CASS INFORMATION SYSTEMS INC
Form 10-K
March 12, 2009

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

FORM 10-K

(Mark One)

|X| ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2008

|_| TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from __________ to __________

Commission file number 2-80070

CASS INFORMATION SYSTEMS, INC.
(Exact name of registrant as specified in its charter)

Missouri	43-1265338
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
13001 Hollenberg Drive, Bridgeton, Missouri	63044
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (314) 506-5500

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

Title of each Class	Name of each exchange on which registered
Common Stock par value $.50	The Nasdaq Global Select Market

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

Common Stock par value $.50
(Title of Class)

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

Indicate by checkmark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes |_| No |X|

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

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

Form 10-K. |_|

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:	|X|
Non-accelerated filer:	|_|	Smaller reporting company:	|_|

Indicate by checkmark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes |_| No |X|

The aggregate market value of the common stock held by non-affiliates of the Registrant was approximately $240,337,000 based on the closing price of the common stock of $32.03 on June 30, 2008, as reported by The Nasdaq Global Select Market.

As of March 6, 2009, the Registrant had 9,213,242 shares outstanding of common stock.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information required for Part III of this report is incorporated by reference to the Registrant's Proxy Statement for the 2009 Annual Meeting of Shareholders.

CASS INFORMATION SYSTEMS, INC.
FORM 10-K ANNUAL REPORT
TABLE OF CONTENTS

PART I.

Item 1.	BUSINESS	1
Item 1A.	RISK FACTORS	3
Item 1B.	UNRESOLVED STAFF COMMENTS	7
Item 2.	PROPERTIES	7
Item 3.	LEGAL PROCEEDINGS	7
Item 4.	SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS	7

PART II.

Item 5.	MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES	8
Item 6.	SELECTED FINANCIAL DATA	10
Item 7.	MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	10
Item 7A.	QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	26

Item 8.	FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA	28
Item 9.	CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE	54
Item 9A.	CONTROLS AND PROCEDURES	54
Item 9B.	OTHER INFORMATION	56
PART III.		
Item 10.	DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE	56
Item 11.	EXECUTIVE COMPENSATION	56
Item 12.	SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS	56
Item 13.	CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE	57
Item 14.	PRINCIPAL ACCOUNTANT FEES AND SERVICES	57
PART IV.		
Item 15.	EXHIBITS AND FINANCIAL STATEMENT SCHEDULES	57
	SIGNATURES	59

Forward-looking Statements - Factors That May Affect Future Results

This report may contain or incorporate by reference forward-looking statements made pursuant to the safe harbor provisions of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Although we believe that, in making any such statements, our expectations are based on reasonable assumptions, forward-looking statements are not guarantees of future performance and involve risks, uncertainties and other factors which may cause future performance to be materially different from expected performance summarized in the forward-looking statements. These risks, uncertainties and other factors are discussed in Part I, Item 1A, "Risk Factors." We undertake no obligation to publicly update or revise any forward-looking statements to reflect changed assumptions, the occurrence of anticipated or unanticipated events, or changes to future results over time.

PART I.

ITEM 1. BUSINESS

Description of Business

Cass Information Systems, Inc. ("Cass" or "the Company") is a leading provider of payment and information processing services to large manufacturing, distribution and retail enterprises across the United States. The Company provides freight invoice rating, payment, audit, accounting and transportation information to many of the nation's largest companies. It is also a processor and payer of utility invoices, including electricity, gas, and other facility related expenses. Additionally, Cass competes in the telecommunications expense management market which includes bill processing, audit and payment services for telephone, data line, cellular and communication equipment expense. Also the Company, through its wholly owned bank subsidiary, Cass Commercial Bank ("the

Bank"), provides commercial banking services. The Bank's primary focus is to support the Company's payment operations and provide banking services to its target markets, which include privately owned businesses and churches and church-related ministries. Services include commercial and commercial real estate, checking, savings and time deposit accounts and other cash management services. The principal offices of the Company are at 13001 Hollenberg Drive, Bridgeton, Missouri 63044. Other operating locations are in Columbus, Ohio, Boston, Massachusetts, Greenville, South Carolina and Wellington, Kansas. The Bank's headquarters are also located at the Bridgeton location, and the Bank operates five other branches, four in the St. Louis metropolitan area and one in southern California.

Company Strategy and Core Competencies

Cass is an information services company with a primary focus on processing payables and payables-related transactions for large corporations located in the United States. Cass possesses four core competencies that encompass most of its processing services.

Data acquisition - This refers to the gathering of data elements from diverse, heterogeneous sources and the building of complete databases for our customers. Data is the raw material of the information economy. Cass gathers vital data from complex and diverse input documents, electronic media, proprietary databases and data feeds, including data acquired from vendor invoices as well as customer procurement and sales systems. Through its numerous methods of obtaining streams and pieces of raw data, Cass is able to assemble vital data into centralized data management systems and warehouses, thus producing an engine to create the power of information for managing critical corporate functions and processing systems.

Data management - Once data is assembled, Cass is able to utilize the power from derived information to produce significant savings and benefits for its clients. This information is integrated into customers' unique financial and accounting systems, eliminating the need for internal accounting processing and providing internal and external support for these critical systems. Information is also used to produce management and exception reporting for operational control, feedback, planning assistance and performance measurement.

Information delivery - Receiving information in the right place at the right time and in the required format is paramount for business survival. Cass' information delivery solutions provide reports, digital images, data files and retrieval capabilities through the Internet or directly into customer internal systems. Cass' proprietary Internet management delivery system is the foundation for driving these critical functions. Transaction, operational, control, status and processing exception information are all delivered through this system creating an efficient, accessible and highly reliable asset for Cass customers.

Financial exchange - Since Cass is unique among its competition in that it owns a commercial bank, it is also able to manage the movement of funds from its customers to their suppliers. This is a distinguishing factor, which clearly requires the processing capability, operating systems and financial integrity of a banking organization. Cass provides immediate, accurate, controlled and protected funds management and transfer system capabilities for all of its customers. Old and costly check processing and delivery mechanisms are replaced with more efficient electronic cash management and funds transfer systems.

Cass' core competencies allow it to perform the highest levels of transaction processing in an integrated, efficient and systematic approach. Not only is Cass able to process the transaction, it is also able to collect the data defining the transaction and effect the financial payment governing its terms.

Cass' shared business processes - Accounting, Human Resources and Technology -

support its core competencies. Cass' accounting function provides the internal control systems to ensure the highest levels of accountability and protection for customers. Cass' human resources department provides experienced people dedicated to streamlining business procedures and reducing expenses. Cass' technology is proven and reliable. The need to safeguard data and secure the efficiency, speed and timeliness that govern its business is a priority within the organization. The ability to leverage technology over its strategic units allows Cass the advantage of deploying technology in a proven and reliable

manner without hindering clients' strategic business and system requirements.

These core competencies, enhanced through shared business processes, drive Cass' strategic business units. Building upon these foundations, Cass continues to explore new business opportunities that leverage these competencies and processes.

Marketing, Customers and Competition

The Company, through its Transportation Information Services business unit, is one of the largest firms in the freight bill processing and payment industry in the United States based on the total dollars of freight bills paid and items processed. Competition consists of a few primary competitors and numerous small freight bill audit firms located throughout the United States. While offering freight payment services, few of these audit firms compete on a national basis. These competitors compete mainly on price, functionality and service levels. The Company, through its Utility Information Services business unit, also competes with other companies, located throughout the United States, that pay utility bills and provide management reporting. Available data indicates that the Company is one of the largest providers of utility information processing and payment services. Cass' Utility Information Services is unique among these competitors in that it is not exclusively affiliated with any one energy service provider ("ESP"). The ESPs market the Company's services adding value with their unique auditing, consulting and technological capabilities. Many of Cass' services are customized for the ESPs, providing a full-featured solution without any development costs to the ESP. Also the Company, through its Telecom Information Services business unit, is a leader in the growing telecom expense management market, and competes with other companies located throughout the United States in this market.

The Bank is organized as a Missouri trust company with banking powers and was founded in 1906. Due to its ownership of a federally insured commercial bank, the Company is a bank holding corporation and was originally organized in 1982 as Cass Commercial Corporation under the laws of Missouri. It was approved by the Board of Governors of the Federal Reserve System (the "Federal Reserve") in February 1983. The Company changed its name to Cass Information Systems, Inc. in January 2001. The Company's bank subsidiary encounters competition from numerous banks and financial institutions located throughout the St. Louis, Missouri metropolitan area and other areas in which the Bank competes. The Bank's principal competitors, however, are large bank holding companies that are able to offer a wide range of banking and related services through extensive branch networks. The Bank targets its services to privately held businesses located in the St. Louis, Missouri area and church and church-related institutions located in St. Louis, Missouri, Orange County, California and other selected cities located throughout the United States. The Bank has not financed, and does not currently finance, sub-prime mortgage loans.

The Company holds several trademarks for the payment and rating services it provides. These include: FreightPay(R), Transdata(R), TransInq(R), Ratemaker(R), Rate Advice(R), First Rate(R), Best Rate(R), Rate Exchange(R) and CassPort(R).

The Company and its subsidiaries are not dependent on any one customer for a significant portion of their businesses. The Company and its subsidiaries have a varied client base with no individual client exceeding 10% of total revenue.

Employees

The Company and its subsidiaries had 709 full-time and 227 part-time employees as of March 2, 2009. Of these employees, the Bank had 62 full-time and two part-time employees.

Supervision and Regulation

The Company and its bank subsidiary are extensively regulated under federal and state law. These laws and regulations are intended to protect depositors, not shareholders. The Bank is subject to regulation and supervision by the Missouri Division of Finance, the Federal Reserve Bank (the "FRB") and the Federal Deposit Insurance Corporation (the "FDIC"). The Company is a bank holding company within the meaning of the Bank Holding Company Act of 1956, as amended, and as such, it is subject to regulation, supervision and examination by the FRB. The Company is required to file quarterly and annual reports with the FRB and to provide to the FRB such additional information as the FRB may require, and it is subject to regular inspections by the FRB. Bank regulatory agencies use Capital Adequacy Guidelines in their examination and regulation of bank holding companies and banks. If the capital falls below the minimum levels established by these guidelines, the agencies may force certain remedial action to be taken. The Capital Adequacy Guidelines are of several types and include risk-based capital guidelines, which are designed to make capital requirements more sensitive to various risk profiles and account for off-balance sheet exposure; guidelines that consider market risk, which is the risk of loss due to change in value of assets and liabilities due to changes in interest rates; and guidelines that use a leverage ratio which places a constraint on the maximum degree of risk to which a bank holding company may leverage its equity capital base. For further discussion of the capital adequacy guidelines and ratios, please refer to Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Item 8, Note 3 of this report.

The FRB also has extensive enforcement authority over bank holding companies, including, among other things, the ability to assess civil money penalties, to issue cease and desist or removal orders and to require that a holding company divest subsidiaries (including its bank subsidiaries). In general, enforcement actions may be initiated for violations of law or regulations or for unsafe or unsound practices. Both the FRB and Missouri Division of Finance also have restrictions on the amount of dividends that banks and bank holding companies may pay.

As a bank holding company, the Company must obtain prior approval from the FRB before acquiring ownership or control of more than 10% of the voting shares of another bank or bank holding company or acquiring all or substantially all of the assets of such a company. In many cases, prior approval is also required for the Company to engage in similar acquisitions involving a non-bank company or to engage in new non-bank activities. Any change in applicable laws or regulations may have a material effect on the business and prospects of the Company.

Website Availability of SEC Reports

Cass files annual, quarterly and current reports with the Securities and Exchange Commission (the "SEC"). Cass will, as soon as reasonably practicable after they are electronically filed with or furnished to the SEC, make available free of charge on its website each of its Annual Reports on Form 10-K, Quarterly

Reports on Form 10-Q, Current Reports of Form 8-K, all amendments to those reports, and its definitive proxy statements. The address of Cass' website is: www.cassinfo.com. All reports filed with the SEC are available for reading and copying at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549-0213 or for more information call the Public Reference Room at 1-800-SEC-0330. The SEC also makes all filed reports, proxy statements and information statements available on its website at www.sec.gov.

The reference to our website address does not constitute incorporation by reference of the information contained on the website and should not be considered part of this report.

Financial Information about Segments

The services provided by the Company are classified in two reportable segments: Information Services and Banking Services. The revenues from external customers, net income and total assets by segment as of and for the three years ended December 31, 2008, are set forth in Item 8, Note 18 of this report.

Statistical Disclosure by Bank Holding Companies

For the statistical disclosure by bank holding companies refer to Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations."

ITEM 1A. RISK FACTORS

This section highlights specific risks that could affect the Company's business. Although this section attempts to highlight key factors, please be aware that other risks may prove to be important in the future. New risks may emerge at any time, and Cass cannot predict such risks or estimate the extent to which they may affect the Company's financial performance. In addition to the factors discussed elsewhere or incorporated by reference in this report, the identified risks that could cause actual results to differ materially include the following:

General political, economic or industry conditions may be less favorable than expected.

Local, domestic, and international economic, political and industry-specific conditions and governmental monetary and fiscal policies affect the industries in which the Company competes, directly and indirectly. Conditions such as inflation, recession, unemployment, volatile interest rates, tight money supply, real estate values, international conflicts and other factors outside of Cass' control may adversely affect the Company. Economic downturns could result in the delinquency of outstanding loans, which could have a material adverse impact on Cass' earnings. If the weak global economic conditions persist well into the future, the Company's financial condition could be negatively impacted.

Unfavorable developments concerning customer credit quality could affect Cass' financial results.

Although the Company regularly reviews credit exposure related to its customers and various industry sectors in which it has business relationships, default risk may arise from events or circumstances that are difficult to detect or foresee. Under such circumstances, the Company could experience an increase in the level of provision for credit losses, delinquencies, nonperforming assets, net charge-offs and allowance for credit losses.

The Company has lending concentrations, including, but not limited to, churches and church-related entities located in selected cities and privately-held businesses located in or near St. Louis, Missouri, that could suffer a significant decline which could adversely affect the Company.

Cass' customer base consists, in part, of lending concentrations in several segments and geographical areas. If any of these segments or areas is significantly affected by the general weak economic conditions that currently exist, the Company could experience increased credit losses, and its business could be adversely affected.

Fluctuations in interest rates could affect Cass' net interest income and balance sheet.

The operations of financial institutions such as the Company are dependent to a large degree on net interest income, which is the difference between interest income from loans and investments and interest expense on deposits and borrowings. Prevailing economic conditions, the fiscal and monetary policies of the federal government and the policies of various regulatory agencies all affect market rates of interest, which in turn significantly affect financial institutions' net interest income. Fluctuations in interest rates affect Cass' financial statements, as they do for all financial institutions. Volatility in interest rates can also result in disintermediation, which is the flow of funds away from financial institutions into direct investments, such as federal government and corporate securities and other investment vehicles, which, because of the absence of federal insurance premiums and reserve requirements, generally pay higher rates of return than financial institutions. As discussed in greater detail in Item 7A, "Quantitative and Qualitative Disclosures about Market Risk," a continuation of the decline in the general level of interest rates, as has been experienced during 2008, can have a negative impact on net interest income.

Methods of reducing risk exposures might not be effective.

Instruments, systems and strategies used to hedge or otherwise manage exposure to various types of credit, interest rate, market and liquidity, operational, regulatory/compliance, business risks and enterprise-wide risks could be less effective than anticipated. As a result, the Company may not be able to effectively mitigate its risk exposures in particular market environments or against particular types of risk.

Customer borrowing, repayment, investment, deposit, and payable processing practices may be different than anticipated.

The Company uses a variety of financial tools, models and other methods to anticipate customer behavior as part of its strategic and financial planning and to meet certain regulatory requirements. Individual, economic, political, industry-specific conditions and other factors outside of Cass' control could alter predicted customer borrowing, repayment, investment, deposit, and payable processing practices. Such a change in these practices could adversely affect Cass' ability to anticipate business needs, including cash flow and its impact on liquidity, and to meet regulatory requirements.

Operational difficulties or security problems could damage Cass' reputation and business.

The Company depends on the reliable operation of its computer operations and network connections from its clients to its systems. Any operational problems or outages in these systems would cause Cass to be unable to process transactions for its clients, resulting in decreased revenues. In addition, any system delays, failures or loss of data, whatever the cause, could reduce client satisfaction with the Company's products and services and harm Cass' financial

results. Cass also depends on the security of its systems. Company networks may be vulnerable to unauthorized access, computer viruses and other disruptive problems. A material security problem affecting Cass could damage its reputation, deter prospects from purchasing its products, deter customers from using its products or result in liability to Cass.

Cass' stock price can become volatile and fluctuate widely in response to a variety of factors.

The Company's stock price can fluctuate based on factors that can include actual or anticipated variations in Cass' quarterly results; new technology or services by competitors; unanticipated losses or gains due to unexpected events, including losses or gains on securities held for investment purposes; significant acquisitions or business combinations, strategic partnerships, joint ventures or capital commitments by or involving the Company or its competitors; changes in accounting policies or practices; failure to integrate acquisitions or realize anticipated benefits from acquisitions; or changes in government regulations.

General market fluctuations, industry factors and general economic and political conditions, such as economic slowdowns or recessions, governmental intervention, interest rate changes, credit loss trends, low trading volume or currency fluctuations also could cause Cass' stock price to decrease regardless of the Company's operating results.

Cass must respond to rapid technological changes and these changes may be more difficult or expensive than anticipated.

If competitors introduce new products and services embodying new technologies, or if new industry standards and practices emerge, the Company's existing product and service offerings, technology and systems may become obsolete. Further, if Cass fails to adopt or develop new technologies or to adapt its products and services to emerging industry standards, Cass may lose current and future customers, which could have a material adverse effect on its business, financial condition and results of operations. The payment processing and financial services industries are changing rapidly and in order to remain competitive, Cass must continue to enhance and improve the functionality and features of its products, services and technologies. These changes may be more difficult or expensive than the Company anticipates.

Competitive product and pricing pressure within Cass' markets may change.

The Company operates in a very competitive environment, which is characterized by competition from a number of other vendors and financial institutions in each market in which it operates. The Company competes with large payment processors and national and regional financial institutions and also smaller auditing companies and banks in terms of products and pricing. If the Company is unable to compete effectively in products and pricing in its markets, business could decline.

Management's ability to maintain and expand customer relationships may differ from expectations.

The industries in which the Company operates are very competitive. The Company not only competes for business opportunities with new customers, but also competes to maintain and expand the relationships it has with its existing customers. The Company continues to experience pressures to maintain these relationships as its competitors attempt to capture its customers.

The introductions, withdrawal, success and timing of business initiatives and strategies, including, but not limited to, the expansion of payment and processing activities to new markets, the expansion of products and services to existing markets and opening of new bank branches, may be less successful or may be different than anticipated. Such a result could adversely affect Cass' business.

The Company makes certain projections and develops plans and strategies for its payment processing and banking products. If the Company does not accurately determine demand for its products and services, it could result in the Company incurring significant expenses without the anticipated increases in revenue, which could result in an adverse effect on its earnings.

Management's ability to retain key officers and employees may change.

Cass' future operating results depend substantially upon the continued service of Cass' executive officers and key personnel. Cass' future operating results also depend in significant part upon Cass' ability to attract and retain qualified management, financial, technical, marketing, sales and support personnel. Competition for qualified personnel is intense, and the Company cannot ensure success in attracting or retaining qualified personnel. There may be only a limited number of persons with the requisite skills to serve in these positions, and it may be increasingly difficult for the Company to hire personnel over time. Cass' business, financial condition and results of operations could be materially adversely affected by the loss of any of its key employees, by the failure of any key employee to perform in his or her current position, or by Cass' inability to attract and retain skilled employees.

Changes in regulation or oversight may have a material adverse impact on Cass' operations.

The Company is subject to extensive regulation, supervision and examination by the Missouri Division of Finance, the FDIC, the FRB, the SEC and other regulatory bodies. Such regulation and supervision governs the activities in which the Company may engage. Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the imposition of restrictions on Cass' operations, investigations and limitations related to Cass' securities, the classification of Cass' assets and determination of the level of Cass' allowance for loan losses. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, legislation or supervisory action, may have a material adverse impact on Cass' operations.

Legal and regulatory proceedings and related matters with respect to the financial services industry, including those directly involving the Company and its subsidiaries, could adversely affect Cass or the financial services industry in general.

The Company is subject to various legal and regulatory proceedings. It is inherently difficult to assess the outcome of these matters, and there can be no assurance that the Company will prevail in any proceeding or litigation. Any such matter could result in substantial cost and diversion of Cass' efforts, which by itself could have a material adverse effect on Cass' financial condition and operating results. Further, adverse determinations in such matters could result in actions by Cass' regulators that could materially adversely affect Cass' business, financial condition or results of operations.

The Company's accounting policies and methods are the basis of how Cass reports its financial condition and results of operations, and they may require management to make estimates about matters that are inherently uncertain. In

addition, changes in accounting policies and practices, as may be adopted by the regulatory agencies, the Financial Accounting Standards Board, or other authoritative bodies, could materially impact Cass' financial statements.

The Company's accounting policies and methods are fundamental to how Cass records and reports its financial condition and results of operations. Management must exercise judgment in selecting and applying many of these accounting policies and methods in order to ensure that they comply with generally accepted accounting principles and reflect management's judgment as to the most appropriate manner in which to record and report Cass' financial condition and results of operations. In some cases, management must select the accounting policy or method to apply from two or more alternatives, any of which might be reasonable under the circumstances yet might result in the Company reporting materially different amounts than would have been reported under a different alternative.

Cass has identified four accounting policies as being "critical" to the presentation of its financial condition and results of operations because they require management to make particularly subjective and/or complex judgments about matters that are inherently uncertain and because of the likelihood that materially different amounts would be reported under different conditions or using different assumptions. More information on Cass' critical accounting policies is contained in Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

From time to time, the regulatory agencies, the Financial Accounting Standards Board ("FASB"), and other authoritative bodies change the financial accounting and reporting standards that govern the preparation of the Company's financial statements. These changes can be hard to predict and can materially impact how management records and reports the Company's financial condition and results of operations.

Cass is subject to examinations and challenges by tax authorities, which, if not resolved in the Company's favor, could adversely affect the Company's financial condition and results of operations.

In the normal course of business, Cass and its affiliates are routinely subject to examinations and challenges from federal and state tax authorities regarding the amount of taxes due in connection with investments it has made and the businesses in which it is engaged. Recently, federal and state taxing authorities have become increasingly aggressive in challenging tax positions taken by financial institutions. These tax positions may relate to tax compliance, sales and use, franchise, gross receipts, payroll, property and income tax issues, including tax base, apportionment and tax credit planning. The challenges made by tax authorities may result in adjustments to the timing or amount of taxable income or deductions or the allocation of income among tax jurisdictions. If any such challenges are made and are not resolved in the Company's favor, they could have an adverse effect on Cass' financial condition and results of operations.

There could be terrorist activities or other hostilities, which may adversely affect the general economy, financial and capital markets, specific industries, and the Company.

The terrorist attacks in September 2001 in the United States and ensuing events, as well as the resulting decline in consumer confidence, had a material adverse effect on the economy. Any similar future events may disrupt Cass' operations or those of its customers. In addition, these events had and may continue to have an adverse impact on the U.S. and world economy in general and consumer confidence and spending in particular, which could harm Cass' operations. Any of these events could increase volatility in the U.S. and world financial markets, which could harm Cass' stock price and may limit the capital resources available

to its customers and the Company. This could have a significant impact on Cass' operating results, revenues and costs and may result in increased volatility in the market price of Cass' common stock.

There could be natural disasters, including, but not limited to, hurricanes, tornadoes, earthquakes, fires and floods, which may adversely affect the general economy, financial and capital markets, specific industries, and the Company.

The Company has significant operations and customer base in Missouri, California, Ohio, Massachusetts, South Carolina, and other regions where natural disasters may occur. These regions are known for being vulnerable to

natural disasters and other risks, such as tornadoes, hurricanes, earthquakes, fires and floods. These types of natural disasters at times have disrupted the local economy, Cass' business and customers and have posed physical risks to Cass' property. A significant natural disaster could materially affect Cass' operating results.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The Company's headquarters are located at 13001 Hollenberg Drive, Bridgeton, Missouri. This location is owned by the Company, and includes a building with approximately 61,500 square feet of office space. The Company also owns a production facility of approximately 45,500 square feet located at 2675 Corporate Exchange Drive, Columbus, Ohio. Additional production facilities are located in Lowell, Massachusetts where approximately 25,800 square feet of office space is leased through March 2011, Greenville, South Carolina where approximately 8,500 square feet of office space is leased through November 2013, Wellington, Kansas where approximately 2,000 square feet of office space is leased through July 2011 and Columbus, Ohio where approximately 8,500 square feet of office space is leased through November 2009.

The Bank's headquarters are also located at 13001 Hollenberg Drive, Bridgeton, Missouri. The Bank occupies approximately 20,500 square feet of the 61,500 square foot building. In addition, the Bank owns a banking facility near downtown St. Louis, Missouri that consists of approximately 1,750 square feet with adjoining drive-up facilities. The Bank has additional leased facilities in Maryland Heights, Missouri (2,500 square feet), Fenton, Missouri (2,000 square feet), Chesterfield, Missouri (2,850 square feet) and Santa Ana, California (3,400 square feet).

Management believes that these facilities are suitable and adequate for the Company's operations.

ITEM 3. LEGAL PROCEEDINGS

The Company and its subsidiaries are not involved in any pending proceedings other than ordinary routine litigation incidental to their businesses. Management believes none of these proceedings, if determined adversely, would have a material effect on the businesses or financial conditions of the Company or its subsidiaries.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders during the fourth

quarter of 2008.

PART II.

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's common stock is quoted on The Nasdaq Global Select Market(R) under the symbol "CASS." As of March 2, 2009, there were 180 holders of record of the Company's common stock. High and low sale prices, as reported by The Nasdaq Global Select Market for each quarter of 2008 and 2007 were as follows:

	2008		2007	
	High	Low	High	Low
1st Quarter	$ 34.87	$ 25.01	$ 35.41	$ 29.34
2nd Quarter	34.71	29.40	34.35	28.28
3rd Quarter	39.15	29.00	34.77	28.90
4th Quarter	36.50	27.14	40.55	30.00

The Company has continuously paid regularly scheduled cash dividends since 1934 and expects to continue to pay quarterly cash dividends in the future. Cash dividends paid per share, restated for stock dividends, by the Company during the two most recent fiscal years were as follows:

	2008	2007
March	$ .120	$ .109
June	.120	.109
September	.120	.109
December	.130	.120

The Company maintains a treasury stock buyback program pursuant to which the Board of Directors has authorized the repurchase of up to 300,000 shares of the Company's common stock. The Company repurchased 120,000 shares for $3,984,000 in 2008 and did not repurchase any shares during 2007. As of December 31, 2008, 180,000 shares remained available for repurchase under the program. A portion of the repurchased shares may be used for the Company's employee benefit plans, and the balance will be available for other general corporate purposes. The stock repurchase authorization does not have an expiration date and the pace of repurchase activity will depend on factors such as levels of cash generation from operations, cash requirements for investments, repayment of debt, current stock price, and other factors. The Company may repurchase shares from time to time on the open market or in private transactions, including structured transactions. The stock repurchase program may be modified or discontinued at any time.

Performance Quoted on The Nasdaq Stock Market for the last Five Fiscal Years

The following graph compares the cumulative total returns over the last five fiscal years of a hypothetical investment of $100 in shares of common stock of the Company with a hypothetical investment of $100 in The Nasdaq Stock Market (US) ("Nasdaq") and in the index of Nasdaq computer and data processing stocks. The graph assumes $100 was invested on December 31, 2003, with dividends reinvested. Returns are based on period end prices.

[THE FOLLOWING DATA IS A REPRESENTATION OF A LINE CHART IN THE PRINTED MATERIAL]

		Dec-2003	Dec-2004	Dec-2005	D
Cass Information Systems Inc.	Return %		18.84	44.64	
	Cum $	100.00	118.84	171.89	
NASDAQ Computer and Data Processing Index	Return %		10.25	3.39	
	Cum $	100.00	110.25	113.99	
NASDAQ 100 Stock Index	Return %		10.75	1.90	
	Cum $	100.00	110.75	112.85	

9

ITEM 6. SELECTED FINANCIAL DATA

The following table presents selected financial information for each of the five years ended December 31. The selected financial data should be read in conjunction with the Company's consolidated financial statements and accompanying notes included in Item 8 of this report.

(Dollars in thousands, except per share data)	2008	2007	2006	20
Fee revenue and other income	$ 53,170	$ 48,200	$ 42,821	$ 38,6
Interest income on loans	34,204	36,288	36,164	32,2
Interest income on debt and equity securities	7,716	5,531	3,627	2,4
Other interest income	2,218	7,527	7,262	3,5
Total interest income	44,138	49,346	47,053	38,2
Interest expense on deposits	3,179	7,728	6,414	4,4
Interest expense on short-term borrowings	12	6	7	
Interest on debentures and other	187	230	198	1
Total interest expense	3,378	7,964	6,619	4,6
Net interest income	40,760	41,382	40,434	33,5
Provision for loan losses	2,200	900	1,150	7
Net interest income after provision	38,560	40,482	39,284	32,7
Operating expense	65,564	62,739	58,277	55,2
Income before income tax expense	26,166	25,943	23,828	16,2
Income tax expense	7,160	8,148	8,367	4,9
Income from continuing operations	$19,006	$ 17,795	$ 15,461	$ 11,2
Net loss from discontinued operations	--	--	(395)	(2
Net income	19,006	17,795	15,066	10,9

Diluted earnings per share from continuing operations	$ 2.03	$ 1.90	$ 1.65	$ 1.
Diluted earnings per share	2.03	1.90	1.61	1.
Dividends per share	.490	.447	.400	.3
Dividend payout ratio	24.14%	23.53%	24.84%	29.
Average total assets	$922,471	$891,734	$839,208	$776,8
Average net loans	546,110	508,621	516,164	506,8
Average debt and equity securities	197,273	141,363	91,555	71,0
Average total deposits	241,844	279,831	278,546	290,5
Average subordinated convertible debentures	3,669	3,699	3,700	3,7
Average total shareholders' equity	104,185	89,427	79,736	71,8
Return on average total assets	2.06%	2.00%	1.80%	1.
Return on average equity	18.24	19.90	18.89	15.
Average equity to assets ratio	11.29	10.03	9.50	9.
Equity to assets ratio at year-end	12.00	11.01	9.78	9.
Net interest margin	5.34	5.45	5.50	4.
Allowance for loan losses to loans at year-end	1.09	1.26	1.31	1.
Nonperforming assets to loans and foreclosed assets	.57	.77	.16	.
Net loan charge-offs to average loans outstanding	.37	.24	.16	.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis provides information about the financial condition and results of operations of the Company for the years ended December 31, 2008, 2007 and 2006. All share and per share data have been restated to give effect to the 50% and 10% stock dividends issued on September 15, 2006 and December 17, 2007, respectively. This discussion and analysis should be read in conjunction with the Company's consolidated financial statements and accompanying notes and other selected financial data presented elsewhere in this report.

10

Executive Overview

Cass provides payment and information processing services to large manufacturing, distribution and retail enterprises from its processing centers in St. Louis, Missouri, Columbus, Ohio, Boston, Massachusetts, Greenville, South Carolina and Wellington, Kansas. The Company's services include freight invoice rating, payment processing, auditing, and the generation of accounting and transportation information. Cass also processes and pays utility invoices, which include electricity, gas and telecommunications expenses, and is a provider of telecom expense management solutions. Cass extracts, stores and presents information from freight, utility and telecommunication invoices, assisting its customers' transportation, energy and information technology managers in making decisions that will enable them to improve operating performance. The Company receives data from multiple sources, electronic and otherwise, and processes the data to accomplish the specific operating requirements of its customers. It then provides the data in a central repository for access and archiving. The data is finally transformed into information through the Company's databases that allow client interaction as required and provide Internet-based tools for analytical processing. The Company also, through Cass Commercial Bank, its St. Louis, Missouri based bank subsidiary, provides banking services in the St. Louis metropolitan area, Orange County, California and other selected cities in the

United States. In addition to supporting the Company's payment operations, the Bank provides banking services to its target markets, which include privately owned businesses and churches and church-related ministries.

The specific payment and information processing services provided to each customer are developed individually to meet each customer's requirements, which can vary greatly. In addition, the degree of automation such as electronic data interchange, imaging, and web-based solutions varies greatly among customers and industries. These factors combine so that pricing varies greatly among the customer base. In general, however, Cass is compensated for its processing services through service fees and account balances that are generated during the payment process. The amount, type and calculation of service fees vary greatly by service offering, but generally follow the volume of transactions processed. Interest income from the balances generated during the payment processing cycle is affected by the amount of time Cass holds the funds prior to payment and the dollar volume processed. Both the number of transactions processed and the dollar volume processed are therefore key metrics followed by management. Other factors will also influence revenue and profitability, such as changes in the general level of interest rates, which have a significant effect on net interest income. The funds generated by these processing activities are invested in overnight investments, investment grade securities and loans generated by the Bank. The Bank earns most of its revenue from net interest income, or the difference between the interest earned on its loans and investments and the interest paid on its deposits. The Bank also assesses fees on other services such as cash management services.

Industry-wide factors that impact the Company include the willingness of large corporations to outsource key business functions such as freight, utility and telecommunication payment and audit. The benefits that can be achieved by outsourcing transaction processing and the management information generated by Cass' systems can be influenced by factors such as the competitive pressures within industries to improve profitability, the general level of transportation costs, deregulation of energy costs and consolidation of telecommunication providers. Economic factors that impact the Company include the general level of economic activity that can affect the volume and size of invoices processed, the ability to hire and retain qualified staff and the growth and quality of the loan portfolio. As lower levels of economic activity are encountered, such as those experienced in the second half of 2008, the number and total dollar amount of transactions processed by the Company may decline thereby reducing fee revenue, interest income, and possibly liquidity. The general level of interest rates also has a significant effect on the revenue of the Company. As discussed in greater detail in Item 7A, "Quantitative and Qualitative Disclosures about Market Risk," a decline in the general level of interest rates, as has been experienced during 2008, can have a negative impact on net interest income.

On July 7, 2006, the Company acquired 100% of the stock of NTransit, Inc. ("NTransit"), a company that provides auditing and expense management of parcel shipments. While this acquisition did not meet the Regulation S-X criteria of a significant business combination, it positioned the Company to expand its offerings in the specialized service and expertise in parcel shipping, which is a unique segment of the transportation industry that has experienced significant growth in recent years.

Total fee revenue and other income in 2008 increased $4,970,000, or 10%, and net interest income after provision for loan losses (also referred to as net investment income) decreased $1,922,000, or 5%, while total operating expenses increased $2,825,000, or 5%. These results were driven by a 1,950,000, or 11%, increase in items processed and $4,715,346,000, or 21%, increase in dollars processed, which were somewhat offset by the impact of a higher provision for loan losses and the decline in the general level of interest rates. The asset quality of the Company's loans and investments appears strong.

Currently, management views Cass' major opportunity and challenge as the continued expansion of its payment and information processing service offerings and customer base. Management intends to accomplish this by maintaining

the Company's lead in applied technology, which we believe, when combined with the security and processing controls of the Bank, makes Cass unique in the industry.

Recent Developments

The U.S. and global economies have experienced and are experiencing significant stress and disruptions in the financial sector. In response to the financial crisis, in October 2008, the Emergency Economic Stabilization Act of 2008 (the "EESA") was signed into law. In addition, the U.S. Treasury Department announced that it has been authorized to purchase equity stakes in participating U.S. financial institutions. Under this program, known as the Troubled Asset Relief Program - Capital Purchase Program (the "TARP Capital Purchase Program"), the U.S. Treasury Department will make capital available to participating U.S. financial institutions in exchange for, generally, preferred stock.

Further, after receiving a recommendation from the boards of the FDIC and the FRB, the U.S. Treasury signed the systemic risk exception to the FDIC Act, enabling the FDIC to temporarily provide a 100% guarantee of the senior debt of all FDIC-insured institutions and their holding companies, as well as non-interest bearing transaction deposit accounts under a Temporary Liquidity Guarantee Program.

After careful assessment, and due to its strong capital base, the Company chose not to participate in the TARP Capital Purchase Program.

The Company elected to participate in the Temporary Liquidity Guarantee Program, as not participating could have put the Company at a competitive disadvantage without the 100% FDIC guarantee of its non-interest bearing transaction deposit accounts. The FDIC guarantee of senior debt was not a factor in the Company's decision process, as it has no senior debt outstanding.

Critical Accounting Policies

The Company has prepared the consolidated financial information in this report in accordance with U.S. generally accepted accounting principles ("U.S. GAAP"). In preparing the consolidated financial statements in accordance with U.S. GAAP, management makes estimates and assumptions that affect the reported amount of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. These estimates have been generally accurate in the past, have been consistent and have not required any material changes. There can be no assurances that actual results will not differ from those estimates. Certain accounting policies that require significant management estimates and are deemed critical to our results of operations or financial position have been discussed with the Audit Committee of the Board of Directors and are described below.

Impairment of Assets. The Company periodically evaluates certain long-term assets such as intangible assets including goodwill, foreclosed assets, internally developed software and investments in private equity securities for impairment. Generally, these assets are initially recorded at cost, and recognition of impairment is required when events and circumstances indicate that the carrying amounts of these assets will not be recoverable in the future. If impairment occurs, various methods of measuring impairment may be called for

depending on the circumstances and type of asset, including quoted market prices, estimates based on similar assets, and estimates based on valuation techniques such as discounted projected cash flows. Assets held for sale are carried at the lower of cost or fair value less costs to sell. These policies affect both segments of the Company and require significant management assumptions and estimates that could result in materially different results if conditions or underlying circumstances change.

Pension Plans. The amounts recognized in the consolidated financial statements related to pensions are determined from actuarial valuations. Inherent in these valuations are assumptions including expected return on plan assets, discount rates at which the liabilities could be settled at December 31, 2008, rate of increase in future compensation levels and mortality rates. These assumptions are updated annually and are disclosed in Note 12 to the consolidated financial statements. The Company adopted Statement of Financial Accounting Standards ("SFAS") No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" ("SFAS No. 158") on December 31, 2006. SFAS No. 158 requires companies to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. The funded status is measured as the difference between the fair value of the plan assets and the projected benefit obligation as of the date of its fiscal year-end.

Income Taxes. The objectives of accounting for income taxes are to recognize the amount of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in an entity's financial statements or tax returns. Judgment is required in addressing the future tax consequences of events that have been recognized in the Company's financial statements or tax returns such as the realization of deferred tax assets, changes in tax laws or interpretations thereof. In addition, the Company is subject to the continuous examination of its income tax returns by the Internal Revenue Service and other taxing authorities. Effective January 1, 2007, the Company adopted FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). FIN 48 provides guidance for the recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. See Note 15 to the consolidated financial statements.

Allowance for Loan Losses. The Company performs periodic and systematic detailed reviews of its loan portfolio to assess overall collectability. The level of the allowance for loan losses reflects management's estimate of the collectability of the loan portfolio. Although these estimates are based on established methodologies for determining allowance requirements, actual results can differ significantly from estimated results. These policies affect both segments of the Company. The impact and associated risks related to these policies on the Company's business operations are discussed in the "Provision and Allowance for Loan Losses" section of this report.

Summary of Results

	December 31,			
(In thousands, except per share data)	2008	2007	2006	2008 v.
Total processing volume	36,416	32,740	29,266	11.

Total processing dollars	$26,900,535	$22,185,189	$19,871,281	21.
Payment and processing fees	$50,721	$45,642	$40,343	11.
Net investment income	$38,560	$40,482	$39,284	(4.
Total net revenue	$91,730	$88,682	$82,105	3.
Average earning assets	$841,367	$809,739	$762,397	3.
Net interest margin*	5.34%	5.45%	5.50%	(2.
Net income from continuing operations	$19,006	$17,795	$15,461	6.
Diluted EPS from continuing operations	$2.03	$1.90	$1.65	6.
Net income	$19,006	$17,795	$15,066	6.
Diluted earnings per share	$2.03	$1.90	$1.61	6.
Return on average assets	2.06%	2.00%	1.80%	
Return on average equity	18.24%	19.90%	18.89%	

* Presented on a tax-equivalent basis

The results of 2008 compared to 2007 include the following significant items:

Payment and processing fee revenue from continuing operations increased as the number of transactions processed increased. This increase was driven mainly by Utility Information Services processing activity which added a significant amount of new business during 2008. Transportation Information Services also achieved record levels of processing during 2008 and record levels of new customers added.

Net investment income decreased $1,922,000 primarily due to both a decline in the general level of interest rates and an increase in the provision for loan losses. The net interest margin on a tax equivalent basis was 5.34% in 2008 compared to 5.45% in 2007. The growth in average earning assets was funded mainly by increases in accounts and drafts payable due to the increase in dollars processed.

There were $552,000 gains from the sale of securities in 2008 and no gains in 2007. Bank service fees decreased $352,000, or 21%, to $1,330,000. Other income from continuing operations decreased $309,000 in 2008 or 35%. Operating expenses from continuing operations increased $2,825,000, or 5%, due mainly to expenses relating to the increase in processing activity.

The results of 2007 compared to 2006 include the following significant items:

Payment and processing fee revenue from continuing operations increased as the number of transactions processed increased. This increase was driven mainly by Utility Information Services processing activity which added a significant amount of new business during 2007. Transportation Information Services also achieved record levels of processing during 2007 and record levels of new customers added.

Net investment income increased $1,198,000 due to an increase in average earning assets. The net interest margin on a tax equivalent basis was 5.45% in 2007 compared to 5.50% in 2006. The growth in average earning assets was funded mainly by increases in accounts and drafts payable due to the increase in dollars processed.

There were no gains from the sale of securities in 2007 and 2006. Bank service fees increased $57,000, or 4%, to $1,682,000. Other income from continuing operations remained fairly constant at $876,000 in 2007 and $853,000 in 2006. Operating expenses from continuing operations increased $4,462,000, or 8%, due mainly to expenses relating to the increase in processing activity.

Fee Revenue and Other Income from Continuing Operations

The Company's fee revenue is derived mainly from freight and utility payment and processing fees. As the Company provides its processing and payment services, it is compensated by service fees which are typically calculated on a per-item basis and by the accounts and drafts payable balances generated in the payment process which can be used to generate interest income. Processing volumes, fee revenue and other income for the years ended December 31, 2008, 2007 and 2006 were as follows:

	December 31,			%
(In thousands)	2008	2007	2006	2008 v. 200
Freight invoice transaction volume	25,854	23,480	22,601	10.1%
Freight invoice dollar volume	$17,482,520	$14,519,906	$14,199,389	20.4%
Utility transaction volume	10,562	9,260	6,665	14.1%
Utility transaction dollar volume	$9,418,015	$7,665,283	$5,671,892	22.9%
Payment and processing revenue	$50,721	$45,642	$40,343	11.1%
Bank service fees	$1,330	$1,682	$1,625	(20.9)%
Gains on sales of investment securities	$552	--	--	N/A
Other	$567	$876	$853	(35.3)%

Fee revenue and other income in 2008 compared to 2007 include the following significant pre-tax components:

Freight volume increased by 2,374,000 transactions during the past year. This increase was due mainly to new business in 2008 somewhat offset by the impact of the general economic slow down on existing customer processing activity, particularly in the second half of the year. Utility volume experienced solid growth, adding more than 1,302,000 transactions in 2008. This growth was due mainly to new business. These transaction volume increases drove most of the $5,079,000 increase in payment and processing revenue.

Fee revenue and other income in 2007 compared to 2006 include the following significant pre-tax components:

Freight volume increased by 879,000 transactions during 2007. This increase was due mainly to new business in 2007. Utility volume experienced significant growth, adding more than 2,595,000 transactions in 2007. This growth was due mainly to new business. These transaction volume increases drove most of the $5,299,000 increase in payment and processing revenue.

Net Interest Income

Net interest income is the difference between interest earned on loans, investments, and other earning assets and interest expense on deposits and other interest-bearing liabilities. Net interest income is a significant source of the Company's revenues. The following table summarizes the changes in tax-equivalent net interest income and related factors for the three periods ended December 31, 2008, 2007 and 2006:

				% Change
(In Thousands)	2008	2007	2006	2008 v. 2007

Average earning assets	$841,366	$809,739	$762,397	3.9%
Net interest income*	44,966	44,115	41,950	1.9%
Net interest margin*	5.34%	5.45%	5.50%	(2.0)%
Yield on earning assets	5.75%	6.43%	6.37%	(10.6)%
Rate on interest bearing liabilities	2.16%	4.20%	3.62%	(48.6)%

*Presented on a tax-equivalent basis using a tax rate of 35%.

Net interest income in 2008 compared to 2007:

The increase in net interest income was caused by the increase in earning assets partially offset by a decrease in net interest margin. The increase in earning assets was funded mainly by the increase in accounts and drafts payable due to the increased dollars processed. The decrease in net interest margin was due mainly to

the reduction in the general level of interest rates. The Company is negatively affected by decreases in the level of interest rates. Conversely, the Company is positively affected by increases in the level of interest rates due to the fact that its rate sensitive assets significantly exceed its rate sensitive liabilities. This is primarily due to the non-interest-bearing liabilities generated by the Company in the form of accounts and drafts payable. More information is contained in the tables below and in Item 7A of this report.

Total average loans increased $37,210,000, or 7%, to $552,333,000. Loans have a positive effect on interest income and the net interest margin due to the fact that loans are one of the Company's highest yielding earning assets for any given maturity.

Total average investment in securities increased $55,910,000, or 40%, to $197,273,000. The investment portfolio will expand and contract over time as the interest rate environment changes and the Company manages its liquidity and interest rate position. The increase in 2008 was due to the purchase of state and political subdivision securities with AA or better credit ratings and maturities approaching ten years. With the declining interest rate environment, the Company made these purchases to reduce the level of short-term rate sensitive assets. All purchases were made in accordance with the Company's investment policy. Total average federal funds sold and other short-term investments decreased $61,493,000, or 40%, to $91,760,000. This decrease was the primary offset to the previously mentioned increases in loans and investment securities.

The Bank's average interest-bearing deposits decreased $33,634,000, or 18%, compared to the prior year. This decrease was primarily the result of the reduction of higher-cost time deposits. Average rates paid on interest-bearing liabilities decreased from 4.20% to 2.16% as a result of an overall decline in the interest rate environment during 2008 combined with the previously mentioned reduction in higher-cost time deposits.

Net interest income in 2007 compared to 2006:

The increase in net interest income was caused by the increase in earning assets partially offset by a slight decrease in net interest

margin. The increase in earning assets was funded mainly by the increase in accounts and drafts payable due to the increased dollars processed. The decrease in net interest margin was due mainly to the reduction in the general level of interest rates. The Company is negatively affected by decreases in the level of interest rates. Conversely, the Company is positively affected by increases in the level of interest rates due to the fact that its rate sensitive assets significantly exceed its rate sensitive liabilities. This is primarily due to the non-interest-bearing liabilities generated by the Company in the form of accounts and drafts payable. More information is contained in the tables below and in Item 7A of this report.

Total average loans decreased $7,244,000, or 1%, to $515,123,000. Loans have a positive effect on interest income and the net interest margin due to the fact that loans are one of the Company's highest yielding earning assets for any given maturity.

Total average investment in securities increased $49,808,000, or 54%, to $141,363,000. The investment portfolio will expand and contract over time as the interest rate environment changes and the Company manages its liquidity and interest rate position. The increase in 2007 was due to the purchase of state and political subdivision securities with AA or better credit ratings and maturities approaching ten years. With the expectations of a declining interest rate environment, the Company made these purchases to reduce the level of short-term rate sensitive assets. All purchases were made in accordance with the Company's investment policy. Total average federal funds sold and other short-term investments increased $4,778,000, or 3%, to $153,253,000. This increase was funded by the increase in accounts and drafts payable.

The Bank's average interest-bearing deposits remained relatively flat with a $6,450,000, or 4%, increase compared to the prior year. Average demand deposits decreased $5,165,000, or 5%, as customers moved their deposited funds into higher yielding off-balance sheet investment products. Average rates paid on interest-bearing liabilities increased from 3.62% to 4.20% as a result of increased rate competition for savings deposits and certificates of deposit in the markets served by the Bank.

Distribution of Assets, Liabilities and Shareholders' Equity; Interest Rate and Interest Differential

The following table contains condensed average balance sheets for each of the periods reported, the tax-equivalent interest income and expense on each category of interest-earning assets and interest-bearing liabilities, and the average yield on such categories of interest-earning assets and the average rates paid on such categories of interest-bearing liabilities for each of the periods reported:

	2008			2007		
(Dollars in thousands)	Average Balance	Interest Income/ Expense	Yield/ Rate	Average Balance	Interest Income/ Expense	Yield/ Rate

Assets(1)						
Earning assets:						
Loans (2,3):						
Taxable	$548,500	$34,030	6.20%	$509,409	$36,021	7.07%
Tax-exempt (4)	3,833	268	6.97	5,714	411	7.19
Securities (5):						
Taxable	2,758	78	2.83	15,309	722	4.72
Tax-exempt (4)	194,515	11,750	6.04	126,054	7,398	5.87
Federal funds sold and other short-term investments	91,760	2,218	2.42	153,253	7,527	4.91
Total earning assets	841,366	48,344	5.75	809,739	52,079	6.43
Nonearning assets:						
Cash and due from banks	11,607			24,313		
Premises and equipment, net	12,393			12,915		
Bank owned life insurance	12,802			12,261		
Goodwill and other intangibles, net	8,216			8,495		
Other assets	42,310			30,513		
Assets related to discontinued operations	--			--		
Allowance for loan losses	(6,223)			(6,502)		
Total assets	$922,471			$891,734		
Liabilities And Shareholders' Equity (1)						
Interest-bearing liabilities:						
Interest-bearing demand deposits	$77,835	$1,086	1.40%	$ 67,719	$2,122	3.13%
Savings deposits	21,434	290	1.35	23,859	795	3.33
Time deposits of $100 or more	32,052	1,102	3.44	65,127	3,357	5.15
Other time deposits	20,712	701	3.38	28,962	1,454	5.02
Total interest-bearing deposits	152,033	3,179	2.09	185,667	7,728	4.16
Short-term borrowings	876	12	1.37	138	6	4.35
Subordinated convertible debentures	3,669	187	5.10	3,699	230	5.33
Total interest-bearing liabilities	156,578	3,378	2.16	189,504	7,964	4.20
Noninterest-bearing liabilities:						
Demand deposits	89,811			94,164		
Accounts and drafts payable	559,230			504,678		
Other liabilities	12,667			13,961		
Liabilities related to discontinued operations	--			--		
Total liabilities	818,286			802,307		
Shareholders' equity	104,185			89,427		
Total liabilities and shareholders' equity	$922,471			$891,734		
Net interest income		$44,966			$44,115	
Net interest margin		5.34%			5.45%	
Interest spread		3.59%			2.23%	

1. Balances shown are daily averages.
2. For purposes of these computations, nonaccrual loans are included in the

average loan amounts outstanding. Interest on nonaccrual loans is recorded when received as discussed further in Item 8, Note 1 of this report.
3. Interest income on loans includes net loan fees of $310,000, $202,000 and $213,000 for 2008, 2007 and 2006, respectively.
4. Interest income is presented on a tax-equivalent basis assuming a tax rate of 35% for 2008, 2007 and 2006. The tax-equivalent adjustment was approximately $4,206,000, $2,733,000 and $1,516,000 for 2008, 2007 and 2006, respectively.
5. For purposes of these computations, yields on investment securities are computed as interest income divided by the average amortized cost of the investments.

16

Analysis of Net Interest Income Changes

The following table presents the changes in interest income and expense between years due to changes in volume and interest rates.

	2008 Over 2007			
(Dollars in thousands)	Volume(1)	Rate(1)	Total	Volume(
Increase (decrease) in interest income:				
Loans (2,3):				
Taxable	$2,643	$(4,634)	$(1,991)	$(527)
Tax-exempt (4)	(132)	(11)	(143)	22
Securities:				
Taxable	(433)	(211)	(644)	(426)
Tax-exempt (4)	4,129	223	4,352	3,464
Federal funds sold and other short-term investments	(2,343)	(2,966)	(5,309)	234
Total interest income	$3,864	$(7,599)	$(3,735)	$2,767
Interest expense on:				
Interest-bearing demand deposits	281	(1,317)	(1,036)	(89)
Savings deposits	(74)	(431)	(505)	(36)
Time deposits of $100 or more	(1,363)	(892)	(2,255)	585
Other time deposits	(350)	(403)	(753)	(24)
Short-term borrowings	13	(7)	6	(1)
Subordinated convertible debenture	(16)	(27)	(43)	6
Total interest expense	(1,509)	(3,077)	(4,586)	441
Net interest income	$5,373	$(4,522)	$851	$2,326

1. The change in interest due to the combined rate/volume variance has been allocated in proportion to the absolute dollar amounts of the change in each.
2. Average balances include nonaccrual loans.
3. Interest income includes net loan fees.
4. Interest income is presented on a tax-equivalent basis assuming a tax rate of 35% for 2008, 2007 and 2006.

Loan Portfolio

Interest earned on the loan portfolio is a primary source of income for the Company. The loan portfolio was $591,976,000 and represented 67% of the Company's total assets as of December 31, 2008 and generated $34,204,000 in revenue during the year then ended. The Company had no sub-prime mortgage loans or residential development loans in its portfolio as of December 31, 2008. The following tables show the composition of the loan portfolio at the end of the periods indicated and remaining maturities for loans as of December 31, 2008.

Loans by Type
(At December 31)

(Dollars in thousands)	2008	2007	2006	2005
Commercial and industrial	$118,044	$100,827	$113,162	$146,892
Real estate: (Commercial and Church)				
Mortgage	412,788	360,907	352,044	348,554
Construction	56,221	31,082	29,779	28,170
Industrial revenue bonds	3,363	4,149	6,293	4,514
Installment	--	--	--	107
Other	1,560	1,490	2,847	1,069
Total loans	$591,976	$498,455	$504,125	$529,306

Loans by Maturity
(At December 31, 2008)

	One Year Or Less		Over 1 Year Through 5 Years		Over 5 Years	
(Dollars in thousands)	Fixed Rate	Floating Rate(1)	Fixed Rate	Floating Rate(1)	Fixed Rate	Flo Rat
Commercial and industrial	$21,294	$ 68,597	$ 18,387	$ 8,505	$1,261	$
Real estate: (Commercial and Church)						
Mortgage	41,369	37,161	323,854	6,078	4,326	
Construction	25,856	13,442	3,398	13,525	--	
Industrial revenue bonds	1,026	-	2,337	--	--	
Other	418	933	206	3	--	
Total loans	$89,963	$120,133	$348,182	$28,111	$5,587	

(1) Loans have been classified as having "floating" interest rates if the rate specified in the loan varies with the prime commercial rate of interest. Note: Due to the historically low interest rates encountered during 2008 the Company instituted a 4% floor for its prime lending rate.

The Company has no concentrations of loans exceeding 10% of total loans, which are not otherwise disclosed in the loan portfolio composition table and as are

discussed in Item 8, Note 5 of this report. As can be seen in the loan composition table above and as are discussed in Item 8, Note 5, the Company's primary market niche for banking services is privately held businesses and churches and church-related ministries.

Loans to commercial entities are generally secured by the business assets of the borrower, including accounts receivable, inventory, machinery and equipment, and the real estate from which the borrower operates. Operating lines of credit to these companies generally are secured by accounts receivable and inventory, with specific percentages of each determined on a customer-by-customer basis based on various factors including the type of business. Intermediate term credit for machinery and equipment is generally provided at some percentage of the value of the equipment purchased, depending on the type of machinery or equipment purchased by the entity. Loans secured exclusively by real estate to businesses and churches are generally made with a maximum 80% loan to value ratio, depending upon the Company's estimate of the resale value and ability of the property to generate cash. The Company's loan policy requires an independent appraisal for all loans over $250,000 secured by real estate. Company management monitors the local economy in an attempt to determine whether it has had a significant deteriorating effect on such real estate credits. When problems are identified, appraised values are updated on a continual basis, either internally or through an updated external appraisal.

Loan portfolio changes from December 31, 2007 to December 31, 2008:

Total loans increased $93,521,000, or 19%, to $591,976,000. This increase was the result of two primary factors: 1) the successful implementation of new marketing efforts by the Company's lending staff and 2) the negative impact of the credit crisis on many of the Company's competitors resulted in more attractive loan growth opportunities. The growth in real estate construction loans was primarily due to increased activity in the church portfolio. At year-end, church and church-related real estate and construction loans totaled $310,329,000, which represents a 22% increase over 2007. Additional details regarding the types and maturities of loans in the loan portfolio are contained in the tables above and in Item 8, Note 5.

Loan portfolio changes from December 31, 2006 to December 31, 2007:

Total loans decreased $5,670,000, or 1%, to $498,455,000. This decrease was due mainly to the reduction in commercial and industrial loans as loans were paid down. At the end of 2007, church and church-related real estate and construction credits totaled $253,626,000, which represents a 12% increase over 2006. Additional details regarding the types and maturities of loans in the loan portfolio are contained in the tables above and in Item 8, Note 5.

Provision and Allowance for Loan Losses

The Company recorded a provision for loan losses of $2,200,000 in 2008, $900,000 in 2007 and $1,150,000 in 2006. The amount of the provisions for loan losses was derived from the Company's quarterly analysis of the allowance for loan losses in relation to probable losses in the loan portfolio. The amount of the provision will fluctuate as determined by these quarterly analyses. The Company had net loan charge-offs of $2,029,000, $1,212,000 and $842,000 in 2008, 2007 and 2006, respectively. The allowance for loan losses was $6,451,000 at December 31, 2008 compared to $6,280,000 at December 31, 2007 and $6,592,000 at December 31, 2006. The year-end 2008 allowance

represented 1.09% of outstanding loans, compared to 1.26% at year-end 2007 and 1.31% at year-end 2006. From December 31, 2007 to December 31, 2008, the level of nonperforming loans decreased $1,262,000 from $2,481,000 to $1,219,000, which represents .21% of outstanding loans. Nonperforming loans are more fully explained in the section entitled "Nonperforming Assets."

The allowance for loan losses has been established and is maintained to absorb probable losses in the loan portfolio. An ongoing assessment of risk of loss is performed to determine if the current balance of the allowance is adequate to cover probable losses in the portfolio. Charges or credits are made to expense to cover any deficiency or reduce any excess, as required. The current methodology employed to determine the appropriate allowance consists of two components, specific and general. The Company develops specific valuation allowances on commercial, commercial real estate, and construction loans based on individual review of these loans and an estimate of the borrower's ability to repay the loan given the availability of collateral, other sources of cash flow and collection options available. The general component relates to all other loans, which are evaluated based on loan grade. The loan grade assigned to each loan is typically evaluated on an annual basis, unless circumstances require interim evaluation. The Company assigns a reserve amount consistent with each loan's rating category. The reserve amount is based on derived loss experience over prescribed periods. In addition to the amounts derived from the loan grades, a portion is added to the general reserve to take into account other factors including national and local economic conditions, downturns in specific industries including loss in collateral value, trends in credit quality at the Company and the banking industry, and trends in risk rating changes. As part of their examination process, federal and state agencies review the Company's methodology for maintaining the allowance for loan losses and the balance in the account. These agencies may require the Company to increase the allowance for loan losses based on their judgments and interpretations about information available to them at the time of their examination.

The following schedule summarizes activity in the allowance for loan losses and the allocation of the allowance to the Company's loan categories. During 2008, the allocation of the allowance to the commercial loan portfolio declined because one loan with a reserve allocation of $900,000 was paid off and one loan of $809,000 was charged off. The allocation to the real estate portfolio increased primarily due to the $51,881,000 in additional loan balances.

Summary of Loan Loss Experience

	December 31,			
(Dollars in thousands)	2008	2007	2006	2005
Allowance at beginning of year	$6,280	$6,592	$6,284	$6,037
Loans charged-off:				
Commercial and industrial loans and industrial revenue bonds ("IRB's")	2,120	337	864	532
Real estate: (Commercial and Church)				
Mortgage	--	1,038	--	22
Other	53	--	--	1
Total loans charged-off	2,173	1,375	864	555
Recoveries of loans previously charged-off:				
Commercial, industrial and IRB's	136	159	22	10
Real estate: (Commercial and Church)				

Mortgage	--	4	--	13
Other	8	--	--	4
Total recoveries of loans previously charged-off	144	163	22	27
Net loans charged-off	2,029	1,212	842	528
Provision charged to expense	2,200	900	1,150	775
Allowance at end of year	$6,451	$6,280	$6,592	$6,284
Loans outstanding:				
Average	$552,333	$515,123	$522,367	$512,966
December 31	591,976	498,455	504,125	529,306
Ratio of allowance for loan losses to loans outstanding:				
Average	1.17%	1.22%	1.26%	1.23%
December 31	1.09%	1.26%	1.31%	1.19%
Ratio of net charge-offs to average loans outstanding	.37%	.24%	.16%	.10%

19

Allocation of allowance for loan losses(1):				
Commercial, industrial and IRB's	$1,521	$3,380	$3,507	$3,419
Real estate: (Commercial and Church)				
Mortgage	4,343	2,564	2,723	2,645
Construction	569	318	271	200
Other loans	18	18	91	20
Total	$6,451	$6,280	$6,592	$6,284
Percent of categories to total loans:				
Commercial and industrial and IRB's	20.5%	21.1%	22.5%	28.6%
Real estate: (Commercial and Church)				
Mortgage	69.7	72.4	69.8	65.9
Construction	9.5	6.2	5.9	5.3
Other	.3	.3	1.8	.2
Total	100.0%	100.0%	100.0%	100.0%

(1) Although specific allocations exist, the entire allowance is available to absorb losses in any particular loan category.

Nonperforming Assets

It is the policy of the Company to continually monitor its loan portfolio and to discontinue the accrual of interest on any loan on which payment of principal or interest in a timely manner in the normal course of business, is doubtful. Subsequent payments received on such loans are applied to principal if there is any doubt as to the collectability of such principal; otherwise, these receipts are recorded as interest income. Interest on nonaccrual and renegotiated loans, which would have been recorded under the original terms of the loans, was approximately $86,000 for the year ended December 31, 2008. Of this amount, approximately $56,000 was actually recorded as interest income on such loans.

Total nonaccrual loans at December 31, 2008 consists of five loans totaling $1,178,000 that relate to businesses that have weak financial positions and/or collateral deficiencies. Allocations of the allowance for loan losses have been established for the estimated loss exposure.

Foreclosed assets and accruing loans 90 days or more past due were $2,177,000 and $41,000, respectively, at December 31, 2008. The foreclosed assets relate to the foreclosure of two loans which were secured by commercial real estate buildings in St. Louis County and St. Charles County, Missouri. These buildings are currently listed for sale and have been recorded at their estimated fair value less costs to sell. The decrease in accruing loans 90 days or more past due is primarily related to one loan of $41,000 that was past its maturity date; however, full payment was received in March, 2009.

The Company does not have any foreign loans. The Company's loan portfolio does not include a significant amount of single family real estate mortgages, as the Company does not market its services to retail customers. Also, the Company had no sub-prime mortgage loans or residential development loans in its portfolio as of December 31, 2008.

The Company does not have any other interest-earning assets which would have been included in nonaccrual, past due or restructured loans if such assets were loans.

Summary of Nonperforming Assets

	December 31,			
(Dollars in thousands)	2008	2007	2006	
Commercial, industrial and IRB's:				
Nonaccrual	$ 278	$ 1,277	$ 795	$
Contractually past due 90 days or more and still accruing	41	496	--	
Renegotiated loans	--	--	--	
Real estate-mortgage:				
Nonaccrual	900	708	--	
Contractually past due 90 days or more and still accruing	--	--	--	
Renegotiated loans	--	--	--	
Total nonperforming loans	1,219	2,481	795	1
Total foreclosed assets	2,177	1,388	--	
Total nonperforming assets	$ 3,396	$ 3,869	$ 795	$1

20

Operating Expenses from Continuing Operations

Operating expenses from continuing operations in 2008 compared to 2007 include the following significant pre-tax components:

Salaries and employees benefits expense increased $2,758,000, or 6%, to

$49,723,000. This is mainly attributable to additional staff related to the increase in processing volume, annual salary increases and the associated increase in benefit expenses.

Occupancy expense increased $122,000, or 6%, to $2,228,000 as a result of additional maintenance and repairs expense plus an increase in rent expense.

Equipment expense decreased $25,000, or 1%, to $3,331,000. This decrease is primarily due to a reduction in contract maintenance expense.

Amortization of intangibles was $280,000 in 2008 and 2007 due to the intangible assets acquired in the acquisition of NTransit in July 2006.

Other operating expense decreased $30,000, or less than 1%, to $10,002,000 due to reductions in postage and supplies, promotional expense and professional services offset by an increase in other real estate owned expense.

Operating expenses from continuing operations in 2007 compared to 2006 include the following significant pre-tax components:

Salaries and employees benefits expense increased $4,289,000, or 10%, to $46,965,000. This is mainly attributable to additional staff related to the increase in processing volume, annual salary increases and the associated increase in benefit expenses.

Occupancy expense increased $127,000, or 6%, to $2,106,000.

Equipment expense increased $428,000, or 15%, to $3,356,000. This increase is primarily due to depreciation related to capital expenditures in 2006 and 2007.

Amortization of intangibles increased $54,000, or 24%, to $280,000 due to the intangible assets acquired in the acquisition of NTransit in July 2006.

Other operating expense decreased $436,000, or 4%, to $10,032,000 due to reductions in outside imaging and legal expenses.

Income Tax Expense

Income tax expense from continuing operations in 2008 totaled $7,160,000 compared to $8,148,000 in 2007, and compared to $8,367,000 in 2006. When measured as a percent of income from continuing operations, the Company's effective tax rate was 27% in 2008, 31% in 2007 and 35% in 2006. The effective tax rate varies from year-to-year primarily due to changes in the Company's amount of investment in tax-exempt municipal bonds and income recognized on bank owned life insurance. The Company's income tax benefit from discontinued operations was $0, $0 and $280,000 with effective rates of 0%, 0%, and 41% for the years 2008, 2007 and 2006, respectively.

Investment Portfolio

Investment portfolio changes from December 31, 2007 to December 31, 2008:

U.S. Treasury securities decreased $1,796,000, or 90%, to $200,000. U.S. government-sponsored corporation and agency securities decreased from $1,499,000 to $0. State and political subdivision securities increased $25,440,000, or 15%, to $192,918,000. The investment portfolio provides the Company with a significant source of earnings,

secondary source of liquidity, and mechanisms to manage the effects of changes in loan demand and interest rates. Therefore, the size, asset allocation and maturity distribution of the investment portfolio will vary over time depending on management's assessment of current and future interest rates, changes in loan demand, changes in the Company's sources of funds and the economic outlook. During this period, the size of the investment portfolio increased as the Company purchased state and political subdivision securities. These securities all had AA or better credit ratings and maturities approaching ten

21

years. With the additional liquidity provided by the increase in accounts and drafts payables and the declining rate environment, the Company made these purchases to continue to reduce the level of short-term rate sensitive assets. All purchases were made in accordance with the Company's investment policy. As of December 31, 2008, the Company had no mortgage-backed securities in its portfolio.

Investment portfolio changes from December 31, 2006 to December 31, 2007:

U.S. Treasury securities decreased $14,828,000, or 88%, to $1,996,000. U.S. government-sponsored corporation and agency securities decreased $1,486,000, or 50%, to $1,499,000. State and political subdivision securities increased $85,271,000, or 104%, to $167,478,000. The investment portfolio provides the Company with a significant source of earnings, secondary source of liquidity, and mechanisms to manage the effects of changes in loan demand and interest rates. Therefore, the size, asset allocation and maturity distribution of the investment portfolio will vary over time depending on management's assessment of current and future interest rates, changes in loan demand, changes in the Company's sources of funds and the economic outlook. During this period the size of the investment portfolio increased as the Company purchased state and political subdivision securities. These securities all had AA or better credit ratings and maturities approaching ten years. With the additional liquidity provided by the increase in accounts and drafts payables and the expectation of a declining rate environment, the Company made these purchases to reduce the level of short-term rate sensitive assets. All purchases were made in accordance with the Company's investment policy. As of December 31, 2007, the Company had no mortgage-backed securities in its portfolio.

There was no single issuer of securities in the investment portfolio at December 31, 2008 for which the aggregate amortized cost exceeded 10% of total shareholders' equity.

Investments by Type

	Decembe	
(Dollars in thousands)	2008	200
U.S. Treasury securities	$ 200	$ 1,99
U.S. government-sponsored corporations and agencies	--	1,49
State and political subdivisions	192,918	167,47
Stock of the Federal Home Loan Bank	465	45
Stock of the Federal Reserve Bank	282	28

Total investments	$ 193,865	$ 171,70

Investment in Debt Securities by Maturity
(At December 31, 2008)

(Dollars in thousands)	Within 1 Year	Over 1 to 5 Years	Over 5 to 10 Years	Over 10 Yea
U.S. Treasury securities	$ 200	$ --	$ --	$
State and political subdivisions(1)	13,229	45,999	72,066	61,6
Total investment in debt securities	$ 13,429	$ 45,999	$ 72,066	$ 61,6
Weighted average yield	4.99%	5.72%	6.18%	6.4

1. Weighted average yield is presented on a tax-equivalent basis assuming a tax rate of 35%.

Deposits and Accounts and Drafts Payable

Noninterest-bearing demand deposits increased $10,110,000, or 11%, from December 31, 2007 to $103,300,000 at December 31, 2008. The average balances of these deposits decreased $4,353,000, or 5%, from 2007 to $89,811,000 in 2008. The increase in ending balances relates mainly to growth in these accounts during the latter part of the year. These balances are primarily maintained by commercial customers and churches and can fluctuate on a daily basis.

Interest-bearing deposits decreased $6,165,000, or 3%, from December 31, 2007 to $174,241,000 at December 31, 2008. The average balances of these deposits decreased to $152,033,000 in 2008 from $185,667,000 in 2007. This decrease was primarily the result of the Company's decision to reduce higher-cost time deposits.

Accounts and drafts payable generated by the Company in its payment processing operations decreased $34,709,000, or 7%, from December 31, 2007 to $479,025,000 at December 31, 2008. The average balance of these funds increased $54,552,000, or 11%, from 2007 to $559,230,000 in 2008. The increase relates to the increase in dollars processed. Due to the Company's payment processing cycle, average balances are much more indicative of the underlying

activity than period-end balances since point-in-time comparisons can be misleading if the comparison dates fall on different days of the week.

The composition of average deposits and the average rates paid on those deposits is represented in the table entitled "Distribution of Assets, Liabilities and Shareholders' Equity; Interest Rate and Interest Differential" which is included earlier in this discussion. The Company does not have any significant deposits from foreign depositors.

As discussed in "Recent Developments," the company elected to participate in the Temporary Liquidity Guarantee Program, as not participating could have put the Company at a competitive disadvantage without the 100% FDIC guarantee of its

non-interest bearing transaction deposit accounts. The cost of this program is 10 basis points or approximately $60,000 on an annual basis based upon the additional covered deposits at December 31, 2008.

Maturities of Certificates of Deposits of $100,000 or More
(At December 31, 2008)

(Dollars in thousands)	
Three months or less	$18,602
Three to six months	15,697
Six to twelve months	10,635
Over twelve months	2,325
Total	$47,259

Subordinated Convertible Debentures

Total subordinated convertible debentures at December 31, 2008 and 2007 were $2,991,000 and $3,688,000, respectively and the average balances of these funds were and $3,669,000 and $3,699,000, respectively. The debentures were issued on August 24, 2004 as part of the Company's purchase of PROFITLAB, Inc. ("PROFITLAB"). For more information on these debentures please refer to Item 8, Note 10 of this report.

Liquidity

The discipline of liquidity management as practiced by the Company seeks to ensure that funds are available to fulfill all payment obligations relating to invoices processed as they become due, meet depositor withdrawal requests and borrower credit demands while at the same time maximizing profitability. This is accomplished by balancing changes in demand for funds with changes in supply of funds. Primary liquidity to meet demand is provided by short-term liquid assets that can be converted to cash, maturing securities and the ability to obtain funds from external sources. The Company's Asset/Liability Committee ("ALCO") has direct oversight responsibility for the Company's liquidity position and profile. Management considers both on-balance sheet and off-balance sheet items in its evaluation of liquidity.

The balances of liquid assets consist of cash and cash equivalents, which include cash and due from banks, federal funds sold, and money market funds, and were $29,485,000 at December 31, 2008, a decrease of $146,585,000 or 83% from December 31, 2007. At December 31, 2008 these assets represented 3% of total assets. The Company decreased liquid assets during 2008 as a result of the significant drop in short-term interest rates. The excess liquidity held at the end of 2007 was invested in higher-yielding loans and investment securities to help maximize net interest income during 2008. Cash and cash equivalents are the Company's and its subsidiaries' primary source of liquidity to meet future expected and unexpected loan demand, depositor withdrawals or reductions in accounts and drafts payable.

Secondary sources of liquidity include the investment portfolio and borrowing lines. Total investment in debt securities available-for-sale at fair value was $193,865,000 at December 31, 2008, an increase of $22,159,000 or 13% from December 31, 2007. These assets represented 22% of total assets at December 31, 2008 and all but less than 1% were state and political subdivision securities. Of the total portfolio, 6% mature in one year, 22% mature after one year through

five years and 72% mature after five years. The Company sold $20,867,000 of securities available-for-sale during 2008 in managing its liquidity position and to take advantage of favorable reinvestment opportunities.

The Bank has unsecured lines of credit at correspondent banks to purchase federal funds up to a maximum of $46,000,000. Additionally, the Bank maintains lines of credit at unaffiliated financial institutions in the maximum amount of $81,643,000 collateralized by U.S. Treasury securities and commercial mortgage loans.

The deposits of the Company's banking subsidiary have historically been stable, consisting of a sizable volume of core deposits related to customers that utilize many other commercial products of the Bank. The accounts and drafts payable generated by the Company have also historically been a stable source of funds.

Net cash flows provided by operating activities from continuing operations for the years 2008, 2007 and 2006 were $22,030,000, $23,652,000 and $17,031,000 respectively. Net income plus depreciation and amortization accounts for most of the operating cash provided. Net cash flows from investing and financing activities fluctuate greatly as the Company actively manages its investment and loan portfolios and customer activity influences changes in deposit and accounts and drafts payable balances. Further analysis of the changes in these account balances is discussed earlier in this report. Due to the daily fluctuations in these account balances, management believes that the analysis of changes in average balances, also discussed earlier in this report, can be more indicative of underlying activity than the period-end balances used in the statements of cash flows. Management anticipates that cash and cash equivalents, maturing investments, cash from operations, and borrowing lines will continue to be sufficient to fund the Company's operations and capital expenditures in 2009.

Capital Resources

One of management's primary objectives is to maintain a strong capital base to warrant the confidence of customers, shareholders, and bank regulatory agencies. A strong capital base is needed to take advantage of profitable growth opportunities that arise and to provide assurance to depositors and creditors. The Company and its banking subsidiary continue to exceed all regulatory capital requirements, as evidenced by the capital ratios at December 31, 2008 as shown in Item 8, Note 3 of this report.

In 2008, cash dividends paid were $.49 per share for a total of $4,499,000, an increase of $381,000, or 9%, compared to $.447 per share and a total of $4,118,000 in 2007. The increase is attributable primarily to the per share amount paid.

Shareholders' equity was $106,241,000, or 12%, of total assets, at December 31, 2008, an increase of $6,789,000 over the balance at December 31, 2007. This increase resulted from net income of $19,006,000, proceeds from the exercise of stock options of $24,000, $697,000 related to the conversion of subordinated debentures, a decrease in other