibit 4 to Registration Statement on Form S-8, Registration Statement No.

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	Bancshares, Inc.	333-11049.
10(e)*	Sandy Spring Bancorp, Inc. 1999 Stock Option Plan	Exhibit 4 to Registration Statement on Form S-8, Registration Statement No. 333-81249.
10(f)*	Sandy Spring National Bank of Maryland Executive Health Insurance Plan	Exhibit 10 to Form 10-Q for the quarter ended March 31, 2002, SEC File No. 0-19065.
10(g)*	Sandy Spring National Bank of Maryland Executive Health Expense Reimbursement Plan, as amended	Exhibit 10(g) to Form 10-K for the year ended December 31, 2001, SEC File No. 0-19065.
10(h)*	Form of Director Fee Deferral Agreement, August 26, 1997, as amended	Exhibit 10(h) to Form 10-K for the year ended December 31, 2003, SEC File No. 0-19065.
10(i)*	Employment Agreement by and among Sandy Spring Bancorp, Inc., Sandy Spring National Bank of Maryland, and Hunter R. Hollar	Exhibit 10A to Form 10-Q for the quarter ended March 31, 2003, SEC File No. 0-19065.
10(j)*	Employment Agreement by and among Sandy Spring Bancorp, Inc., Sandy Spring Bank, and Philip J. Mantua	Exhibit 10(l) to Form 10-K for the year ended December 31, 2004, SEC File No. 0-19065.
10(k)*	Employment Agreement by and among Sandy Spring Bancorp, Inc., Sandy Spring Bank, and Daniel J. Schrider	Exhibit 10(b) to Form 10-Q for the quarter ended September 30, 2004, SEC File No. 0-19065.
10(l)*	Employment Agreement by and among Sandy Spring Bancorp, Inc., Sandy Spring Bank, and Frank H. Small	Exhibit 10(o) to Form 10-K for the year ended December 31, 2002, SEC File No. 0-19065.

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10(m)*	Employment Agreement by and among Sandy Spring Bancorp, Inc., Sandy Spring Bank, and Sara E. Watkins	Exhibit 10(p) to Form 10-K for the year ended December 31, 2002, SEC File No. 0-19065.
10(n)*	Employment Agreement by and among Sandy Spring Bancorp, Inc., Sandy Spring Bank, and Ronald E. Kuykendall	Exhibit 10(q) to Form 10-K for the year ended December 31, 2002, SEC File No. 0-19065.
10(p)*	Employment Agreement by and among Sandy Spring Bancorp, Inc., Sandy Spring Bank, and R. Louis Caceres	Exhibit 10(a) to Form 10-Q for the quarter ended September 30, 2004, SEC File No. 0-19065.
10(q)*	Form of Sandy Spring National Bank of Maryland Officer Group Term Replacement Plan	Exhibit 10(r) to Form 10-K for the year ended December 31, 2001, SEC File No. 0-19065.
10(r)	Sandy Spring Bancorp, Inc. Directors' Stock Purchase Plan	Exhibit 4 to Registration Statement on Form S-8, File No. 333-117330.
10(s)*	Amended and Restated Potomac Bank of Virginia 199 Stock Option Plan	Exhibit 4.1 to Registration Statement on Form S-8, File No. 333-141052
10(t)*	Amended and Restated Potomac Bank of Virginia Employee Stock Purchase Plan	Exhibit 4.2 to Registration Statement on Form S-8, File No. 333-141052
10(u)*	Amended and Restated CN Bancorp, Inc. Stock Option Plan	Exhibit 4.1 to Registration Statement on Form S-8, File No. 333-144949
10(v)*	Sandy Spring Bank Executive Incentive Retirement Plan	
21	Subsidiaries	
23	Consent of Registered Public Accounting Firm	
31 (a),(b)	Rule 13a-14(a)/15d-14(a) Certifications	
32 (a),(b)	18 U.S.C. Section 1350 Certifications	

\* Management Contract or Compensatory Plan or Arrangement filed pursuant to Item 15(c) of this Report.

**Shareholders may obtain, upon payment of a reasonable fee, a copy of the exhibits to this Report on Form 10-K by writing Ronald E. Kuykendall, General Counsel and Secretary, at Sandy Spring Bancorp, Inc., 17801 Georgia Avenue, Olney, Maryland 20832. Shareholders also may access a copy of the Form 10-K including exhibits on the SEC Web site at [www.sec.gov](http://www.sec.gov) or through the Company's Investor Relations Web site maintained at [www.sandyspringbank.com](http://www.sandyspringbank.com).**

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**Signatures**

Pursuant to the requirements of Section 13 of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SANDY SPRING BANCORP, INC.  
(Registrant)

By: /s/ Hunter  
R. Hollar  
Hunter R. Hollar  
President and  
Chief Executive  
Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated as of February 28, 2007.

Principal Executive Officer and Director:  
/s/ Hunter R. Hollar  
Hunter R. Hollar  
President and Chief Executive Officer

Principal Financial and Accounting Officer:  
/s/ Philip J. Mantua  
Philip J. Mantua  
Executive Vice President and Chief Financial  
Officer

Signature	Title
/s/ John Chirtea John Chirtea	Director
/s/ Mark E. Friis Mark E. Friis	Director
/s/ Susan D. Goff Susan D. Goff	Director
/s/ Solomon Graham Solomon Graham	Director
/s/ Marshall H. Groom Marshall Groom	Director
/s/ Gilbert L. Hardesty Gilbert L. Hardesty	Director
/s/ Pamela A. Little Pamela A. Little	Director
/s/ Charles F. Mess Charles F. Mess	Director



/s/ Robert L. Orndorff  
Robert L. Orndorff

Director

/s/ David E. Rippeon  
David E. Rippeon

Director

/s/ Craig A. Ruppert  
Craig A. Ruppert

Director

/s/ Lewis R. Schumann  
Lewis R. Schumann

Director

/s/ W. Drew Stabler  
W. Drew Stabler

Chairman of the Board,  
Director