

**OFFICE OF THRIFT SUPERVISION**

**WASHINGTON, D.C. 20552**

**FORM 10-K**

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

For the Fiscal Year Ended July 31, 2004

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

For transition period from \_\_\_\_\_ to \_\_\_\_\_

Docket Number 8173

**THE WASHINGTON SAVINGS BANK, F.S.B.**

(Exact name of registrant as specified in its charter)

U.S.

52-1271169

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification Number)

4201 Mitchellville Road, Suite 200, Bowie, Maryland

20716

(Address of principal executive offices)

(Zip code)

Registrant's telephone number, including area code: (301) 352-3120

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 \$1.00 per share

American Stock Exchange

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

None

(Title of class)

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



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 an accelerated filer (as defined in Exchange Act Rule 12b-2).

Yes



No



The aggregate market value of the voting stock held by non-affiliates of the registrant was \$37,681,326 as of January 31, 2004.

Number of shares of Common Stock outstanding on October 8, 2004, was 7,349,919.

Documents Incorporated by Reference:

Part III - Proxy Statement for 2004 Annual Meeting of Stockholders



## Form 10-K Cross-Reference Sheet

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\* Certain disclosures are incorporated by reference from registrant's definitive Proxy Statement for the Annual Meeting of Stockholders to be held November 18, 2004, which Proxy Statement will be filed not later than 120 days after the end of the fiscal year covered by this Annual Report on Form 10-K.

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## PART I

### Item 1. Business

The Washington Savings Bank, F.S.B. ("WSB") is a federally chartered, federally insured stock savings bank which was organized in 1982 as a Maryland-chartered, privately insured savings and loan association. It received federal insurance in 1985 and a federal savings bank charter in 1986. WSB is a member of the Federal Home Loan Bank ("FHLB") system and its deposits are insured by the Federal Deposit Insurance Corporation ("FDIC") to the maximum amount provided by law. WSB is subject to supervision and regulation by the Office of Thrift Supervision ("OTS").

WSB has five savings branches in Maryland. They are located in Bowie, Waldorf, Crofton, Millersville and Odenton, all of which are adjacent to the Baltimore-Washington corridor. WSB also has eleven mortgage loan origination offices, with four Virginia offices, one Pennsylvania office and six Maryland offices. Three of the Maryland mortgage loan offices are located adjacent to the Bowie, Waldorf and Odenton branches. The other three Maryland offices are located in Rockville, Bethesda and Annapolis. The Virginia offices are located in Woodbridge, Richmond, Oakton and Fredericksburg and the Pennsylvania office is located in Mechanicsburg.

WSB is engaged primarily in the business of attracting deposit accounts from the general public and using such funds, together with other borrowed funds, to make first and second mortgage loans, land acquisition and development loans, construction loans, consumer loans, and non-residential mortgage loans, with an emphasis on residential lending.

#### Lending Activities

General. Lending by WSB has historically focused on residential mortgage loans and construction loans on residential projects. The following table sets forth information concerning WSB's gross loan portfolio at the dates indicated:

	July 31,									
	2004		2003		2002		2001		2000	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
(dollars in thousands)										
Held for Sale:										
Single-family	\$14,697	3.03%	\$97,902	24.77%	\$14,909	7.31%	\$11,488	7.34%	\$3,941	2.79%
Held for Investment:										
Permanent mortgage loans:										
Single-family(1)	170,719	35.26%	121,336	30.69%	113,736	55.82%	83,682	53.52%	77,991	55.18%
Non-residential	15,964	3.30%	6,637	1.68%	8,671	4.26%	7,923	5.07%	7,590	5.37%
Land	44,478	9.19%	23,291	5.89%	15,210	7.47%	13,768	8.81%	10,622	7.52%
Construction loans:										
Single-family	225,803	46.63%	141,829	35.88%	45,590	22.38%	34,296	21.93%	35,972	25.45%
Other property	9,000	1.86%	2,203	0.56%	1,535	0.75%	3,857	2.47%	3,749	2.65%
Other:										
Consumer installment loans	391	0.08%	442	0.11%	335	0.16%	609	0.39%	541	0.38%
Account loans	236	0.05%	250	0.06%	383	0.19%	178	0.11%	291	0.21%
Commercial loans	<u>2,933</u>	<u>0.60%</u>	<u>1,416</u>	<u>0.36%</u>	<u>3,380</u>	<u>1.66%</u>	<u>560</u>	<u>0.36%</u>	<u>632</u>	<u>0.45%</u>
	469,524	96.97%	297,404	75.23%	188,840	92.69%	144,873	92.66%	137,388	97.21%
Total loans receivable	<u>\$484,221</u>	<u>100.00%</u>	<u>\$395,306</u>	<u>100.00%</u>	<u>\$203,749</u>	<u>100.00%</u>	<u>\$156,361</u>	<u>100.00%</u>	<u>\$141,329</u>	<u>100.00%</u>

(1) Includes \$5.0 million, \$2.8 million, \$2.4 million, \$1.3 million and \$.5 million of second mortgage loans, at July 31, 2004, 2003, 2002, 2001 and 2000, respectively.

Contractual Maturities. The following table reflects the approximate schedule of contractual principal repayments of the held-for-investment loan portfolio at July 31, 2004. With respect to adjustable rate loans, the following table reflects the approximate schedule of contractual maturities:

Approximate Principal Repayments Contractually Due in Years Ending July 31,	Real Estate Mortgage Loans		Real Estate Construction Loans		Consumer Installment and Account Loans	Commercial Loans	Total
	Fixed Rate	Adjustable Rate	Fixed Rate	Adjustable Rate			
(dollars in thousands)							
2005.....	\$ 18,307	\$ --	\$ 222,399	\$ --	\$ 249	\$ 1,000	\$ 241,955
2006.....	31,604	--	11,048	--	22	532	43,206
2007.....	4,884	--	1,356	--	74	--	6,314
2008 to 2009.....	38,687	--	--	--	162	1,174	40,023
2010 to 2014.....	20,362	45	--	--	14	--	20,421
2015 to 2019.....	6,291	--	--	--	--	--	6,291
2020 and thereafter.....	109,220	1,761	--	--	106	227	111,314
Total.....	<u>\$ 229,355</u>	<u>\$ 1,806</u>	<u>\$ 234,803</u>	<u>\$ --</u>	<u>\$ 627</u>	<u>\$ 2,933</u>	<u>\$ 469,524</u>

Prepayment Experience. Contractual principal repayment terms do not necessarily reflect the actual repayment experience within the loan portfolio. The average lives of mortgage loans are expected to be substantially less than their contractual terms due to loan prepayments and refinancings. The following table presents estimated maturities of WSB's loan portfolio based upon WSB's historic prepayment experience and prepayment experience statistics as provided by the OTS. With respect to adjustable rate loans, the following table reflects the approximate schedule of contractual maturities:

Estimated Prepayments in Years Ending July 31,	Mortgage Loans		Construction		Consumer Installment and Account Loans	Commercial Loans	Total
	Fixed Rate	Adjustable Rate	Fixed Rate	Adjustable Rate			
(dollars in thousands)							
2005.....	\$ 46,232	\$ --	\$ 211,323	\$ --	\$ 249	\$ 1,000	\$ 258,804
2006.....	31,206	--	23,480	--	22	532	55,240
2007.....	38,142	--	--	--	74	--	38,216
2008 to 2009.....	46,232	--	--	--	162	1,174	47,568
2010 to 2014.....	23,071	45	--	--	14	--	23,130
2015 to 2019.....	23,116	--	--	--	--	--	23,116
2020 and thereafter.....	21,356	1,761	--	--	106	227	23,450
Total.....	<u>\$ 229,355</u>	<u>\$ 1,806</u>	<u>\$ 234,803</u>	<u>\$ --</u>	<u>\$ 627</u>	<u>\$ 2,933</u>	<u>\$ 469,524</u>

Origination, Purchase and Sale of Loans. As a federal savings bank, WSB has authority to originate and purchase loans secured by real estate located throughout the United States. Generally, WSB makes loans in and around its market area, which primarily is the Baltimore-Washington corridor, Virginia and Southeast Pennsylvania. Historically, however, WSB has not engaged in the purchasing of loans.

In addition to accepting loan requests from its customer base, WSB employs thirty-five loan originators and compensates these individuals primarily on an incentive basis. The loan originators and other members of WSB's management maintain contacts with local builders, developers and realtors, which provide WSB with additional potential customers. WSB also enhances its business contacts within the communities it serves by participating in local civic organizations.

WSB originates residential loans for its portfolio and for sale in the secondary market. WSB's general practice has been to sell loans on an individual basis to various lenders throughout the country, without retaining loan servicing rights (commonly referred to as "servicing released"). In general, higher coupon loans, such as second mortgages, construction loans, and construction/permanent loans, are held in WSB's portfolio, while conforming first mortgages are sold at or shortly after origination. WSB also utilizes available funds to retain certain higher-yielding fixed rate residential mortgage loans in its portfolio in order to improve interest income. During the past three fiscal years, WSB has settled 9,840 loans with a principal value of approximately \$2.1 billion. The proceeds from loan sales are used to fund other loans held for investment, mortgage-backed securities ("MBS") and investment securities. WSB also has approval to sell loans to the Fannie Mae ("FNMA") and Freddie Mac ("FHLMC"), which enhances the ability of WSB to sell its mortgage loans and to convert pools of loans into marketable Ginnie Mae ("GNMA"), FNMA and FHLMC participation certificates. See "Business-Mortgage-Backed Securities."

Loan Underwriting Policies. Under WSB's loan approval policy, secured loans up to \$350,000 may be approved by WSB's Assistant Director of Lending and loans up to \$500,000 may be approved by WSB's Director of Lending. Loans up to \$750,000 may be approved by the Chairman of the Board, President or a Senior Vice President, individually. For Loans between \$500,001 and \$1,000,000 must be approved by any two of following: the Chairman of the Board, President, a Senior Vice President, or the Director of Lending. For loans between \$1,000,001 and \$2,000,000, three member of the WSB's Loan Committee must approve these loans. Loans over \$2,000,000 must be approved by the Board of Directors. All loans approved must comply with federal regulations. Generally, WSB will make residential mortgage loans in amounts up to the limits established from time to time by FNMA and FHLMC for secondary market resale purposes. This amount is presently \$333,700 for single-family, residential loans, although WSB will make loans in excess of this amount, if it believes it can sell the loans in the secondary market, or if it believes the loans should be held in its portfolio. However, loans for resale in the secondary market up to \$650,000 may be approved by any member of WSB's Loan Committee.

WSB obtains detailed loan applications to determine the borrowers' ability to repay and verifies the more significant items on these applications through credit reports, financial statements and confirmations. WSB also requires appraisals of collateral and title insurance. Most borrowers must establish a mortgage escrow account for items such as real estate taxes, governmental charges and hazard and private mortgage insurance premiums.

WSB's lending policy generally requires private mortgage insurance when the loan-to-value ratio exceeds 80%. WSB generally does not lend in excess of 90% of the appraised value of single-family residential dwellings even when private mortgage insurance is obtained, except for Federal Housing Administration ("FHA"), Veterans Administration ("VA")

and Farmers Home Administration (“FmHA”) loans, which permit higher loan-to-value ratios. Underwriting policies on other types of loans are described below.

Under federal law, the aggregate amount of loans that WSB may make to any one borrower and related entities is generally limited to 15% of WSB's unimpaired capital and unimpaired surplus. WSB's general lending limit at July 31, 2004 was approximately \$7.8 million. WSB has not made any loans aggregated in excess of this limit.

Single-Family Residential Real Estate Lending. At July 31, 2004, WSB had a total of \$486.4 million in loans and MBS. Loans secured by first or second mortgages on single-family properties consisted of \$185.4 million or 38.12% of total loans and MBS consisted of \$2.2 million, or \$0.44% of total loans.

WSB's single-family residential loans have historically provided for fixed interest rates at terms of up to 30 years. WSB originates conventional mortgage loans, FHA, VA, and loans in excess of the FNMA and FHLMC ceilings both for sale in the secondary market and for its own portfolio. Adjustable-rate mortgages are also offered, with rates adjusting to external indices in one to ten years. WSB has also made loans which fully amortize in 15 years and, on investment properties, loans which are due and payable in five years, subject to extension in some circumstances.

Non-Residential Real Estate Lending. WSB makes permanent mortgage loans on various non-residential properties, including office buildings and warehouses. Non-residential loans are made on properties located in or around WSB's market area. Non-residential real estate lending may entail significant additional risks as compared to single-family residential property lending. At July 31, 2004, non-residential real estate loans represented \$16.0 million, or 3.30%, lot loans and land loans represented \$44.5 million, or 9.19%, of WSB's total loans and MBS.

Acquisition, Development and Construction Lending. WSB provides construction loans for single-family and multi-family residences and for non-residential properties. These loans usually include funding for the acquisition and development of unimproved properties to be used for residential or non-residential construction. WSB may provide permanent financing on the same projects for which it has provided the construction financing.

Acquisition, development and construction lending, while providing higher yields, may also have greater risks of loss than long-term mortgage loans on improved, owner-occupied properties. At July 31, 2004, acquisition, development and construction loans represented \$234.8 million, or 48.49%, of WSB's total loans and MBS. WSB expects to continue construction lending at levels consistent with federal regulations. However, WSB expects to reduce the rate of the growth on its construction loan portfolio to comply with the Supervisory Agreement entered into with OTS. (See “MD&A- Regulatory Matters”).

WSB generally makes land acquisition loans with terms of up to three years and loan-to-value ratios of up to 80%, land development loans with terms of up to two years and loan-to-value ratios of up to 75%, and construction loans with terms of generally up to one year and loan-to-value ratios of up to 80%.

Commercial Lending. Federal laws and regulations permit thrift institutions to lend up to 20% of total assets in commercial loans on an unsecured basis or secured by collateral other than real estate, provided that amounts in excess of 10% of assets may be used only for small business loans. WSB does not actively promote these kinds of loans and at July 31, 2004, commercial loans represented \$2.9 million, or .60%, of WSB's total loans and MBS, which was significantly below the limit permitted by the regulations. In addition, WSB has issued a limited number of standby letters of credit, generally to development loan customers in connection with development work financed by WSB. Non-residential loans secured by real property are limited in the aggregate to 400% of WSB's capital unless the OTS specifically approves investment in a greater amount.

Consumer Lending. Federal laws and regulations permit a federally chartered thrift institution to make secured and unsecured consumer loans in an aggregate amount up to 35% of the institution's total assets. The 35% limitation does not include home equity loans (loans secured by the equity in the borrower's residence, but not necessarily for the purpose of improvement), home improvement loans or loans secured by deposits. WSB has not actively promoted these kinds of loans. Consumer loans, including loans secured by deposits, represented \$627,000, or .13% of WSB's total loans and MBS, at July 31, 2004.

Loan Fees and Service Charges. In addition to interest earned on loans, WSB receives income through servicing of loans and certain loan fees in connection with loan originations, loan modifications, loan commitments, late payments, changes of property ownership inspection fees and other services related to its loans. Income from these activities varies from period to period with the volume and types of loans made and repaid. WSB charges loan origination fees, which are calculated as a percentage of the amount loaned. The fees received in connection with the origination of construction and mortgage loans have generally been from one to four points (one point being equivalent to 1% of the principal amount of the loan) and are dependent upon market conditions and other factors. Loan origination fees, net of certain costs, are deferred and recognized as a yield adjustment over the lives of the loans utilizing the interest method.

Non-Performing Assets, Allowance for Loan Losses and Asset Classification. WSB categorizes its classified assets within four categories: Special Mention, Substandard, Doubtful and Loss. Special Mention loans have potential weaknesses that deserve management's attention. These loans are not adversely classified and do not expose an institution to sufficient risk to currently warrant adverse classification. Substandard loans are loans that have a well-defined weakness. They are characterized by the distinct possibility that WSB will sustain some loss if the deficiencies are not corrected. The Doubtful category consists of loans where WSB expects a loss, but not a total loss. Various subjective factors are considered with the most important consideration being the estimated underlying value of the collateral in determining the loss reserve for these loans. Loans that are classified as "Loss" are fully reserved on WSB's financial statements.

The allowance for loan losses is an estimate of the losses that may be sustained in our loan portfolio. The allowance is based on two principles of accounting: (a) Statement on Financial Accounting Standards ("SFAS") 5, "Accounting for Contingencies", which requires that losses be accrued when they are probable of occurring and are estimable and (b) SFAS No. 114, "Accounting by Creditors for Impairment of a Loan", which requires that losses be accrued when it is probable that the Company will not collect all principal and interest payments

according to the contractual terms of the loan. The loss, if any, is determined by the difference between the loan balance and the value of collateral, the present value of expected future cash flows, or values observable in the secondary markets.

All loans are individually evaluated if they are deemed classified. WSB also evaluates all delinquent loans, individually. The rest of the portfolio is evaluated as a group and a determination is made, periodically, concerning the inherent risks associated with particular types of loans and an allowance is assigned to those particular loan groups. WSB's management regularly reviews the loan portfolio and places loans on non-accrual status when, in the opinion of management, its collection of principal or interest is unlikely.

Federal regulations require WSB to classify loans and assets considered to be of lesser quality as substandard, doubtful or loss, according to criteria developed by the management of WSB. For the portion of assets classified as substandard or doubtful, WSB is required to establish prudent allowances for loan losses. For the portion of assets classified as loss, WSB is required to either establish specific allowances equal to 100% of the amount classified or charge-off such amount.

Real estate acquired at or in lieu of foreclosure is classified as real estate owned ("REO") until such time as it is sold. When the property is acquired, it is recorded at the lower of net carrying value or fair value, less estimated costs to sell subsequent to acquisition. Operating expenses of REO are reflected in non-interest expenses. Any write-down of the property at the acquisition date is charged against the allowance for loan losses with any subsequent additional write-downs reflected in non-interest expenses.

WSB also maintains allowances for loan losses based, in part, on historical loan loss experience and management's determination of risk factors in various portions of the loan portfolio. Additions to the allowance are made through periodic charges to income (provision for loan losses), and actual loan losses are charged against the allowance, while recoveries are added to the allowance. The following table sets forth information concerning the allocation of the allowance to each loan category. The allowance established for each category is not necessarily indicative of future losses or charge-offs for that category and does not restrict the use of the allowance to absorb losses in any category.

	2004		2003		2002		2001		2000	
	Allowance Amount	Percentage of loans in each category to Total loans	Allowance Amount	Percentage of loans in each category to Total loans	Allowance Amount	Percentage of loans in each category to Total loans	Allowance Amount	Percentage of loans in each category to Total loans	Allowance Amount	Percentage of loans in each category to Total loans
Single family	\$ 1,274	36.31%	\$ 911	40.79%	\$ 874	59.51%	\$ 684	57.80%	\$ 612	56.78%
Non-Residential	119	3.41%	50	2.23%	69	4.68%	65	5.47%	59	5.53%
Commercial	22	0.63%	11	0.48%	27	1.82%	5	0.38%	5	0.46%
Construction	1,752	48.06%	1,065	47.66%	361	24.58%	280	23.62%	282	26.17%
Land and Development	332	9.52%	192	7.86%	133	8.20%	144	9.51%	113	7.74%
Other	4	2.07%	5	0.98%	5	1.21%	6	3.21%	6	3.33%
Total	<u>\$ 3,503</u>	<u>100.00%</u>	<u>\$ 2,234</u>	<u>100.00%</u>	<u>\$ 1,469</u>	<u>100.00%</u>	<u>\$ 1,184</u>	<u>100.00%</u>	<u>\$ 1,077</u>	<u>100.00%</u>

## Mortgage-Backed Securities

In addition to short-term investments, when management believes favorable interest rate spreads are available, WSB also invests excess funds in MBS. GNMA participation certificates represent interests in pools of loans which are either insured by the FHA or guaranteed by the VA. FHLMC participation certificates are guaranteed by the FHLMC and FNMA participation certificates are guaranteed by the FNMA. The United States is not obligated to fund either FHLMC's obligations or FNMA's obligations. Nevertheless, WSB believes that the risk of credit loss on its MBS portfolio is limited.

The primary risk of holding these securities is the fluctuation of principal value corresponding to changes in interest rates. The following table sets forth the book value and estimated market value of the MBS portfolio at the dates indicated.

	<u>Years Ending July 31,</u>				
	<u>2004</u>	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>
	(dollars in thousands)				
Mortgage-backed securities:					
Amortized cost.....	\$2,114	\$819	\$40,063	\$56,262	\$69,177
Estimated fair value.....	\$2,155	\$842	\$40,549	\$56,898	\$66,918

Although MBS do not alter the overall maturity of WSB's assets as compared to holding a comparable portfolio of whole loans, they are more liquid than whole mortgage loans. MBS may also be used as collateral for short-term and long-term borrowings, which WSB may make from time to time. WSB does not generally employ hedging strategies in connection with its MBS portfolio.

The following table shows, as of July 31, 2004, the estimated principal repayment experience within the MBS portfolio, at amortized cost, net of discounts and premiums, as suggested by the OTS.

<u>Estimated Repayments in Years Ending July 31,</u>	(dollars in thousands)
2005.....	\$ 529
2006 to 2007.....	1,057
2008 to 2009.....	528
2010 to 2014.....	-
2015 to 2024.....	-
2025 and thereafter.....	-
Total.....	<u>\$ 2,114</u>

During fiscal year 2004, WSB had no sales compared to approximately \$32.9 million and \$138.2 million of its MBS available for sale for fiscal years 2003 and 2002, and experienced no pre-tax gains in fiscal 2004 compared to \$879,700 and \$1,424,400 in fiscal years 2003 and 2002, or approximately \$0, \$581,000 and \$940,000 after tax, in fiscal years 2004, 2003 and 2002, respectively.

## Other Investment Activities

In addition to investment in MBS, excess short-term funds have generally been invested in federal funds, agency callable paper, zero coupon bonds and preferred trust coupon bonds. WSB's portfolio of investment securities provides a source of liquidity when loan demand exceeds funding capability, provides funding for unexpected savings and certificate of deposit ("CD") withdrawals, provides funds for CD maturities, serves as a vehicle for interest-rate risk management, and provides a source of income. WSB is required to maintain certain liquidity ratios and generally does so by investing in securities that qualify as liquid assets under federal regulations. WSB is also required to hold FHLB stock in specified amounts and to maintain certain reserves with the Federal Reserve Bank of Richmond. See "Business-Supervision and Regulation."

The following table sets forth certain information regarding WSB's investment securities (excluding MBS), at amortized cost and other interest-earning assets for the periods indicated. WSB had no investments to a single issuer that exceeded 10% of stockholders' equity.

	July 31,		
	2004	2003	2002
	(dollars in thousands)		
Federal Home Loan Bank stock.....	\$ 4,495	\$ 4,095	\$ 2,995
Other Investments:			
Zero Coupon Bond.....	1,539	2,317	5,025
FHLB and FNMA Callable Paper.....	-	-	10,140
Preferred Trust Coupon Bonds.....	4,049	4,052	4,063
Total Other Investments.....	<u>\$ 5,588</u>	<u>\$ 6,369</u>	<u>\$ 19,228</u>

The following table sets forth WSB's scheduled maturities on other investments:

### **Investment Scheduled Maturity Table as of July 31, 2004**

	Up to One Year		One to Five Years		Five to Ten years		More than Ten Years		Total Investment Securities	
	Carrying Value	Average Yield	Carrying Value	Average Yield	Carrying Value	Average Yield	Carrying Value	Average Yield	Carrying Value	Average Yield
FHLB Stock	\$ -	-	\$ -	-	\$ -	-	\$ 4,495	3.50%	\$ 4,495	3.50%
Other Investments:										
Held to Maturity										
Zero Coupon Bond	\$ -	-	\$ -	-	\$ -	-	\$ 1,539	7.67%	\$ 1,539	7.67%
Preferred Trust Coupon Bond	-	-	-	-	-	-	4,049	9.59%	4,049	9.59%
Total Other Investments	<u>\$ -</u>	-	<u>\$ -</u>	-	<u>\$ -</u>	-	<u>\$ 5,588</u>	9.06%	<u>\$ 5,588</u>	9.06%

## Sources of Funds

General. Deposits are the primary source of WSB's funds for use in lending and for other general business purposes. In addition to deposits, WSB obtains funds from loan amortizations and prepayments and sales of loans, MBS and investment securities. WSB also has access to short- and long-term borrowings from commercial banks and, in the form of advances, from the FHLB of Atlanta. Loan repayments are a relatively stable source of funds, while deposit inflows and outflows are significantly influenced by general market interest rates and economic conditions. Borrowings may be used to compensate for seasonal or other reductions in normal sources of funds or for deposit inflows at less than projected levels. At July 31, 2004, WSB had borrowings of \$89.9 million in the form of advances from the FHLB of Atlanta.

Deposits. The mix of WSB's deposits reflects WSB's emphasis on longer-term CDs. WSB advertises for CDs from time to time generally when it has the need for deposits of specific maturities. Significant balances in CDs are generated from WSB customers who use its branches and from depositors around the country who follow WSB's pricing policies in various newsletters which are neither initiated by nor paid for by WSB. WSB has received deposits through brokers on an occasional basis in a manner consistent with federal regulations. The cost of these deposits are similar to WSB's posted rates or less than the borrowed fund rates for similar terms.

During fiscal year 2004, WSB offered slightly higher interest rates than the general market, which increased total deposits to \$378 million, a 29.7% increase in total deposits as of July 31, 2004, as compared to July 31, 2003.

The following table shows the distribution of WSB's deposits by type of deposit, including accrued interest, for the periods indicated.

	July 31,					
	2004		2003		2002	
	<u>Amount</u>	<u>Percent</u>	<u>Amount</u>	<u>Percent</u>	<u>Amount</u>	<u>Percent</u>
	(dollars in thousands)					
Savings accounts	\$ 66,953	17.70%	\$ 60,491	20.75%	\$ 45,664	21.85%
NOW accounts -- interest bearing	18,850	4.98	16,432	5.63	16,767	8.02
Checking accounts -- non-interest bearing	10,346	2.74	7,007	2.40	6,229	2.98
Time deposits	<u>282,136</u>	<u>74.58</u>	<u>207,697</u>	<u>71.22</u>	<u>140,349</u>	<u>67.15</u>
Total deposits at end of period	<u>\$ 378,285</u>	<u>100.00%</u>	<u>\$ 291,627</u>	<u>100.00%</u>	<u>\$ 209,009</u>	<u>100.00%</u>

The following table presents average balances and average interest rates, including accrued interest, of WSB's total deposits, for the periods indicated.

	July 31,					
	2004		2003		2002	
	Average Amount	Average Rate	Average Amount	Average Rate	Average Amount	Average Rate
	(dollars in thousands)					
Savings accounts	\$ 65,120	1.20%	\$ 51,358	1.19%	\$ 44,033	2.04%
NOW accounts- interest bearing	\$ 18,137	0.20%	\$ 16,935	0.20%	\$ 15,556	0.73%
Checking accounts- non-interest bearing	\$ 9,104	- %	\$ 7,452	- %	\$ 6,533	- %
Time deposits	\$ 232,601	3.61%	\$ 156,839	4.03%	\$ 136,787	5.49%

The following table presents, by various interest-rate categories, the amounts of time deposit accounts, excluding accrued interest payable of \$500,344 at July 31, 2004, which will mature during the periods indicated.

Time Deposit Accounts by Interest Rate	Amounts at July 31, 2004 Maturing in Twelve Months Ending July 31,				
	July 31, 2004	2005	2006	2007	2008 and After
	(dollars in thousands)				
Balance \$100,000 or less					
6.00% or less	\$ 202,942	\$ 49,736	\$ 44,986	\$ 20,853	\$ 87,367
6.01% to 8.00%	36,852	31,070	5,651	-	131
Total	<u>\$ 239,794</u>	<u>\$ 80,806</u>	<u>\$ 50,637</u>	<u>\$ 20,853</u>	<u>\$ 87,498</u>
Balance greater than \$100,000					
6.00% or less	\$ 31,329	\$ 19,663	\$ 6,393	\$ 1,817	\$ 3,456
6.01% to 8.00%	10,512	8,789	1,619	-	104
Total	<u>\$ 41,841</u>	<u>\$ 28,452</u>	<u>\$ 8,012</u>	<u>\$ 1,817</u>	<u>\$ 3,560</u>
Grand Total	<u>\$ 281,635</u>	<u>\$ 109,258</u>	<u>\$ 58,649</u>	<u>\$ 22,670</u>	<u>\$ 91,058</u>

The following table contains information pertaining to approximately 203 certificates of deposit accounts held by WSB in excess of \$100,000 as of July 31, 2004.

<u>Time Remaining Until Maturity</u>	<u>Certificate of Deposits</u> (dollars in thousands)
Less than three months	\$ 4,228
3 months to 6 months	6,992
6 months to 12 months	17,231
Greater than 12 months	<u>13,390</u>
Total	<u>\$ 41,841</u>

Borrowings. At July 31, 2003, WSB had a total of \$96.3 million in borrowed funds, consisting of FHLB advances of \$81.9 million, a line of credit advance of \$10.0 million and reverse repurchase agreements of \$4.4 million. During fiscal year ending July 31, 2004, WSB repaid the \$10.0 million line of credit and the \$4.4 million reverse repurchase agreement and \$21.0 million daily rate credit. Also during fiscal 2004, \$10.0 million of WSB's adjusted rate FHLB advances matured and \$5.0 million of fixed rate FHLB was called. WSB replaced these advances with \$5.0 million in adjustable rate advances. During fiscal year ending July 31, 2004, one of WSB's \$5.0 million adjustable FHLB advance was converted to a fixed rate by FHLB.

At July 31, 2004, WSB had a total of \$39.0 million in FHLB daily rate credit advances bringing the balance to \$89.9 million in FHLB advances at July 31, 2004.

### Subsidiaries

#### WSB, Inc.

WSB established a wholly owned service corporation subsidiary, WSB, Inc., in 1985. WSB, Inc. purchases land to develop into single-family building lots that are offered for sale to third parties. The subsidiary also builds homes on certain lots on a contract basis. During fiscal 2002, WSB, Inc. sold 5 lots in Peachtree Hollow, in Charles County, Maryland, all of which included finished houses and completed a finished home on the Benedict Plantation lot also located in Charles County, Maryland. During fiscal 2003, WSB, Inc. bought and sold another lot in Benedict Plantation. During fiscal 2004, WSB, Inc. purchased one lot to construct a house. The lot is currently being developed and WSB, Inc. expects completion next fiscal year. See Note 5 of Notes to Consolidated Financial Statements.

#### WSB Investments, Inc.

During 2000, WSB established a wholly-owned operating subsidiary, WSB Investments, Inc., which was incorporated under the laws of the State of Delaware for the purpose of maintaining and managing a portfolio of investment securities. WSB's investment portfolio totaled \$5.6 million, \$6.3 million and \$52.1 million as of July 31, 2004, 2003 and 2002, respectively and pre-tax earnings of \$626 thousand, \$2.5 million and \$5.7 million for the fiscal years ended July 31, 2004, 2003 and 2002, respectively.

### Employees

WSB had 139 full-time and 34 part-time employees at July 31, 2004. WSB provides health and life insurance benefits and a profit sharing plan. WSB also offers a 401(K) plan that allows employee contributions only. None of the employees are represented by a collective bargaining union. WSB believes that it enjoys good relations with its employees.

### Available Information

Our internet address is [www.twsb.com](http://www.twsb.com). There we make available, free of charge, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to these reports as soon as practicable after we file them with or furnish them to the OTS. Our OTS reports can be accessed through our financial information section of our

website. The information found on our website is not a part of this or any other report we file or furnish to the OTS.

### Supervision and Regulation

As a thrift institution, WSB is subject to extensive regulation and periodic examination by the OTS and its deposits are insured by the FDIC through the FDIC's Savings Association Insurance Fund ("SAIF"). The lending activities and other investments of WSB must comply with various federal regulatory requirements and WSB must periodically file reports with the OTS describing its activities and financial condition. WSB is also subject to certain reserve requirements promulgated by the Board of Governors of the Federal Reserve System (the "Federal Reserve Board"). This supervision and regulation is intended primarily for the protection of depositors. Certain of these regulatory requirements are referred to below or appear elsewhere herein.

On March 19, 2004, the Board of Directors announced that WSB had agreed to enter into a Supervisory Agreement with the OTS. During the course of a routine review of WSB by the OTS bank regulatory authorities, examiners identified certain supervisory issues, primarily related to compliance. The Supervisory Agreement formalizes the current understandings of both WSB and the OTS of the actions that WSB and its Board of Directors must undertake to address the compliance issues. The Supervisory Agreement also covers issues related to WSB's lending policies and procedures, and addresses WSB's compliance with regulations concerning bank secrecy and real estate lending. WSB has adopted all of the policies and procedures required by the Supervisory Agreement and has submitted certain of the policies to the OTS for its approval. (For a more detailed discussion of the Supervisory Agreement, see Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.)

Federal Home Loan Bank System. WSB is a member of the FHLB of Atlanta, which is one of 12 regional Federal Home Loan Banks. The Federal Home Loan Banks provide a central credit facility primarily for member institutions. At July 31, 2004 and 2003, WSB had advances of \$89.9 million and \$81.9 million, respectively, from the FHLB of Atlanta. The FHLB borrowings are collateralized by a blanket collateral loan agreement under which WSB must maintain minimum eligible collateral for the outstanding advances. Under this agreement, the limit on WSB's FHLB borrowings was approximately \$118.9 million, at July 31, 2004.

As a member, WSB is required to acquire and hold shares of capital stock in the FHLB of Atlanta in an amount not less than 1% of the aggregate unpaid principal of its residential mortgage loans, home purchase contracts, and similar obligations at the beginning of each year, or 1/20th of its advances from the FHLB of Atlanta, whichever is greater. WSB was in compliance with this requirement with an investment in FHLB of Atlanta stock at July 31, 2004, of \$4.5 million.

Liquidity Requirements. The OTS requires thrifts to maintain sufficient liquidity to ensure its safe and sound operation. Liquid assets are defined to include cash, deposits maintained pursuant to Federal Reserve Board reserve requirements, time deposits in certain institutions and certain savings deposits, obligations of the United States and certain of its agencies and qualifying obligations of the states and political subdivisions thereof, highly rated corporate debt, mutual funds that are restricted by their investment policies to investing only in liquid

assets, certain mortgage loans and mortgage-related securities, bankers acceptances, and notes issued by SAIF and the Bank Insurance Fund ("BIF") to the order of a financial institution. As of the calendar quarter ending June 30, 2004, WSB's average daily balance of liquid assets was \$32.9 million, exceeding the \$14.5 million required. In addition to meeting the minimum liquidity requirement, each thrift institution must maintain sufficient liquidity to ensure its safe and sound operation.

Internal sources of operational liquidity used by WSB are cash, various short-term investments, MBS and loans classified available-for-sale. Additionally, WSB may borrow funds from commercial banks or from the FHLB of Atlanta or the Federal Reserve Bank "discount window" after exhausting FHLB sources. In prior fiscal years, WSB also has utilized short-term borrowings in the form of reverse repurchase agreements from a commercial bank to meet short-term liquidity needs.

Qualified Thrift Lender Test. If WSB qualifies as a domestic building and loan association under the Internal Revenue Code, or maintains an appropriate level of certain investments, called "Qualified Thrift Investments" ("QTIs"), it qualifies as a "Qualified Thrift Lender" ("QTL"). QTIs must represent 65% of portfolio assets during 9 out of every 12 months on a continuous basis. A thrift institution that fails to maintain its QTL status will be permitted to requalify once, and if it fails the QTL test a second time, it will become immediately subject to all penalties as if all time periods prior to incurring such penalties had expired. Failure by WSB to maintain its status as a QTL will result in the following restrictions on operations: (i) WSB would not be able to engage in any new activity or make any new investment, directly or indirectly, unless such activity or investment was permissible for both national banks and thrift institutions; (ii) the branching powers of WSB would be restricted to those of a national bank, and (iii) payment of dividends by WSB would be subject to the rules regarding payment of dividends by a national bank. Additional restrictions would apply three years after an institution ceased to be a QTL, including requirements to dispose of certain impermissible assets. At July 31, 2004, WSB's QTL ratio was 95.5%, which exceeded the requirement.

Capital Standards. WSB is subject to capital standards imposed by the OTS. These standards call for a minimum "leverage ratio" of core capital to adjusted total assets of 4%, a minimum ratio of tangible capital to adjusted total assets of 1.5%, and a minimum ratio of risk-based capital to risk-weighted assets of 8%. The regulations both define core capital or tangible capital as including common stock (including retained earnings), noncumulative perpetual preferred stock and related surplus, minority equity interests in consolidated subsidiaries, and certain non-withdrawable accounts, less intangible assets and certain investments in subsidiaries. Core capital also includes certain unamortized goodwill. In addition, an amount equal to the lesser of 90% of the fair market value, or 100% of remaining unamortized book value, of purchased credit card relationships and mortgage servicing rights (subject to certain restrictions) may be used in calculating core capital. At July 31, 2004, WSB's ratios exceeded all regulatory capital requirements. See "Management's Discussion and Analysis of Financial Condition and Results of Operations - Financial Condition and Liquidity" and Note 12 of Notes to Consolidated Financial Statements.

The OTS has issued guidelines regarding the management of interest rate risk. The OTS requires thrift institutions to establish and maintain Board of Directors' approved limits on ratios between the net present value of the institution's assets, liabilities and off-balance sheet contracts (referred to as net portfolio value or "NPV"), and the value of these assets and

liabilities under sudden interest rate shocks of plus or minus 100, 200 and 300 basis points. As part of WSB's regular examination and rating by OTS examiners, WSB's level of interest rate risk is evaluated based primarily upon the interest rate sensitivity of its NPV in the event of an interest rate shock of 200 basis points.

The OTS also requires management to assess the risks and returns associated with complex securities and financial derivatives. For significant transactions, management must assess the incremental effect of the proposed transaction on the interest rate risk profile of the institution, including the expected change in the institution's NPV as a result of parallel shifts of plus or minus 100, 200 and 300 basis points in the yield curve. Complex securities and financial derivative transactions may require analysis of an even wider range of scenarios. In general, complex securities or financial derivatives with high price sensitivity should only be used as part of transaction strategies that lower an institution's interest rate risk, as measured by the sensitivity of NPV to changes in interest rates.

The OTS regulations also give the OTS broad authority to establish minimum capital requirements for specific institutions at levels greater than the regulatory minimums discussed above upon a determination that an institution's capital is or may become inadequate in view of the circumstances. These circumstances may include an institution receiving special supervisory attention, experiencing losses, experiencing poor liquidity or cash flows, and facing other risks identified by the regulators. The OTS also has broad authority to issue capital directives requiring its institutions to achieve compliance or take a variety of other actions intended to achieve capital compliance, including reducing asset or liability growth and restricting payments of dividends.

OTS regulations generally require that subsidiaries of a thrift institution be separately capitalized and that investments in, and extensions of credit to, any subsidiary engaged in activities not permissible for a national bank be deducted from the computation of a thrift institution's capital. Certain subsidiaries are exempt if engaged in impermissible activities solely as an agent for its customers, if engaged solely in mortgage banking, or if the subsidiary is itself a depository institution that was acquired by a thrift institution prior to May 1, 1989.

Prompt Corrective Action. The federal banking agencies have established by regulation, for each capital measure, the levels at which an insured institution is well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized or critically undercapitalized. The federal banking agencies are required to take prompt corrective action with respect to insured institutions that fall below the adequately capitalized level. Any insured depository institution that falls below the adequately capitalized level must submit a capital restoration plan, with increasing scrutiny and more stringent restrictions being imposed as an institution's capital declines. As of July 31, 2004, WSB was deemed to be well-capitalized.

Deposit Insurance. The deposits of WSB are insured up to \$100,000 per insured depositor (as defined by law and regulation) by the FDIC and are backed by the full faith and credit of the United States Government. The deposits of WSB are currently insured under the SAIF.

The FDIC has implemented a risk-based deposit insurance assessment system. Under this system, the assessment rate for an insured depository institution depends on the assessment risk classification assigned to the institution by the FDIC which is determined by the institution's capital level and supervisory evaluations. Deposit insurance assessment rates currently are

within a range of \$0.00 to \$0.27 per \$100 of insured deposits. Under current FDIC assessment guidelines, WSB expects that it will not incur any FDIC deposit insurance assessments for the remainder of 2004. However, the deposit insurance assessments imposed by the FDIC are subject to change.

In addition, assessments may be required to be made on insured depository institutions in general in order to restore the deposit insurance fund to a minimum coverage level of insured deposits.

WSB is subject to assessments for the payments on the bonds issued in the late 1980's to recapitalize the former Federal Savings and Loan Insurance Corporation. The rates of assessment for the payments on the bonds for the calendar quarters beginning on July 1, 2004 and October 1, 2004 are, respectively, 1.48 and 1.46 basis points for SAIF-insured deposits.

The FDIC may terminate the deposit insurance of any insured, depository institution, including WSB, if it determines after a hearing that the institution has engaged or is engaging in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, order or any condition imposed by an agreement with the FDIC. It also may suspend deposit insurance temporarily during the hearing process for the permanent termination of insurance, if the institution has no tangible capital. If insurance of accounts is terminated, the accounts at the institution at the time of the termination, less subsequent withdrawals, shall continue to be insured for a period of six months to two years, as determined by the FDIC. WSB's management is not aware of any existing circumstances, which would result in termination of WSB's deposit insurance.

Legislation was enacted in 1996 which contemplates the merger of the SAIF, of which WSB is a member, with the BIF, which generally insures deposits in national and state-chartered banks. A condition to the combined insurance fund, however, is that the savings association charter be eliminated. Several proposals in this regard have been introduced in Congress over the years, but have not been enacted. If legislation is passed abolishing the federal thrift charter, WSB may be required to convert to a national bank regulated by the Office of the Comptroller of the Currency ("OCC"). Regulation by the OCC could subject WSB to additional limitations on the types of business activities in which it may engage. WSB is unable to predict whether such legislation will be enacted.

Restrictions on Capital Distributions. Thrift institutions are subject to limitations on their ability to make capital distributions such as dividends, stock redemptions or repurchases, cash-out mergers, and other transactions charged to the capital account of a thrift institution.

Generally, no application or notice to the OTS is required for WSB to pay dividends that do not exceed, when combined with all distributions made during the calendar year, an amount equal to its net income year-to-date plus retained net income for the preceding two years, provided that WSB remains well-capitalized after the distribution and is eligible for expedited treatment under the OTS regulations. For all other capital distributions, WSB must file an application or notice with the OTS.

Federal Reserve System. Pursuant to regulations of the Federal Reserve Board, a thrift institution must maintain non-interest-bearing reserves at the Federal Reserve Bank, calculated daily, equal to 3% on the first \$45.4 million of transaction accounts (less a \$6.6 million

exclusion), and 10% on any additional amount. These percentages are subject to adjustment by the Federal Reserve Board to a level between 8% and 14%. WSB has consistently met its reserve requirements.

Effective January 9, 2003, the Federal Reserve Board amended its rules governing the operation of its “discount window,” which provides credit to help depository institutions meet temporary liquidity needs. The Federal Reserve Board replaced its adjustment credit, extended at a below-market rate, with primary credit, extended for very short terms at 1% above the federal funds rate, as a backup facility for financial institutions that are in generally sound financial condition. This change is intended to reduce the need for Federal Reserve System review of discount window borrowings and make the discount window a more attractive alternative when money market liquidity sources tighten. A secondary credit program will be available for depository institutions that do not qualify for primary credit, at a higher interest rate level.

Community Reinvestment. In 1977, Congress enacted the Community Reinvestment Act to encourage depository institutions, including thrifts, to help meet the credit needs of their entire communities, including low- and moderate-income areas, consistent with safe and sound banking practices. In implementing the Act, federal banking agencies have subjected “small” depository institutions, those with less than \$250 million in assets as the end of either of the two previous years, to streamlined examinations and reduced data collection and regulatory reporting requirements, under the Community Reinvestment Act. Effective October 1, 2004, the OTS raised the asset threshold for thrifts to qualify for streamlined examinations to \$1 billion. As a result, WSB qualifies for streamlined Community Reinvestment Act examinations, based on its present asset size. Standard Community Reinvestment Act examinations evaluate depository institutions under lending, investment and community service tests. Streamlined examinations, however, focus on the lending activities of depository institutions, thereby requiring them to maintain and aggregate less data for examiners to review to assess performance under the Community Reinvestment Act.

Privacy Regulations. All financial institutions, including WSB, are required to establish policies and procedures to restrict the sharing of nonpublic customer data with nonaffiliated parties at the customer’s request and to protect customer data from unauthorized access. WSB has developed such policies and procedures for itself and its subsidiaries and believes it is in compliance with all applicable privacy laws and regulations.

Under Title III of the USA PATRIOT Act, all financial institutions, including WSB, are required to take certain measures to identify their customers, prevent money laundering, monitor customer transactions and report suspicious activity to U.S. law enforcement agencies. Financial institutions also are required to respond to requests for information from federal banking regulatory authorities and law enforcement agencies, and information-sharing among financial institutions is encouraged by an exemption for complying financial institutions from the privacy provisions of the Gramm-Leach-Bliley Act and other privacy laws and from certain antitrust laws. Financial institutions that hold correspondent accounts for foreign banks or provide private banking services to foreign individuals are required to take measures to avoid dealing with certain foreign individuals or entities, including foreign banks with profiles that raise money laundering concerns. Correspondent accounts with “shell banks,” defined as foreign banks with no physical presence in any country, are barred altogether. The Secretary of the Treasury has adopted regulations to implement several of these provisions. All financial

institutions also are required to establish internal anti-money laundering programs. The effectiveness of a financial institution in combating money laundering activities is a factor to be considered in any application submitted by the financial institution under the Bank Merger Act, which applies to WSB. WSB has in place a Bank Secrecy Act and USA PATRIOT Act compliance program, and it engages in very few transactions of any kind with foreign financial institutions or foreign persons.

### Federal and State Taxation

Federal Income Taxation. WSB is generally subject to federal income taxation in the same manner as a regular corporation. However, as a thrift institution, in computing taxable income, WSB is permitted to deduct from its gross income each year certain amounts relating to its reserve for bad debts. Thrift institutions that qualify as small banks may use the “experience method” to calculate the amount of their bad debt reserve deductions. Under this method, a bad debt deduction is generally allowed for the amount necessary to increase the accumulated bad debt reserve to a level determined on the basis of actual net charge-offs during the most recent six-year period. For recent taxable years, WSB has elected to use this method.

Thrifts are required to recapture any excess reserves accumulated after 1987, but the recapture of any excess reserves accumulated prior to 1988 is deferred until the occurrence of certain remote contingencies including (i) failure to qualify as a bank for federal income tax purposes and (ii) distributions to stockholders that are treated as made out of reserves accumulated prior to 1988. Thrift institutions are given six years to account for any excess reserves that need to be recaptured, beginning with the first taxable year beginning after December 31, 1995, and are permitted to delay the timing of this recapture for one or two years, subject to whether they meet certain residential loan test requirements. WSB is required under these provisions to recapture excess tax reserves arising after 1987. However, WSB does not anticipate that such recapture will have a material impact on its financial position or results of operations, as this liability has been reflected in WSB’s financial statements.

WSB is subject to an alternative minimum tax which is imposed to the extent it exceeds WSB's regular income tax for the year. The alternative minimum tax is imposed at the rate of 20% of a specially computed tax base ("alternative minimum taxable income"). Included in this base are a number of preference items and adjustments, including the following: (i) interest on certain tax-exempt bonds issued after August 7, 1986, and (ii) 75% of the amount by which its adjusted current earnings exceeds its alternative minimum taxable income (computed before applying this adjustment and certain net operating losses).

WSB’s Federal income tax returns were last audited by the Internal Revenue Service as of July 31, 1999.

### Maryland State Taxation.

WSB is taxed in the same manner as commercial banks and regular business corporations. It is subject to a tax of 7% of its Maryland modified income.

## Item 2. Properties

At July 31, 2004, WSB operated five savings branch locations in Bowie, Crofton, Millersville, Odenton, and Waldorf, Maryland. Space for three of its branches, Millersville, Odenton and Waldorf, are under long-term leases with third parties. WSB purchased and renovated an existing branch building in July 1995 for its Crofton location. During fiscal 1997, WSB opened its fifth branch and relocated its corporate, administrative, and accounting offices to WSB's new five-story building in Bowie. At July 31, 2004, all of the Bowie building's residual space was tenant occupied. WSB also operates eleven mortgage loan origination offices in Maryland, Virginia and Pennsylvania. Six offices are located in Maryland, of which three are located adjacent to the Bowie, Waldorf and Odenton branches. The other three Maryland loan offices are located in Bethesda, Rockville and Annapolis. The Virginia offices are located in Woodbridge, Richmond, Oakton and Fredericksburg and the Pennsylvania office is located in Mechanicsburg.

## Item 3. Legal Proceedings

In the ordinary course of business, WSB becomes a defendant in various judicial and administrative proceedings; however, in the opinion of management, there is no proceeding pending or threatened which, if adversely determined, would result in a material adverse effect on WSB's financial condition or results of operations. WSB knows of no material proceedings to which any director, officer or affiliate of WSB, any owner of record or beneficially of more than five percent of any class of voting securities of WSB or any associate of any such director, officer, affiliate of WSB or such security holder of WSB is a party adverse to or has a material interest adverse to WSB or its subsidiaries.

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

Not Applicable.

## PART II

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

WSB's Common Stock is traded on the American Stock Exchange under the symbol "WSB". The high and low closing sale prices of WSB's Common Stock for each quarterly period within the past two years as reported on the American Stock Exchange are listed below:

Fiscal Period	Price per Share				Cash Dividends	
	2004		2003		Paid per Share	
	High	Low	High	Low	2004	2003
1st Quarter	\$9.76	\$8.80	\$5.74	\$4.82	\$0.050	\$0.040
2nd Quarter	11.09	8.83	5.74	4.92	0.050	0.027 *
3rd Quarter	10.57	8.93	7.67	5.28	0.060	0.027
4th Quarter	10.48	8.90	10.60	7.49	0.060	0.040

\*In the 2<sup>nd</sup> quarter, effective December 2002, WSB began to pay cash dividends on a quarterly basis, prior to this date, WSB paid semi-annual cash dividends.

The above high and low closing prices and cash dividends per share reflect WSB's three-for-two stock split declared during fiscal 2003.

As of October 8, 2004, WSB had 330 record holders of its Common Stock.

Cash dividends are subject to determination and declaration by the Board of Directors, which takes into account WSB's financial condition, results of operations, tax considerations, industry standards, economic conditions, and other factors, including regulatory restrictions. WSB expects to continue to pay quarterly cash dividends in the future. However, the ability of WSB to continue to pay quarterly cash dividends will be dependent on earnings, financial condition and business of WSB, as well as other factors, such as regulatory requirements. For a discussion of the regulatory restrictions on the declaration and payment of dividends, see "Business—Supervision and Regulation—Restrictions on Capital Distributions."

#### Equity Compensation Plan Information

<u>Plan Category</u>	Number of securities to be issued upon exercise of outstanding <u>options, warrants and rights</u>	Weighted average exercise price of outstanding <u>options, warrants and rights</u>	Number of securities remaining available for future issuance under equity compensation plans (excluding <u>securities reflected in column (a)</u> )
	(a)	(b)	(c)
Equity compensation plans approved by security holders:			
Non-employee Director's Plan	45,000	\$ 4.68	-
1988 Plan	12,675	5.29	-
1997 Plan	336,000	2.99	6,000
1999 Plan	470,300	3.84	3,000
2001 Plan	<u>279,750</u>	<u>4.89</u>	<u>391,500</u>
	1,143,725	3.90	400,500
Equity compensation plans not approved by security holders:	<u>-</u>	<u>-</u>	<u>-</u>
Total	<u>1,143,725</u>	<u>\$ 3.90</u>	<u>400,500</u>

## **Item 6. Selected Financial Data**

### Selected Consolidated Financial and Other Data

The following tables set forth selected consolidated financial information for WSB. The selected financial condition and operations data have been extracted from WSB's consolidated financial statements for each of the years in the five-year period ended July 31, 2004. The selected financial data should be read in conjunction with, and are qualified in their entirety by, the consolidated financial statements and related notes of WSB contained elsewhere herein.

	<b>Years Ended July 31,</b>				
	<b>2004</b>	<b>2003</b>	<b>2002</b>	<b>2001</b>	<b>2000</b>
	(in thousands except per share and other data)				
<b>Selected Financial Condition Data:</b>					
Total loans receivable, net.....	\$ 480,718	\$ 393,070	\$ 202,279	\$ 155,177	\$ 140,252
Mortgage-backed securities .....	2,155	842	40,160	56,898	66,918
Other investments and other interest-earning assets(1).....	20,057	22,896	37,057	52,921	49,131
Total assets.....	521,480	433,032	292,890	277,533	270,525
Deposits.....	378,285	291,627	209,009	194,127	191,727
Borrowings.....	89,900	96,331	47,900	50,900	52,384
Total stockholders' equity.....	48,808	39,447	32,524	28,808	23,857

	<b>Years Ended July 31,</b>				
	<b>2004</b>	<b>2003</b>	<b>2002</b>	<b>2001</b>	<b>2000</b>
	(in thousands except per share and other data)				
<b>Selected Operations Data:</b>					
Total interest income.....	\$ 32,411	\$ 24,675	\$ 21,262	\$ 21,484	\$ 19,957
Total interest expense.....	12,049	11,224	12,026	13,508	13,737
Net interest income.....	20,362	13,451	9,236	7,976	6,220
Provision for loan losses.....	1,395	1,265	310	255	36
Net interest income after provision for loan losses.....	18,967	12,186	8,926	7,721	6,184
Loan related fees.....	2,105	2,001	160	180	152
Gain on sale of loans and mortgage- related securities.....	2,982	6,427	3,107	969	380
Other income.....	1,336	1,444	2,377	2,909	1,818
Total non-interest income.....	6,423	9,872	5,644	4,058	2,351
Total non-interest expenses.....	11,054	11,111	7,438	7,138	6,376
Earnings before income taxes.....	14,336	10,946	7,132	4,641	2,160
Provision for income taxes.....	5,448	3,409	2,567	1,311	757
Net earnings.....	\$ 8,888	\$ 7,537	\$ 4,565	\$ 3,330	\$ 1,402
<b>Earnings per common share:</b>					
Basic earnings per share (2).....	\$ 1.25	\$ 1.09	\$ 0.67	\$ 0.49	\$ 0.21
Diluted earnings per share (2).....	\$ 1.11	\$ 0.98	\$ 0.62	\$ 0.48	\$ 0.21

<b>Average shares outstanding:</b>					
Average shares outstanding (2).....	7,131	6,895	6,855	6,855	6,776
Average diluted shares outstanding (2)....	8,040	7,727	7,357	6,971	6,810

<b>Other Data:</b>					
Return on average assets.....	2.02%	2.20%	1.58%	1.21%	0.54%
Return on average equity.....	20.23%	21.15%	14.94%	12.52%	6.11%
Equity-to-assets ratio.....	9.36%	9.10%	11.10%	10.38%	8.80%
Dividend payout ratio.....	17.70%	12.30%	10.90%	13.47%	32.03%
Interest rate spread.....	4.03%	3.64%	2.94%	2.59%	2.12%
Number of savings branches at end of period.....	5	5	5	5	5
Number of mortgage origination offices at end of period.....	11	11	8	6	6

(1) Other investments and other interest-earning assets include federal funds sold, Federal Home Loan Bank stock, Federal Reserve Bank deposits, zero coupon bonds, FHLB and FNMA callable paper and Preferred Trust Coupon Bonds.

(2) Adjusted for three-for-two stock split effective April 23, 2003.

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

### General

WSB's results of operations are primarily determined by the difference between the interest income and fees earned on loans, investments and other interest-earning assets, and the interest expense paid on deposits, borrowings and other interest-bearing liabilities. The difference between the average yield earned on interest-earning assets and the average cost of interest-bearing liabilities is known as net interest-rate spread. The principal expense to WSB is the interest it pays on deposits. The difference between interest income on interest-earning assets and interest expense on interest-bearing liabilities is referred to as net interest income. Net interest income is significantly affected by general economic conditions and by policies of state and federal regulatory authorities and the monetary policies of the Federal Reserve Board. WSB's net income is also affected by the level of its other income, including loan related fees, deposit-based fees, rental income, operations of its service corporation subsidiary, gains on sales of REO, loans and investment securities as well as its operating and tax expenses.

Both basic and diluted earnings per share amounts are shown on the Consolidated Statements of Earnings. However, "basic earnings per share" is utilized in the report's narrative when per share amounts are listed, unless otherwise stated. The information provided for both basic and diluted earnings per share reflect the three-for-two stock split that was declared in fiscal 2003.

### Forward Looking Statements

This annual report on Form 10-K contains statements that are forward looking. Forward looking statements are identified by terminology such as "may", "will", "believe", "expect", "estimate", "anticipate", "continue", or similar expressions. These statements are based on current expectations and assumptions that are subject to risks and uncertainties. Actual results could differ materially because of these risks and uncertainties, including changes in interest rates, changes in the economy, restrictions on our business practices due to our supervisory agreement with the OTS, credit or other risks of lending and investment activity, competitive and regulatory factors, changes in accounting rules and policies and legal and regulatory proceedings.

### Critical Accounting Policies

WSB's financial statements are prepared in accordance with United States generally accepted accounting principles ("GAAP"). The preparation of such financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. The financial information contained within WSB's statements is, to a significant extent, financial information that is based on measures of the financial effects of transactions and events that have already occurred. A variety of factors could affect the ultimate value that is obtained either when earning income, recognizing an expense, recovering an asset or relieving a liability. Certain policies inherently have a greater reliance on the use of estimates, assumptions and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. WSB uses historical loss factors as one

factor in determining an inherent loss that may be present in WSB's loan portfolio. Actual losses could differ significantly from the historical factors that WSB uses. In addition, GAAP itself may change from one previously acceptable method to another method. Although the economics of WSB's transactions would be the same, the timing of events that would impact WSB's transactions could change.

Management views allowance for loan losses as a critical accounting policy. The allowance for loan losses is an estimate of the losses that may be sustained in WSB's loan portfolio. The allowance is based on two basic principles of accounting: (i) Statement of Financial Accounting Standards ("SFAS") No. 5 "Accounting for Contingencies", which requires that losses be accrued when they are probable of occurring and estimable and (ii) SFAS No. 114 "Accounting by Creditors for Impairment of a Loan", which requires that losses be accrued based on the difference between the value of collateral, present value of future cash flows or values that are observable in the secondary market and the loan balance.

WSB's allowance for loan losses has three basic components: the specific allowance, the formula allowance and the non-specific allowance. Each of these components is determined based upon estimates that can and do change when the actual events occur. The specific allowance is used to individually allocate an allowance for loans identified for impairment testing. Impairment testing includes consideration of the borrower's overall financial condition, resources and payment record, support available from financial guarantors and the fair market value of collateral. These factors are combined to estimate the probability and severity of inherent losses. When impairment is identified, then a specific reserve is established based on WSB's calculation of the loss embedded in the individual loan. Large groups of smaller balance, homogeneous loans are collectively evaluated for impairment. Accordingly, WSB does not separately identify individual consumer and residential loans for impairment. The formula allowance is used for estimating the loss on those loans internally classified as high risk exclusive of those identified for impairment testing. The loans meeting the criteria for special mention, substandard, doubtful and loss, as well as, impaired loans are segregated from performing loans within the portfolio. Internally classified loans are then grouped by loan type (commercial, commercial real estate, commercial construction, residential real estate, residential construction or installment). Each loan type is assigned an allowance factor based on management's estimate of the associated risk, complexity and size of the individual loans within the particular loan category. Classified loans are assigned a higher allowance factor than non-rated loans due to management's concerns regarding collectibility or management's knowledge of particular elements surrounding the borrower. Allowance factors grow with the worsening of the internal risk rating. The non-specific formula is used to estimate the loss of non-classified loans and loans identified for impairment testing for which no impairment was identified. These loans are also segregated by loan type and allowance factors are assigned by management based on delinquencies, loss history, trends in volume and terms of loans, effects of changes in lending policy, the experience and depth of management, national and local economic trends, concentrations of credit, quality of loan review system and the effect of external factors (i.e. competition and regulatory requirements). The factors assigned differ by loan type. The unallocated allowance captures losses whose impact on the portfolio have occurred but have yet to be recognized in either the formula allowance or the specific allowance.

Management has significant discretion in making the judgments inherent in the determination of the provision and allowance for loan losses, including in connection with the valuation of collateral, a borrower's prospects of repayment, and in establishing allowance factors on the formula allowance and nonspecific allowance components of the allowance. The establishment of allowance factors is a continuing exercise, based on management's continuing assessment of the global factors discussed above and their impact on the portfolio, and allowance factors may change from period to period, resulting in an increase or decrease in the amount of the provision or allowance, based upon the same volume and classification of loans. Changes in allowance factors will have a direct impact on the amount of the provision, and a corresponding effect on net earnings. Errors in management's perception and assessment of the global factors and their impact on the portfolio could result in the allowance not being adequate to cover losses in the portfolio, and may result in additional provisions or charge-offs. For additional information regarding the allowance for loan losses, refer to the discussion under the caption "Allowance for Loan and REO Losses" below.

### Results of Operations

General. Net earnings for the fiscal year ended July 31, 2004 were \$8,888,000, or \$1.25 per basic share, compared to \$7,537,000, or \$1.09 per basic share, for the fiscal year ended July 31, 2003, and \$4,565,000, or \$0.67 per basic share, for the fiscal year ended July 31, 2002.

WSB's net earnings for the fiscal year ending July 31, 2004, included no gains from the sale of mortgage-backed securities compared to pre-tax gains of \$879,700 and \$1,424,400 for fiscal years ending July 31, 2003 and 2002, respectively. These gains, net of taxes, were approximately \$581,000, or \$.08 per basic share, for fiscal 2003, compared to \$940,000, or \$0.13 per basic share, for fiscal 2002.

WSB's net earnings for fiscal 2003 was also positively affected by granting to the Maryland Environmental Trust, a deed of conservation easement on the real estate held for investment property with an appraised value of \$2,145,000 and a carrying value of \$506,000, which resulted in reducing income tax expense by approximately \$745,000. The positive net effect on net earnings was approximately \$239,000, or \$0.03 per basic share.

Before giving effect to the above-mentioned after tax securities gains and grant of conservation easement for fiscal 2003, net earnings would have been \$8,888,000, \$6,717,000 and \$3,625,000 for fiscal years ending July 31, 2004, 2003 and 2002, respectively.

The increase in net earnings for fiscal 2004, as compared to fiscal 2003, was primarily due to increases of \$6,912,000 in net interest income, which offset a \$3,449,000 decrease in non-interest income.

The \$6.9 million increase in net interest income for fiscal 2004 as compared to fiscal 2003, was primarily due to a higher volume of interest earning assets and a lower cost of funds on WSB's interest bearing liabilities, which resulted in an increased interest rate spread. Non-interest income, excluding the MBS gains, decreased \$2.6 million during fiscal 2004 primarily due to a decrease in gain on sale of loans. Non-interest expenses remained stable for fiscal year 2004, compared to fiscal year 2003.

The increase in net interest income for fiscal 2003 as compared to fiscal 2002, was primarily due to a higher volume of interest earning assets and a lower cost of funds on WSB's interest bearing liabilities, which resulted in an increased interest rate spread. Non-interest income, excluding the effects of gains resulting from the sale of MBS, increased \$4.8 million during fiscal 2003 primarily due to an increase in gain on sale of loans and loan related fees, which were the result of a higher volume of real estate settlements in fiscal 2003 compared to fiscal 2002. The increase in non-interest expenses was primarily due to an increase in salaries and benefits due to a greater loan volume and increased loan origination staff. During fiscal 2003, WSB opened three new mortgage origination offices, one located in Fairfax, Virginia, one in Fredericksburg, Virginia and the other in Annapolis, Maryland.

Another significant factor affecting earnings during the past three years has been in the gain on sale of loans. Gain on sale of loans was \$2,982,000 for the year ended July 31, 2004, compared to \$5,547,000 for 2003, a \$2,565,000 or 46% decrease. The decrease in realized gains for fiscal 2004 is primarily due to the decline in the amount of loans originated for sale in the secondary market due to the increase in mortgage interest rates. The increase on the gain on sale of loans for fiscal 2003 was \$3,864,000, or 230%, over the gain on sale of loans for fiscal 2002. The increase in realized gains for fiscal 2003 was primarily attributable to the decline in the interest rates, where historic lows in mortgage rates were experienced, resulting in extraordinary levels of mortgage refinancings. WSB has increased both its number of loan origination offices and the number of loan officers during the past three years in response to the level of mortgage refinancings. Because the mortgage banking activity is very sensitive to mortgage interest rates, there can be no assurance that these levels of gains will be achieved in future periods.

Regulatory Actions. During the third quarter of fiscal 2004, WSB entered into a supervisory agreement with the OTS that addressed a number of supervisory issues primarily related to compliance. Under the supervisory agreement, among other things, WSB must (i) comply with various federal laws and regulations related to bank secrecy and real estate lending, (ii) conduct annual compliance audits and (iii) review and revise certain loan policies and procedures. In addition to adopting a number of policies and procedures addressing these supervisory issues, we have submitted to the OTS a comprehensive three year business plan, which among other things, discusses the limitations for each type of loan activity, including our construction loan portfolio. If we fail to comply with the supervisory agreement, including compliance with the various policies and business plan required, we may be subject to additional enforcement action including the imposition of civil money penalties.

The principal effects of this Supervisory Agreement on WSB's loan portfolio is expected to be a reduction in the rate of growth of its construction loans and a change of the composition of the construction loan portfolio. The construction loan portfolio will also continue to be affected by general economic conditions and the demand in WSB's markets for new construction projects. For these and other factors, management of WSB does not expect its construction loan portfolio to grow at rates comparable to those in recent periods. If the construction loan portfolio's growth is limited by the effect of this policy or general economic conditions, WSB's net interest rate spread and net interest income may be adversely affected. Additionally, the OTS has not yet approved WSB's business plan. If the OTS requires modification to our business plan, our future results and business prospects could also be adversely affected.

Average Balances. The following table sets forth, for the periods indicated, information regarding: (i) the total dollar amounts of interest income from interest-earning assets and the resulting average yields; (ii) the total dollar amounts of interest expense on interest-bearing liabilities and the resulting average costs; (iii) net interest income; (iv) interest rate spread; (v) average interest-earning assets and the total yield earned on average interest-earning assets; (vi) average interest-bearing liabilities and the total percentage cost of average interest-bearing liabilities; and (vii) the ratio of total interest-earning assets to total interest-bearing liabilities. Average balances, yields, and costs are calculated on the basis of month-end averages (except deposits, which are on the basis of daily averages) for all periods through July 31, 2004.

Weighted average yields and costs at July 31, 2004 are also indicated. Non-accrual loans are included in total loan balances, lowering the effective yield for the loan portfolio in the aggregate.

	Year Ended July 31,								
	2004			2003			2002		
	Average <u>Balance</u>	<u>Interest</u>	Yield/ <u>Cost</u>	Average <u>Balance</u>	<u>Interest</u>	Yield/ <u>Cost</u>	Average <u>Balance</u>	<u>Interest</u>	Yield/ <u>Cost</u>
	(dollars in thousands)								
Interest-earning assets:									
Loans .....	\$407,332	\$31,554	7.75%	\$290,537	\$22,577	7.77%	\$167,734	\$14,375	8.57%
Mortgage-backed securities .....	2,092	122	5.83	17,717	928	5.24	75,962	4,900	6.45
Investment securities (excluding MBS) .....	9,705	624	6.44	14,445	1,024	7.09	24,957	1,803	7.22
Other interest-earning assets .....	<u>11,190</u>	<u>111</u>	<u>.99</u>	<u>11,424</u>	<u>146</u>	<u>1.28</u>	<u>8,838</u>	<u>184</u>	<u>2.09</u>
Total interest-earning assets (1) ..	<u>\$430,319</u>	<u>\$32,411</u>	<u>7.52%</u>	<u>\$334,123</u>	<u>\$24,675</u>	<u>7.39%</u>	<u>\$277,491</u>	<u>\$21,262</u>	<u>7.66%</u>
Interest-bearing liabilities:									
Deposits .....	320,331	9,360	2.92	228,211	8,363	3.66	201,959	9,146	4.53
Other borrowings .....	<u>67,572</u>	<u>2,689</u>	<u>3.98</u>	<u>74,482</u>	<u>2,862</u>	<u>3.84</u>	<u>52,409</u>	<u>2,880</u>	<u>5.50</u>
Total interest-bearing Liabilities (1) .....	<u>\$387,903</u>	<u>\$12,049</u>	<u>3.49%</u>	<u>\$302,693</u>	<u>\$11,225</u>	<u>3.75%</u>	<u>\$254,368</u>	<u>\$12,026</u>	<u>4.72%</u>
Net interest income/interest rate spread (2) .....		<u>\$20,362</u>	<u>4.03%</u>		<u>\$13,450</u>	<u>3.64%</u>		<u>\$9,236</u>	<u>2.94%</u>
Net yield on interest-earning assets (3) .....			<u>4.73%</u>			<u>4.03%</u>			<u>3.33%</u>
Ratio of interest-earning assets to interest-bearing liabilities .....			<u>110.93%</u>			<u>110.38%</u>			<u>109.09%</u>

- (1) This is a weighted average yield.
- (2) Interest-rate spread is the arithmetic difference between the average yield on interest-earning assets (expressed as a percentage) and the average cost of interest-bearing liabilities (expressed as a percentage).
- (3) Net yield on interest-earning assets is the ratio of net interest income to average interest-earning assets.

**Rate/Volume Analysis.** The following table shows, for the periods indicated, the changes in interest income and interest expense attributable to: (i) changes in volume (change in volume multiplied by prior period rate); and (ii) changes in rate (change in rate multiplied by current period volume).

	Year Ended July 31,					
	2004 v. 2003			2003 v. 2002		
	Increase (Decrease)			Increase (Decrease)		
	Due to <u>Volume</u>	Due to <u>Rate</u>	<u>Net</u>	Due to <u>Volume</u>	Due to <u>Rate</u>	<u>Net</u>
	(dollars in thousands)					
<b>Interest Income:</b>						
Loans(1).....	\$ 9,074	\$ (97)	\$ 8,977	\$ 10,524	\$ (2,322)	\$ 8,202
Mortgage-backed securities.....	(819)	13	(806)	(3,757)	(215)	(3,972)
Investment securities .....	(336)	(64)	(400)	(759)	(20)	(779)
Other interest-earning assets.....	<u>(3)</u>	<u>(32)</u>	<u>(35)</u>	<u>54</u>	<u>(92)</u>	<u>(38)</u>
Total interest income.....	<u>7,916</u>	<u>(180)</u>	<u>7,736</u>	<u>6,062</u>	<u>(2,649)</u>	<u>3,413</u>
<b>Interest Expense:</b>						
Deposits.....	3,372	(2,375)	997	1,189	(1,972)	(783)
Other borrowings.....	<u>(265)</u>	<u>92</u>	<u>(173)</u>	<u>1,214</u>	<u>(1,232)</u>	<u>(18)</u>
Total interest expense.....	<u>3,107</u>	<u>(2,283)</u>	<u>824</u>	<u>2,403</u>	<u>(3,204)</u>	<u>(801)</u>
Increase in net interest income.....	<u>\$ 4,809</u>	<u>\$ 2,103</u>	<u>\$ 6,912</u>	<u>\$ 3,659</u>	<u>\$ 555</u>	<u>\$ 4,214</u>

(1) Includes approximately \$1,802,000, \$1,305,000 and \$683,000 of loan fees earned for fiscal 2004, 2003 and 2002, respectively.

**Net Interest Income.** During fiscal 2004, net interest income increased \$6.9 million, or 51.38%, to \$20.4 million from \$13.4 million in fiscal 2003. This increase is primarily due to increases in the average volume of interest earnings assets. For the year ended July 31, 2004, the average balance of WSB's total interest-earning assets increased to \$430.3 million from \$334.1 million for the year ended July 31, 2003. The average balance increase in interest-earning assets was primarily due to an increase primarily in construction loans, which offset the decrease in MBS and investment securities. The average yield on WSB's interest-earning assets for the year ended July 31, 2004 increased to 7.52% from 7.39% for the year ended July 31, 2003. The increase in the average yield is the result of restructuring the balance sheet to include more higher yielding loans with emphasis on construction loans.

The average balance of interest-bearing liabilities increased to \$387.9 million for the year ended July 31, 2004 as compared to \$302.7 million for the year ended July 31, 2003, due to an increase in WSB's deposits. Much of this increase is due to increased time deposits. These funds were used primarily to fund WSB loan originations. As a result of lower interest rates on deposits and borrowings, the average cost of interest-bearing liabilities decreased to 3.49% in fiscal 2004 from 3.75% in fiscal 2003. At July 31, 2004, 2003 and 2002, WSB's time deposits were \$282.1 million, \$207.7 million and \$140.3 million, respectively, and the corresponding interest expense on these deposits was approximately \$8.5 million, \$7.5 million and \$8.0 million, respectively. This total at July 31, 2004, included 28 accounts totaling approximately \$102.2 million of deposits received through brokers. These funds were primarily used to fund loan originations. The interest rates on these brokered deposits are similar to WSB's posted rates or less than the borrowed fund rates for similar terms.

During fiscal 2003, net interest income increased \$4.2 million, or 45.63%, to \$13.4 million from \$9.2 million in fiscal 2002. The increase was primarily due to an increase in the average volume of interest earning assets. The average balance increase in interest earning assets was primarily due to an increase in construction loans, which offset the decrease in MBS and investment securities.

Allowance for Loan and REO Losses. WSB's loan portfolio is subject to varying degrees of credit risk. Credit risk is mitigated through portfolio diversification, limiting exposure to any single customer, or industry. WSB maintains an allowance for loan losses (the "allowance") to absorb losses inherent in the loan portfolio. The allowance is based on careful, continuous review and evaluation of the loan portfolio. The methodology for assessing the appropriateness of the allowance includes: (1) a formula allowance reflecting historical losses by credit category, (2) the specific allowance for risk rated credits on an individual or portfolio basis, and (3) a non-specific allowance which considers risk factors not evaluated by the other two components of the methodology. The amount of the allowance is reviewed monthly by the Loan Committee, and reviewed and approved monthly by the Board of Directors.

The allowance is increased by provisions for loan losses, which are charged to expense. Charge-offs of loan amounts determined by management to be uncollectible or impaired decrease the allowance, while recoveries of loans previously charged-off are added back to the allowance. WSB makes provisions for credit losses in amounts necessary to maintain the allowance at an appropriate level, as established by use of the allowance methodology.

Management believes that the allowance reflects its best estimate of the losses existing in the loan held-for-investment portfolio as of the balance sheet date. The loan-held for sale portfolio has already been committed to be purchased by investors and will be settled subsequent to year end. Analysis of WSB's history of sold loans indicates that no credit losses have been realized after the sale of loans. WSB's determination of the adequacy of the allowance requires significant judgment, and estimates of probable losses in the loan-held for investment portfolio can vary significantly from the amounts actually observed. Future additions to the allowance may be necessary based on changes in the credits comprising the portfolio and changes in the financial condition of borrowers, such as may result from changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the loan portfolio and the allowance. Such review may result in additional provisions based upon their judgments of information available at the time of each examination.

Management has developed a comprehensive review process to monitor the adequacy of the allowance for loan losses. The review process and guideline were developed utilizing guidance from federal banking regulatory agencies and relies on relevant observable data. The observable data considered in the determination of the allowance is modified if other more relevant data becomes available. The results of this review process support management's view as to the adequacy of the allowance as of the balance sheet date. Please refer to the discussion under the caption, "Critical Accounting Policies" for an overview of the underlying methodology management employs on a monthly basis to maintain the allowance.

Changes in estimation methods may take place based upon the status of the economy and the estimate of the value of the property securing loans and as a result, the allowance may increase or decrease. Future adjustments could substantially affect the amount of the allowance.

The provision for loan losses was \$1,395,000 in 2004 compared to \$1,265,000 in 2003. The increase in the provision was the result of several factors including a significant increase in the entire loan portfolio, greater concentration in construction lending, higher volume of unseasoned loans within the portfolio, greater reliance on loans from brokers and higher levels of non-performing assets and delinquencies. Offsetting some of these negative trends is the rising real estate market, both locally and nationally. Management, aware of the strong growth experienced by WSB and the problems which could develop in an unmonitored environment, is intent on maintaining a strong credit review system and risk rating process.

As of July 31, 2004, the allowance increased by \$1,269,000, or 56.8%, to \$3,503,300 from \$2,234,300 at July 31, 2003. Most of this change was attributable to higher volume of construction loans. The construction loan portfolio grew by 59% over the period to \$226.4 million from \$142.1 million. This increase is a result of a higher demand for lending for construction rehabilitation loans. During fiscal 2004, approximately \$164,000 was charged-off. Of this total, \$96,000 was construction loans, \$65,000 was mortgage residential loans and \$3,000 was consumer loans. The risks associated with construction lending are considered to be greater than traditional residential mortgage lending.

At July 31, 2003, the allowance increased by \$764,900, or 52.1%, to \$2,234,300 from \$1,469,400 at July 31, 2002. This increase was due to a higher volume of construction loans. The construction loan portfolio grew by 213% over the period to \$142.1 million from \$45.4 million. During fiscal 2003, WSB charged-off \$500,000 of which \$402,000 were three construction loans to the same borrower.

During fiscal 2004, WSB made no provisions for REO losses, compared to a \$16,000 provision and a \$40,000 provision for REO losses made for fiscal years 2003 and 2002, respectively. The value of REO property held due to foreclosures at July 31, 2004, 2003 and 2002, were \$690,000, \$487,000 and \$437,000, respectively, which was net of reserves for REO losses of \$0, \$40,000 and \$24,000. The REO properties consist of \$626,000 in residential construction loans and \$64,000 in residential single-family loans. Management is actively seeking buyers for these properties.

During fiscal 2003, WSB granted a deed of conservation easement on undeveloped property that had been previously classified as "Real-estate held for investment", to the Maryland Environmental Trust. At the time of the grant, the investment property had an appraised value of \$2.1 million. Prior to the granting of the easement, the property had a carrying balance of \$506,000.

The following table sets forth information as to non-accrual loans. WSB generally discontinues the accrual of interest on loans 90 days or more past due, or in the opinion of management, loans that the payment of principal or interest is unlikely, at which time all previously accrued but uncollected interest is deducted from income.

	At July 31,				
	2004	2003	2002	2001	2000
	(dollars in thousands)				
Loans accounted for on a non-accrual basis:					
Mortgage loans:					
Single family	\$ 1,586	\$ 1,412	\$ 727	\$ 408	\$ 514
Land	1	-	133	-	-
Construction	424	520	62	-	27
Non-mortgage loans:					
Consumer	-	21	-	-	-
Total non-accrual loans	<u>\$ 2,011</u>	<u>\$ 1,953</u>	<u>\$ 922</u>	<u>\$ 408</u>	<u>\$ 541</u>
Accruing loans which are contractually past due 90 days or more but with current payments:					
Mortgage loans:					
Single family	\$ -	\$ -	\$ -	\$ -	\$ -
Construction	1,592	-	-	-	-
Non-mortgage loans:					
Consumer	-	-	-	-	-
Total accruing loans greater than 90 days past due	<u>\$ 1,592</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Total non-performing loans	<u>\$ 3,603</u>	<u>\$ 1,953</u>	<u>\$ 922</u>	<u>\$ 408</u>	<u>\$ 541</u>
Foreclosed real estate	<u>690</u>	<u>487</u>	<u>437</u>	<u>475</u>	<u>491</u>
Total non-performing assets	<u>\$ 4,293</u>	<u>\$ 2,440</u>	<u>\$ 1,359</u>	<u>\$ 883</u>	<u>\$ 1,032</u>
Total non-accrual and accruing loans to total loans held-for-investment	<u>0.77%</u>	<u>0.66%</u>	<u>0.49%</u>	<u>0.28%</u>	<u>0.39%</u>
Allowance for loan losses to total non-performing loans (including loans contractually past due 90 days or more)	<u>0.97%</u>	<u>114.43%</u>	<u>159.44%</u>	<u>290.07%</u>	<u>199.13%</u>
Total non-accrual and accruing loans greater than 90 days past due to total assets	<u>0.69%</u>	<u>0.45%</u>	<u>0.31%</u>	<u>0.15%</u>	<u>0.20%</u>
Total non-performing assets to total assets	<u>0.82%</u>	<u>0.56%</u>	<u>0.46%</u>	<u>0.32%</u>	<u>0.38%</u>

Total non-accrual loans increased by 2.97% to \$2,011,000 at July 31, 2004, compared to \$1,953,000 at July 31, 2003. This slight increase is the result of the increase in the loan portfolio.

Total accruing loans greater than 90 days past due increased by \$1.6 million in fiscal 2004 and were comprised of construction loans that are not contractually current. Although these loans have current payments, the maturity dates have expired and a request for an extension needs to be formally filed on their current contract to extend the maturity date to make the loan current.

The following table sets forth information as to loans defined as delinquent (between 60 days and 90 days past due) on which WSB continued to accrue interest.

	At July 31,				
	2004	2003	2002	2001	2000
	(dollars in thousands)				
Loans past due (60 to 90 days):					
Mortgage loans:					
Single family	\$1,841	\$1,065	\$ 515	\$ 548	\$ 362
Land	27	115	143	125	27
Construction	3,678	387	187	456	-
Non-mortgage loans:					
Commercial	-	60	-	-	-
Consumer	-	-	10	1	-
Total past due loans	<u>\$5,546</u>	<u>\$1,627</u>	<u>\$ 855</u>	<u>\$ 1,130</u>	<u>\$ 389</u>

The construction loan portfolio increased by 59.3 % and the single-family mortgage loan portfolio increased by 40.6% for fiscal 2004 compared to fiscal 2003. The increased loan volume resulted in a significant increase in WSB's past due loans, primarily in construction loans. Of the \$3.7 million in past due construction loans, \$2.2 million, or 38.8%, are loans that have current payments but are administratively past due. The maturity dates on these loans have expired and a request for an extension needs to be formally filed on their current contract to extend the maturity date to make the loan current.

The following table set forth information as to the allowance for loan losses:

	Year Ended July 31,				
	2004	2003	2002	2001	2000
	(dollars in thousands)				
Average loans held for investment	<u>\$ 382,575</u>	<u>\$ 254,916</u>	<u>\$ 156,504</u>	<u>\$ 140,349</u>	<u>\$ 124,014</u>
Total gross loans outstanding- held for investment at year end	<u>\$ 469,524</u>	<u>\$ 297,404</u>	<u>\$ 188,840</u>	<u>\$ 144,873</u>	<u>\$ 137,388</u>
Allowance, beginning of year	\$ 2,234	\$ 1,469	\$ 1,184	\$ 1,077	\$ 1,119
Provision for loan losses	1,395	1,265	310	255	36
Charge-offs					
single family	(65)	(61)	(1)	(55)	(61)
construction	(96)	(402)	(42)	(80)	-
other	(3)	(44)	(7)	(16)	(19)
	(164)	(507)	(50)	(151)	(80)
Recoveries :					
single family	32	-	-	-	-
construction	-	-	25	-	-
other	6	7	-	3	2
Net charge-offs	(126)	(500)	(25)	(148)	(78)
Allowance, end of year	<u>\$ 3,503</u>	<u>\$ 2,234</u>	<u>\$ 1,469</u>	<u>\$ 1,184</u>	<u>\$ 1,077</u>
Allowance as a percentage of total gross loans-held for investment	0.75%	0.75%	0.78%	0.82%	0.78%
Net charge-offs as a percentage of average loans	0.03%	0.20%	0.01%	0.11%	0.06%

Non-Interest Income. Total non-interest income for the years ended July 31, 2004, 2003, and 2002 was \$6.4 million, \$9.9 million and \$5.6 million respectively. Prior to giving effect to sales of MBS during each of the respective periods, adjusted non-interest income was \$6.4 million, \$9.0 million and \$4.2 million for fiscal years 2004, 2003, and 2002, respectively.

Loan related fees currently being recognized in non-interest income are primarily late fees, document preparation fees, tax service fees and construction inspection fees. Gain on sale of loans includes servicing release fees and discount points earned on loans sold. Other income includes primarily fees from WSB's deposit-based operations.

The \$2.6 million, or 28.6%, decrease in adjusted non-interest income in fiscal 2004, compared to fiscal 2003, was primarily due to a decrease in the gain on sale of loans. Gain on sale of loans decreased \$2.6 million due to the current interest rate environment on mortgage loans, which resulted in a substantial decrease on gain on sale of loans sold in the secondary market due to a decrease in the volume of loans originated for sale during fiscal 2004 compared to fiscal 2003. WSB originated approximately 1,856 loans that were sold in the secondary market totaling \$351.8 million during fiscal 2004, compared to 2,839 loans totaling \$562.7 million during fiscal 2003.

The \$3.9 million increase in adjusted non-interest income in fiscal 2003 compared to fiscal 2002 was primarily due to increases in gain on sale of loans and loan related fees. Gain on sale of loans increased \$3.9 million due to a higher volume of loans originated for sale during fiscal 2003 as compared to fiscal 2002. WSB originated approximately 2,839 loans that were sold in the secondary market in fiscal 2003, compared to 1,018 loans in fiscal 2002.

Non-Interest Expenses. Non-interest expenses were \$11.0 million, \$11.1 million, and \$7.4 million for the years ended July 31, 2004, 2003, and 2002, respectively.

The \$57,000 decrease in non-interest expenses during fiscal 2004 as compared to fiscal 2003 was primarily due to decreases of \$78,000 in salaries and benefits and \$497,000 in donations offsetting the \$104,000 increase in occupancy expense and \$226,000 increase in other expenses, such as courier service, telephone, repairs and installation, and other operating expenses. Most of these fiscal 2004 increases related to costs associated with the openings of the new loan origination offices which were opened in the second half of fiscal 2003.

During the first quarter of fiscal 2003, WSB granted a deed of conservation easement on the real estate held for investment property with an appraised value of \$2.1 million and a carrying balance of \$506,000 to the Maryland Environmental Trust. The \$506,000 was included in donation expense in fiscal year 2003.

The \$3.7 million increase in non-interest expenses during fiscal 2003 as compared to fiscal 2002 was primarily due to increases of \$2.5 million in salaries and benefits, \$97,000 in occupancy expense, \$526,000 in donations and \$393,000 in other expenses, including increases in various items such as service contracts, courier services, telephone, and repairs and installations. Most of these fiscal 2003 increases related to costs associated with the increase in loan origination volume and the opening of new loan origination offices. The increase in donation is the result of the deed of conservation easement on the real estate held-for-investment property to the Maryland Environmental Trust for \$506,000.

Income Taxes. Although WSB has generally provided for income taxes at substantially equivalent statutory rates, the tax effects of certain operations have caused variances in WSB's overall effective tax rates from year to year. As a result, WSB's effective tax rates for fiscal 2004, 2003, and 2002 were 38.0%, 31.1%, and 36.0%, respectively. The reduction in the effective tax rate for 2003, compared to 2004 and 2002, was primarily the result of the deed of conservation easement granted to the Maryland Environmental Trust on the real estate held for investment.

Financial Condition and Liquidity.

General. WSB has generally sought to lengthen its deposit maturities and decrease the effect of short-term interest rate swings through its pricing of its CDs. WSB advertises its lower-cost NOW accounts and offers fee-free checking incentives, an overdraft protection program, a variable money market savings account priced to current interest rates and the advantages of customer access to ATM networks. See "Quantitative and Qualitative Disclosures About Market Risk—Asset and Liability Management."

Total assets were \$521.5 million at July 31, 2004 as compared to \$433.0 million at July 31, 2003. The \$88.5 million, or 20.42%, increase in assets during fiscal 2004 was principally attributable to an increase in loans receivable funded from a growth in deposits. Liabilities increased by \$79.1 million, or 20.09%, to \$472.7 million at July 31, 2004 as compared to \$393.6 million at July 31, 2003, as a result of an increase in WSB's total deposits.

Liquidity. WSB must meet requirements for liquid assets and for liquidity described in "Business—Supervision and Regulation—Liquidity Requirements." As of calendar quarter ending June 30, 2004, WSB's long-term average daily balance of liquid assets was \$32.9 million, exceeding the \$14.5 million balance required.

Contractual Obligations. The following table lists WSB's contractual obligations as of July 31, 2004. Off-balance sheet financial instruments include commitments to extend credit, standby letters of credit, long-term borrowings, time deposits, operating lease obligations and financial guarantees. See Footnote 14 in our notes to consolidated financial statements contained elsewhere in this report for a complete description of off-balance sheet financial instruments.

	Payments due by period (dollars in thousands)				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Commitments to extend credit	\$ 11,969	\$ 11,969	\$ -	\$ -	\$ -
Long-term debt	50,900	5,000	-	-	45,900
Stand by letters of credit	1,269	1,269	-	-	-
Lease commitments	1,133	-	353	738	42
Deposits	282,136	109,451	81,464	91,221	-
Service contracts	1,212	402	810	-	-
<b>Total</b>	<b>\$ 348,619</b>	<b>\$ 128,091</b>	<b>\$ 82,627</b>	<b>\$ 91,959</b>	<b>\$ 45,942</b>

Capital. Current statutory provisions and OTS regulations establish standards for capital, require subsidiaries of a federally-chartered thrift institution to be separately capitalized, and require investments in and extension of credit to any subsidiary engaged in activities not permissible for a national bank to be deducted in the computation of an institution's regulatory capital. These regulations have affected WSB and its service corporation subsidiary, which is engaged in real estate development and construction activities. Therefore, for regulatory capital calculations, WSB was required to deduct \$93,000 from its assets and the \$32,100 investment in its subsidiary from capital due to the subsidiary's real estate development and construction activities. In addition, WSB's regulatory capital reflects a decrease of \$27,500, while its regulatory assets reflect a decrease of \$41,600; both of which represent unrealized gains (after-tax for capital deductions and pre-tax for asset deductions, respectively) on MBS classified as available-for-sale. See "Business— Supervision and Regulation," "Business—Subsidiaries" and Note 12 of Notes to Consolidated Financial Statements. The minimum regulatory capital and ratios required, WSB's actual regulatory capital and ratios, and the amount by which WSB's ratios exceed the minimum regulatory requirements, as of July 31, 2004, are as follows:

<u>Capital Category</u>	<u>Regulatory Ratios Required</u>	<u>WSB's Ratios</u>	<u>WSB's Excess of Requirements</u>	<u>Calculations Based Upon</u>	
Leverage	\$20,853,803	\$48,748,698	\$27,894,895	\$ 48,748,698	Regulatory Capital
	4.00%	9.35%	5.35%	\$ 521,345,087	Regulatory Assets
Tangible	\$7,820,176	\$48,748,698	\$40,928,522	\$ 48,748,698	Regulatory Capital
	1.50%	9.35%	7.85%	\$ 521,345,087	Regulatory Assets
Risk-Based	\$34,936,383	\$52,252,027	\$17,315,644	\$ 52,252,027	Regulatory Capital
	8.00%	11.97%	3.97%	\$ 436,704,790	Risk-Weighted Assets

WSB's management believes that under current regulations, WSB will continue to meet its minimum capital requirements for the foreseeable future. However, events beyond the control of WSB, such as changes to market interest rates or a downturn in the economy in areas where WSB has most of its loans, could adversely affect future earnings and, consequently, the ability of WSB to meet its future minimum capital requirements.

WSB has paid cash dividends to stockholders since March 1993. Cash dividends are subject to determination and declaration by the Board of Directors, which takes into account WSB's financial condition, results of operations, tax considerations, industry standards, economic conditions, and other factors, including regulatory restrictions. Cash dividends are paid on a quarterly basis. For a discussion of the regulatory restrictions on the declaration and payment of dividends, see "Business—Supervision and Regulation—Restrictions on Capital Distributions."

#### Impact of Inflation and Changing Prices

The Consolidated Financial Statements of WSB and related notes presented elsewhere herein have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"), which require the measurement of financial position and

operating results in terms of historical dollars without considering changes in the relative purchasing power of money over time due to inflation.

Unlike those of many industries, most of the assets and liabilities of financial institutions such as WSB are monetary in nature. Monetary items, which are those assets and liabilities that are convertible into a fixed number of dollars regardless of changes in prices, include cash, investments, loans and other receivables, savings accounts, short-term and long-term debt and, in WSB's case, most of its other liabilities. Virtually all of WSB's assets and liabilities are monetary in nature. Inflation has had an immaterial effect on WSB's operations in the three most recent fiscal years.

## **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

### Market Risks

Management of WSB considers interest rate risk ("IRR") and credit risk as the two most significant factors impacting WSB's financial performance. WSB currently utilizes no derivatives to mitigate its credit risk, relying instead on loan review and an adequate loan loss reserve. WSB's exposure to IRR is reviewed on at least a quarterly basis by the Board of Directors and management, and is measured in accordance with OTS Thrift Bulletin No. 13a using interest rate sensitivity analysis, including NPV and net interest income under various interest rate scenarios.

The OTS provides all institutions that file the Consolidated Maturity Rate Schedule ("CMR") as part of their quarterly thrift financial reports with a quarterly interest rate sensitivity report of NPV. The NPV is defined as the present value ("PV") of expected cash flows from existing assets, less the PV of expected cash flows from existing liabilities, plus the PV from existing off-balance sheet contracts. In addition to the discounted cash flow analysis, the OTS simulator model also employs an option-based pricing approach to measuring the interest rate sensitivity of the NPV. Per the OTS interest rate risk exposure report, WSB's sensitivity measure, or decline in the NPV ratio, at June 30, 2004 was 59 basis points, compared to 26 basis points at June 30, 2003. The 33 basis point decline resulted primarily from the increase in the loan portfolio, particularly in the short-term construction loan portfolio. The construction loan portfolio growth is limited by the effect of the OTS agreement and this may have an impact on WSB's NPV ratio in the future. WSB relies on the OTS model and does not prepare its own model.

WSB management uses an internally-prepared net interest income model to measure the effect on net interest income of different interest rate scenarios applied to anticipated levels and mixes of assets and liabilities.

The following table compares the calculated estimates of change in NPV and net interest income as of June 30, 2004 to current limits established by management and approved by the Board of Directors. All changes are measured as percentage changes from the values of projected NPV and net interest income at current interest rates.

Percentage Change In

Basis Point Change In Market Rates	Net Interest Income		Net Portfolio Value as a % of PV of Assets	
	Board Limits	Projected Change	Minimum Board Limits	OTS Projected Change
+300	-40%	+26%	5%	14%
+200	-30%	+17%	6%	15%
+100	-20%	+ 8%	7%	15%
Current	0%	-	8%	15%
-100	-20%	- 8%	9%	14%
-200	-30%	-17%	10%	N/A
-300	-40%	-26%	11%	N/A

The models utilized to produce the table presented above employ numerous assumptions, including relative levels of market interest rates, asset prepayments and the decay rate of deposits. The actual affects of real interest rate changes may differ from the forecasted affects of hypothetical interest rate changes and should not be relied upon as indicative of actual future results. Further, the computations do not contemplate actions that management and the Board of Directors may undertake in response to changes in interest rates.

Asset and Liability Management

Management recognizes that WSB’s profitability is dependent to a large extent upon its net interest income, which in turn is dependent upon the achievement of a positive interest rate spread that can be sustained during fluctuations in prevailing interest rates. Interest rate sensitivity is a measure of the difference between amounts of interest-earning assets and interest-bearing liabilities which either reprice or mature within a given period of time. The difference, or the interest rate repricing “gap”, provides an indication of the extent to which an institution’s interest rate spread will be affected by changes in interest rates. A gap is considered positive when the amount of interest rate sensitive assets exceeds the amount of interest rate sensitive liabilities, and is considered negative when the amount of interest rate sensitive liabilities exceeds the amount of interest rate sensitive assets. Generally, during a period of rising interest rates, a negative gap would adversely affect net interest income, while a positive gap would result in an increase in net interest income. Conversely, during a period of falling interest rates, a negative gap would result in an increase in net interest income, while a positive gap would negatively affect net interest income.

The following table sets forth the amounts of WSB’s interest rate sensitive assets and liabilities at July 31, 2004 which are anticipated, based upon certain assumptions, to reprice or mature in each of the time periods shown:

**Maturing or Repricing in**

	<u>1 Year or Less</u>	<u>1-3 Years</u>	<u>3-5 Years</u>	<u>More than 5 Years</u>	<u>Total</u>
	(dollars in thousands)				
Total interest rate sensitive assets.....	\$289,268	\$ 97,925	\$ 48,007	\$ 69,702	\$504,902
Total interest rate sensitive liabilities .....	<u>145,581</u>	<u>118,643</u>	<u>122,990</u>	<u>81,858</u>	<u>469,072</u>
Positive (negative) gap .....	<u>\$143,687</u>	<u>\$(20,718)</u>	<u>\$(74,983)</u>	<u>\$(12,156)</u>	<u>\$ 35,830</u>
Ratio of positive (negative) gap to total assets .....	27.6%	(4.0)%	(14.4)%	2.3%	6.9%
Cumulative positive (negative) gap .....		\$122,969	\$ 47,986	\$ 35,830	
Ratio of cumulative positive (negative) gap to total assets .....		23.6%	9.2%	6.9%	

As indicated in the table above, WSB's balance sheet reflects a positive gap of \$143.7 million in the one year or less time period, and a negative gap of \$20.7 million in the one to three year time period, resulting in a cumulative positive gap of \$123.0 million for the combined interval of three years or less.

WSB has historically funded long term mortgage loans and MBS investments with long term CD's. Management of WSB believes that the effective maturity of its mortgage loan and MBS portfolios would be substantially less than the contractual maturities of the underlying loans, thus approximately matching the maturity intervals of both the interest rate sensitive assets and liabilities.

## Item 8. Financial Statements and Supplementary Data

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Audit Committee of the  
Board of Directors and Stockholders of  
The Washington Savings Bank, F.S.B.  
Bowie, Maryland

We have audited the accompanying consolidated statements of financial condition of The Washington Savings Bank, F.S.B. and Subsidiaries (the "Company") as of July 31, 2004 and 2003, and the related consolidated statements of earnings, stockholders' equity, and cash flows for the three years in the period ended July 31, 2004. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of July 31, 2004 and 2003, and the results of its operations and its cash flows for the three years in the period ended July 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

*Stegman & Company*

Baltimore, Maryland  
August 31, 2004

**THE WASHINGTON SAVINGS BANK, F.S.B., AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**  
**AS OF JULY 31, 2004 AND 2003**

	<u>2004</u>	<u>2003</u>
<b>ASSETS</b>		
CASH AND CASH EQUIVALENTS:		
Cash	\$ 3,004,533	\$ 2,050,330
Federal funds sold	9,974,000	12,397,000
Total cash and cash equivalents	<u>12,978,533</u>	<u>14,447,330</u>
LOANS RECEIVABLE - (Note 2):		
Held for investment	469,524,162	297,403,518
less: allowance for loan losses	(3,503,329)	(2,234,348)
Total - Held-for-investment	<u>466,020,833</u>	<u>295,169,170</u>
Held for sale	14,696,830	97,901,757
Total loans receivable - net	<u>480,717,663</u>	<u>393,070,927</u>
Mortgage-backed securities - available for sale at fair value (Note 3)	2,155,182	842,235
Investment Securities - held to maturity at amortized cost, (fair value of \$5,662,684 and \$6,223,778 at July 31, 2004 and 2003, respectively) (Note 4)	5,587,560	6,369,417
Investment in FHLB Stock, at cost	4,495,000	4,095,000
Accrued interest receivable on loans	2,963,284	1,979,540
Accrued interest receivable on investments and mortgage-backed securities	29,420	22,941
Real estate acquired in settlement of loans (Note 6)	689,971	486,526
Real estate held for investment	87,897	-
Premises and equipment - net (Note 7)	6,305,829	6,528,410
Deferred tax asset (Note 13)	3,616,006	2,514,638
Other assets	1,853,301	2,675,246
<b>TOTAL ASSETS</b>	<u>\$ 521,479,646</u>	<u>\$ 433,032,210</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
LIABILITIES:		
Deposits (Note 8):		
Noninterest bearing	\$ 10,345,534	\$ 7,007,195
Interest-bearing	367,939,410	284,619,912
Total Deposits	<u>378,284,944</u>	<u>291,627,107</u>
Other Borrowings (Note 9)	89,900,000	96,330,757
Advances from borrowers for taxes and insurance	1,412,564	1,471,235
Accounts payable, accrued expenses and other liabilities	3,073,837	2,946,440
Income taxes payable	-	1,209,496
Total Liabilities	<u>472,671,345</u>	<u>393,585,035</u>
COMMITMENTS AND CONTINGENCIES (Notes 11 and 14)		
STOCKHOLDERS' EQUITY (Note 12):		
Preferred stock, no stated par value; 10,000,000 shared authorized; none issued and outstanding		
Common stock, \$1 par value; 20,000,000 shares authorized; 7,956,850 and 7,567,650 shares issued *	7,956,850	7,567,650
Additional paid-in capital *	1,704,955	92,502
Treasury Stock; 610,681 and 641,595 shares at cost *	(645,124)	(677,781)
Retained earnings - substantially restricted	39,764,172	32,449,769
Accumulated other comprehensive income	27,448	15,035
Total stockholders' equity	<u>48,808,301</u>	<u>39,447,175</u>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<u>\$ 521,479,646</u>	<u>\$ 433,032,210</u>

\* Includes adjustment for the three-for-two stock split, effective April 23, 2003  
See notes to consolidated financial statements.

**THE WASHINGTON SAVINGS BANK, F.S.B. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF EARNINGS**  
**FOR THE YEARS ENDED JULY 31, 2004, 2003 AND 2002**

	<u>2004</u>	<u>2003</u>	<u>2002</u>
<b>INTEREST INCOME:</b>			
Interest and fees on loans	\$ 31,554,005	\$ 22,576,677	\$ 14,374,670
Interest on mortgage-backed securities	121,912	928,384	4,900,412
Interest and dividends on investments	735,217	1,169,867	1,987,238
Total interest income	<u>32,411,134</u>	<u>24,674,928</u>	<u>21,262,320</u>
<b>INTEREST EXPENSE:</b>			
Interest on deposits	9,360,125	8,362,564	9,145,638
Interest on other borrowings	2,688,782	2,861,700	2,880,363
Total interest expense	<u>12,048,907</u>	<u>11,224,264</u>	<u>12,026,001</u>
<b>NET INTEREST INCOME</b>	20,362,227	13,450,664	9,236,319
Provision for loan losses	<u>1,395,000</u>	<u>1,265,000</u>	<u>310,000</u>
<b>NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES</b>	<u>18,967,227</u>	<u>12,185,664</u>	<u>8,926,319</u>
<b>NON-INTEREST INCOME:</b>			
Loan-related fees	2,104,752	2,000,980	929,425
Gain on sale of loans	2,981,869	5,546,912	1,682,559
Gain on sale of mortgage-backed securities - available-for-sale	-	879,691	1,424,414
Rental Income	778,507	755,979	729,547
Gain on sale of real estate acquired in settlement of loans	115,814	109,381	59,582
Service charges on deposits	172,177	192,567	210,814
Net gain on sale of building lots and homes	-	62,076	225,777
Other income	269,559	323,849	382,267
Total non-interest income	<u>6,422,678</u>	<u>9,871,435</u>	<u>5,644,385</u>
<b>NON-INTEREST EXPENSES:</b>			
Salaries and benefits	6,328,446	6,406,282	3,877,513
Occupancy expense	738,550	634,395	537,495
Deposit insurance premiums	130,808	109,300	103,559
Depreciation	578,800	559,384	577,121
Advertising	110,756	96,054	81,279
Service bureau charges	425,689	399,631	346,254
Service charges from banks	144,332	120,492	121,310
Stationery, printing & supplies	253,875	250,463	181,420
Donations	41,683	538,975	13,298
Other taxes	139,763	108,467	120,388
Provisions for losses on real estate acquired in settlement of loans	7,450	16,059	-
Other expenses	2,154,061	1,871,760	1,478,964
Total non-interest expenses	<u>11,054,213</u>	<u>11,111,262</u>	<u>7,438,601</u>
<b>EARNINGS BEFORE PROVISION FOR INCOME TAXES</b>	14,335,692	10,945,837	7,132,103
<b>PROVISION FOR INCOME TAXES (Note 13)</b>	<u>5,447,900</u>	<u>3,408,800</u>	<u>2,567,500</u>
<b>NET EARNINGS</b>	<u>\$ 8,887,792</u>	<u>\$ 7,537,037</u>	<u>\$ 4,564,603</u>
<b>BASIC EARNINGS PER COMMON SHARE*</b>	<u>\$1.25</u>	<u>\$1.09</u>	<u>\$0.67</u>
<b>DILUTED EARNINGS PER COMMON SHARE*</b>	<u>\$1.11</u>	<u>\$0.98</u>	<u>\$0.62</u>
<b>AVERAGE COMMON SHARES OUTSTANDING*</b>	<u>7,131,363</u>	<u>6,894,651</u>	<u>6,855,684</u>
<b>AVERAGE DILUTED COMMON SHARES*</b>	<u>8,040,246</u>	<u>7,726,909</u>	<u>7,357,260</u>

\*Includes adjustment for the three-for-two stock split, effective April 23, 2003.

See notes to consolidated financial statements.

**THE WASHINGTON SAVINGS BANK, F.S.B. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
**YEARS ENDED JULY 31, 2004, 2003 AND 2002**

	<u>Common Stock</u>	<u>Additional Paid-In Capital</u>	<u>Treasury Stock</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income(Loss)</u>	<u>Total Stockholders' Equity</u>
<b>BALANCES, JULY 31, 2001</b>	\$ 5,035,649	\$ 1,513,933	\$ (737,145)	\$ 22,587,931	\$ 407,278	\$ 28,807,646
Comprehensive Income:						
Net earnings	-	-	-	4,564,604	-	4,564,604
Net changes in unrealized depreciation on available for sale securities (net of reclassification adjustment)	-	-	-	-	(345,091)	(345,091)
Total comprehensive income						<u>4,219,513</u>
Cash dividend (0.073 per common share)	-	-	-	(502,750)	-	(502,750)
<b>BALANCES, JULY 31, 2002</b>	<u>\$ 5,035,649</u>	<u>\$ 1,513,933</u>	<u>\$ (737,145)</u>	<u>\$ 26,649,785</u>	<u>\$ 62,187</u>	<u>\$ 32,524,409</u>
Exercise of Stock Options	14,250	20,000	-	-	-	34,250
Issuance of Stock to Profit Sharing Plan-at market	-	169,030	36,866	-	-	205,896
Stock Issued	-	92,502	22,498	-	-	115,000
Comprehensive Income:						
Net earnings	-	-	-	7,537,037	-	7,537,037
Net changes in unrealized depreciation on available for sale securities (net of reclassification adjustment)	-	-	-	-	(47,152)	(47,152)
Total comprehensive income						<u>7,489,885</u>
Adjustments (3-for-2 stock split)	2,517,751	(1,702,963)		(814,788)		-
Cash dividend (0.134 per common share)	-	-	-	(922,265)	-	(922,265)
<b>BALANCES, JULY 31, 2003</b>	<u>\$ 7,567,650</u>	<u>\$ 92,502</u>	<u>\$ (677,781)</u>	<u>\$ 32,449,769</u>	<u>\$ 15,035</u>	<u>\$ 39,447,175</u>
Exercise of Stock Options	389,200	695,515	-	-	-	1,084,715
Tax effect of Stock Options Exercised	-	639,400	-	-	-	639,400
Issuance of Stock to Profit Sharing Plan-at market	-	277,538	32,657	-	-	310,195
Comprehensive Income:						
Net earnings	-	-	-	8,887,792	-	8,887,792
Net changes in unrealized appreciation on available for sale securities (net of reclassification adjustment)	-	-	-	-	12,413	12,413
Total comprehensive income						<u>8,900,205</u>
Cash dividend (0.22 per common share)	-	-	-	(1,573,389)	-	(1,573,389)
<b>BALANCES, JULY 31, 2004</b>	<u>\$ 7,956,850</u>	<u>\$ 1,704,955</u>	<u>\$ (645,124)</u>	<u>\$ 39,764,172</u>	<u>\$ 27,448</u>	<u>\$ 48,808,301</u>

See notes to consolidated financial statements

**THE WASHINGTON SAVINGS BANK, F.S.B., AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**YEARS ENDED JULY 31, 2004, 2003 AND 2002**

	<u>2004</u>	<u>2003</u>	<u>2002</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net earnings	\$ 8,887,792	\$ 7,537,037	\$ 4,564,604
Adjustments to reconcile net earnings to net cash provided (used) by operating activities:			
Provision for loan losses	1,395,000	1,265,000	310,000
Provision for losses on real estate acquired in settlement of loans	7,450	16,058	-
Depreciation	578,800	559,383	577,121
Donation of Land	-	506,000	-
Amortization	3,480	605,681	1,854,681
Gain on sale of mortgage-backed securities	-	(879,691)	(1,424,414)
Gain on sale of other real estate owned	(115,814)	(109,381)	(59,582)
Gain on sale of loans	(2,981,869)	(5,546,912)	(1,682,559)
Gain on sale of building lots and homes	-	(62,076)	(225,777)
Loans originated held for sale	(351,828,747)	(562,651,832)	(183,877,141)
Proceeds from sale of loans held for sale	438,015,543	485,205,969	188,980,554
Increase (decrease) in other assets	60,563	(1,520,116)	(304,423)
(Increase) decrease in accrued interest receivable	(990,223)	(280,193)	43,888
Deferred income taxes	(1,555,876)	(1,532,800)	(289,767)
Increase (decrease) in federal and income taxes payable/receivable	-	1,209,496	(996,708)
Increase in accounts payable, accrued expenses and other liabilities	437,593	971,258	339,915
Increase (decrease) in accrued interest payable	20,713	(67,433)	(100,532)
Decrease (increase) in net deferred loan fees	754,685	(49,537)	31,306
	<u>92,689,090</u>	<u>(74,824,089)</u>	<u>7,741,167</u>
Net cash provided (used) by operating activities			
<b>INVESTING ACTIVITIES:</b>			
Net increase in loans	(173,001,349)	(109,645,036)	(165,448,684)
Purchase of mortgage-backed securities - available for sale	(1,914,623)	(31,094,947)	(102,056,553)
Purchase of mortgage-backed securities - held to maturity	-	-	(37,603,050)
Repayment of mortgage-backed securities	620,483	37,721,947	131,773,215
Sale of mortgage backed securities	-	32,875,541	138,237,379
Purchase of Federal Home Loan Bank Stock	(400,000)	(1,100,000)	(450,000)
Recall of investment securities - held to maturity	778,377	12,872,908	20,074,056
Purchase of premises and equipment	(356,220)	(674,426)	(614,928)
Land development costs incurred	(87,897)	(45,006)	(576,414)
Sale of land held for development	-	115,082	1,277,464
Development of real estate acquired in settlement of loans	(1,001,588)	(28,242)	(282,108)
Sale of real estate acquired in settlement of loans	906,507	702,994	421,305
	<u>(174,456,310)</u>	<u>(58,299,184)</u>	<u>(15,248,317)</u>
Net cash (used) by investing activities			
<b>FINANCING ACTIVITIES:</b>			
Net increase in demand deposits, NOW accounts and savings accounts	12,216,600	15,272,787	10,075,828
Proceeds from issuance of certificates of deposit	137,945,264	102,781,382	29,480,220
Payments for maturing certificates of deposit	(63,524,739)	(35,368,993)	(24,573,100)
Net (decrease) increase in advance payments by borrowers for taxes and insurance	(58,671)	302,633	233,270
Cash dividend	(1,573,389)	(922,266)	(502,750)
Increase in FHLB Advances	8,000,000	34,000,000	-
(Decrease) increase in other borrowings	(14,430,757)	14,430,757	(3,000,000)
Proceeds from exercise of stock options and reduction of treasury stock	1,724,115	34,250	-
	<u>80,298,423</u>	<u>130,530,550</u>	<u>11,713,468</u>
Net cash provided by financing activities			
<b>NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS</b>	(1,468,797)	(2,592,723)	4,206,318
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>	14,447,330	17,040,053	12,833,735
<b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>	<u>\$ 12,978,533</u>	<u>\$ 14,447,330</u>	<u>\$ 17,040,053</u>
<b>CASH PAID DURING THE PERIOD FOR:</b>			
Income taxes	<u>\$ 8,274,595</u>	<u>\$ 3,856,375</u>	<u>\$ 3,564,208</u>
Interest	<u>\$ 12,025,269</u>	<u>\$ 11,739,797</u>	<u>\$ 12,135,518</u>
Non-cash transactions:			
Issuance of treasury stock	\$ 310,196	\$ 320,896	\$ -
Reduction in accrued expenses	(310,196)	(320,896)	-
Transfer MBS held-to-maturity to available-for-sale	-	27,094,717	-
Donation of land held for investment	-	506,000	-
Real estate acquired in settlement of loans	888,988	630,622	21,015

**THE WASHINGTON SAVINGS BANK, F.S.B., AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**YEARS ENDED July 31, 2004, 2003, and 2002**

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**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Principles of Consolidation* - The consolidated financial statements include The Washington Savings Bank, F.S.B. (WSB) and its wholly owned subsidiaries, WSB, Inc. and WSB Investments, Inc. (collectively referred to herein, as the “Company”). All significant intercompany balances and transactions between entities have been eliminated.

*Nature of Operations* - WSB is primarily engaged in the business of obtaining funds in the form of savings deposits and investing such funds in mortgage loans on residential, construction, and commercial real estate, and various types of consumer and other loans, mortgage-backed securities, and investment and money market securities. WSB grants loans throughout the Washington DC, Baltimore, Southern Pennsylvania, Northern Virginia and surrounding metropolitan areas. Its borrowers’ ability to repay is, therefore, dependent upon the economy of that area. WSB, Inc. is primarily engaged in the business of developing single family residential lots. WSB Investments, Inc. is primarily engaged in maintaining and managing an investment portfolio.

*Management Estimates* - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant changes in the near-term relate to the determination of the allowance for loan losses and the valuation of real estate held for development, real estate acquired in settlement of loans and real estate held for investment.

*Cash and Cash Equivalents* - Cash and cash equivalents include demand deposits at other financial institutions and federal funds sold. All cash equivalents have original maturities of three months or less.

*Investment Securities and Mortgage-Backed Securities* - Investment Securities and Mortgage-Backed Securities are required to be segregated into the following three categories: trading, held-to-maturity, and available-for-sale. Trading securities are purchased and held principally for the purpose of reselling them within a short period of time with unrealized gains and losses included in earnings. Debt securities classified as held-to-maturity are accounted for at amortized cost and require the Company to have both the positive intent and ability to hold those securities to maturity. Securities not classified as either trading or held-to-maturity are considered to be available-for-sale. Unrealized gains and losses for available-for-sale securities are excluded from earnings and reported, net of income taxes, as other comprehensive income, a separate component of stockholders’ equity, until realized. If it is determined that any unrealized losses are other than temporary, a charge to earnings is made and a new cost basis is

established. Realized gains or losses on the sale of investment and mortgage-backed securities are reported in earnings and determined using the amortized cost of the specific security sold.

*Loan Origination Fees, Discounts, and Premiums on Loans* - Loan origination fees and direct loan origination costs are deferred and recognized as an adjustment to yield over the lives of the related loans utilizing the interest method. The amortization of such deferred fees and costs is adjusted for the prepayment experience on a loan-by-loan basis. Commitment fees to originate or purchase loans are deferred, and if the commitment is exercised, they are recognized over the life of the loan as an adjustment of yield. If the commitment expires unexercised, commitment fees are recognized in income upon expiration of the commitment.

*Loans* - WSB originates mortgage loans for portfolio investment or sale in the secondary market. During the period of origination, mortgage loans are designated as either held-for-sale or held-for-investment purposes. Mortgage loans held for sale are carried at the lower of cost or fair value, determined on an individual loan basis. There was no valuation allowance during the three years ended July 31, 2004. The basis of loans sold include any deferred loan fees and costs. Transfers of loans held for investment to the held-for-sale portfolio are recorded at the lower of cost or market value on the transfer date with any reduction in a loan's value reflected as a write-down of the recorded investment resulting in a new cost basis with a corresponding charge to the allowance for loan losses. Mortgage loans held for investment are recorded at amortized cost.

*Income Recognition on Loans* - Interest on loans is credited to income as earned on the principal amount outstanding using the interest method. For those loans that are carried on non-accrual status, interest income is recognized on the cash basis. Loans are generally placed on non-accrual status when the collection of principal or interest is 90 days or more past due, or earlier, if collection is deemed uncertain. Previously accrued but uncollected interest on these loans is charged against interest income. Loans may be reinstated to accrual status when such loans have been brought current.

*Allowance for Loan Losses* - The allowance for loan losses represents an amount which, in management's judgment, reflects probable losses on existing loans and other extensions of credit that may become uncollectible as of the balance sheet date. The allowance for loan losses consists of an allocated component and a non-specific component. The components of the allowance for loan losses represent an estimation done pursuant to either Statement of Financial Accounting Standards ("SFAS") No. 5, "Accounting for Contingencies," or SFAS No. 114, "Accounting by Creditors for Impairment of a Loan." The adequacy of the allowance for loan losses is determined through review and evaluation of the loan portfolio along with ongoing monthly assessments of the probable losses inherent in that portfolio, and, to a lesser extent, in unused commitments to provide financing. Loans deemed uncollectible are charged against, while recoveries are credited to, the allowance. Management adjusts the level of allowance through the provision for loan losses, which is recorded as a current period operating expense. The Company's methodology for assessing the appropriateness of the allowance consists of several key elements, which include the formula allowance, specific allowances and the non-specific allowance. The amount of the allowance is reviewed monthly by the Loan Committee, and reviewed and approved by the Board of Directors.

The formula allowance is calculated by applying loss factors to corresponding categories of outstanding loans. Loss factors consider the Company's historical loss experience in the various portfolio categories over the prior twelve quarters. The use of these loss factors is intended to reduce the differences between estimated losses inherent in the portfolio and observed losses.

Specific allowances are established in cases where management has identified significant conditions or circumstances related to a loan that management believes indicate the probability that a loss has been incurred in an amount different from the amount determined by application of the formula allowance. For other problem-graded credits, allowances are established according to the application of loan risk factors. These factors are set by management to reflect its assessment of the relative level of risk inherent in each grade.

The non-specific allowance is based upon management's evaluation of various conditions that are not directly measured in the determination of the formula and specific allowances. Such conditions include general economic and business conditions affecting key lending areas, loan quality trends (including trends in delinquencies and nonperforming loans expected to result from existing conditions), loan volumes and concentrations, specific industry conditions within portfolio categories, recent loss experience in particular loan categories, duration of the current business cycle, bank regulatory examinations results and management's judgment with respect to various other conditions including credit administration and management and the quality of risk identification systems. Executive management reviews these conditions monthly.

Management believes that the allowance for loan losses reflects its best estimate of the probable losses in the held-for-investment loan portfolio as of the balance sheet date. However, the determination of the allowance requires significant judgment, and estimates of probable losses inherent in the loan portfolio can vary significantly from the amounts actually observed. While management uses available information to recognize probable losses, future additions to the allowance may be necessary based on changes in the credits comprising the loan portfolio and changes in the financial condition of borrowers, such as may result from changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review WSB's loan portfolio and allowance for loan losses. Such review may result in recognition of additions to the allowance for loan losses based on the examiners' judgments of information available to them at the time of their examination.

*Impairment of Loans* - WSB considers a loan impaired when it is probable that WSB will be unable to collect all interest and principal payments as scheduled in the loan agreement in accordance with SFAS No. 114. A loan is tested for impairment once it becomes 90 days past due. A loan is not considered impaired during a period of "insignificant delay" in payment if the ultimate collectibility of all amounts due is expected. WSB defines an "insignificant delay" in payment as past due less than 90 days. A valuation allowance is maintained to the extent that the measure of the impaired loan is less than the recorded investment. WSB's residential mortgage and consumer loan portfolios are collectively evaluated for impairment. The impairment of a loan is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or the fair value of the collateral if repayment is expected to be provided by the collateral. Generally, WSB's impairment on such loans is measured by reference to the fair value of the collateral. Interest income on impaired loans is recognized on the cash basis.

*Real Estate Acquired in Settlement of Loans* - Real estate acquired in settlement of loans is carried at the lower of WSB's recorded investment or fair value at the date of acquisition. Write-downs to fair value at the date of acquisition are charged to the allowance for loan losses. Costs relating to the development and improvement of a property are capitalized, whereas those relating to holding the property are charged to expense when incurred. The real estate is carried at the lower of net carrying value or fair value less estimated costs to sell subsequent to acquisition. Operating expenses of real estate owned are reflected in other non-interest expenses.

The amounts WSB could ultimately recover from real estate acquired in settlement of loans could differ materially from the amounts used in arriving at the net carrying value of the assets because of future market factors beyond WSB's control or changes in WSB's strategy for recovering its investment.

*Premises and Equipment* - Depreciation on buildings, furniture, and equipment is computed using the straight-line method over each asset's estimated useful life. Leasehold improvements are amortized using the straight-line method over the lesser of the estimated useful life or the lease term. Such estimated useful lives are as follows:

Buildings	39 years
Improvement to buildings	5-10 years
Leasehold improvements	5-10 years
Furniture, equipment	7 years
Computer equipment	4 years
Software	3 years
Automobiles	3 years

*Mortgage Banking Activities* – It is the current practice of WSB to sell mortgage loans without retaining loan servicing rights (commonly referred to as “servicing released”). WSB has not purchased mortgage loans with servicing rights subsequent to 1994. Prior to 1995, WSB originated and sold some mortgage loans with servicing retained. The accounting treatment in effect at that time prohibited the capitalization of mortgage rights on internally originated loans that were subsequently sold. Accordingly, there are no capitalized mortgage servicing assets at July 31, 2004 and 2003.

*Advertising Costs* – The Company expenses advertising costs as they are incurred.

*Income Taxes* – The Company files a consolidated federal income tax return with its subsidiaries. Deferred income tax assets and liabilities are recognized for the future income tax consequences attributed to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Any deferred tax asset is reduced by the amount of any tax benefit that more likely than not will not be realized.

*Earnings Per Share* - Basic earnings per share (EPS) excludes dilution and is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if options to issue common stock were exercised. The fiscal year 2002 has been adjusted to reflect

the April 10, 2003 three-for-two stock split. No shares of common stock equivalents were excluded from the diluted EPS computation for the three fiscal years ended July 31, 2003. Average common and common equivalent shares used in the determination of earnings per share were:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Weighted average common shares	7,131,363	6,894,651	6,855,684
Effect of dilutive stock options	<u>908,883</u>	<u>832,258</u>	<u>501,576</u>
Diluted common shares	<u>8,040,246</u>	<u>7,726,909</u>	<u>7,357,260</u>

*Reclassifications* - Certain reclassifications have been made to the prior years' consolidated financial statements to conform to the 2004 presentation.

*Stock-Based Compensation* - WSB has adopted the disclosure-only provisions of SFAS No. 123, "Accounting for Stock-Based Compensation" and SFAS No. 148 "Accounting for Stock-Based Compensation-Transition and Disclosure", but applies Accounting Principles Board Opinion No. 25 and related interpretations in accounting for its Stock Option Plans ("the Plans"). No compensation expense related to the Plans was recorded during the three years ended July 31, 2004. If WSB had elected to recognize compensation cost based on fair value at the grant dates for awards under the Plan consistent with the method prescribed by SFAS No. 123, net income and earnings per share would have been changed to the pro forma amounts as follows for the three years ended July 31, 2004.

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Net income, as reported	\$ 8,887,792	\$ 7,537,037	\$ 4,564,604
Less pro forma stock-based compensation expense Determined under the fair value method, net of related tax effects	(370,464)	(503,204)	(391,127)
Pro forma net income	\$ 8,517,328	\$ 7,033,833	\$ 4,173,477
Net income per share:			
Basic - as reported	\$ 1.25	\$ 1.09	\$ 0.67
Basic - pro forma	\$ 1.19	\$ 1.07	\$ 0.61
Diluted - as reported	\$ 1.11	\$ 0.98	\$ 0.62
Diluted - pro forma	\$ 1.06	\$ 0.96	\$ 0.57

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions used for grants during the years ended July 31, 2003 and 2002. There were no option grants during fiscal year ended July 31, 2004, however, grants in prior years vested during fiscal 2004.

	<u>2003</u>	<u>2002</u>
Dividend yield	0.64%	2.25%
Expected volatility	33%	33%
Risk free rate	4.64%	4.84%
Expected lives (in years)	10	10

*New Accounting Pronouncements* - On March 9, 2004, the SEC issued Staff Accounting Bulletin 105, "Application of Accounting Principles to Loan Commitments." (SAB 105) to inform registrants of the Staff's view that the fair value of the recorded loan commitments should not consider the expected future cash flows related to the associated servicing of the future loan. The provisions of SAB 105 must be applied to loan commitments accounted for as derivatives for reporting periods beginning after March 31, 2004. WSB does not currently include, and was not including, the value of mortgage servicing or any other internally-developed intangible assets in the valuation of its mortgage loan commitments. The adoption of SAB 105 did not have a material impact on WSB's financial condition or results of operations.

In January 2003, the Financial Accounting Standards Board (the "FASB") issued Interpretation No. 46, "Consolidation of Variable Interest Entities" ("Interpretation No. 46"), which explains identification of variable interest entities and the assessment of whether to consolidate those entities. FIN 46 Revised ("FIN 46R"), issued in December 2003, replaces FIN 46. FIN 46R requires public entities to apply FIN 46 or FIN 46R to all entities that are considered variable interest entities in practice and under the FASB literature that was applied before the issuance of FIN 46 by the end of the first reporting period that ends after December 15, 2003. For any variable interest entities ("VIE") that must be consolidated under FIN 46R, the assets, liabilities and noncontrolling interests of the VIE initially would be measured at their carrying amounts with any difference between the net amount added to the statement of condition and any previously recognized interest being recognized as the cumulative effect of an accounting change. If determining the carrying amounts is not practicable, fair value at the date FIN 46R first applies may be used to measure the assets, liabilities and noncontrolling interest of the VIE. WSB has no variable interest entities as defined by FIN 46R.

In November 2003, the Emerging Issues Task Force ("EITF") of the FASB issued EITF Abstract 03-1, "The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments" ("EITF 03-1") effective for fiscal years ending after December 15, 2003. This abstract provides guidelines on the meaning of other-than-temporary impairment and its application to investments, in addition to requiring quantitative and qualitative disclosures in the financial statements. In March 2004, the EITF issued a Consensus on Issue 03-1 (the "Consensus") requiring that the provisions of EITF 03-1 be applied to cost-method investments for annual periods ending after June 30, 2004. The Consensus also requires several additional disclosures for cost-method investments. Recognition and measurement guidance of the Consensus will be applied to other-than-temporary impairment evaluations in reporting periods beginning after June 15, 2004, as required. The Company has implemented the guidelines of this Consensus. The adoption of the Consensus did not have any impact on WSB's financial statements.

## 2. LOANS RECEIVABLE

Loans receivable held-for-investment consist of the following:

	July 31,	
	2004	2003
FIRST MORTGAGE LOANS:		
Secured by single-family residences	\$ 161,689,584	\$ 115,001,457
Secured by 5 or more- residential	4,243,284	3,829,979
Secured by other properties	16,066,907	6,660,384
Construction loans	226,356,376	142,075,341
Land and land development loans	44,854,719	23,418,295
Land acquisition loans	9,113,846	2,229,585
	<u>462,324,716</u>	<u>293,215,041</u>
SECOND MORTGAGE LOANS	5,071,443	2,751,198
CONSUMER AND OTHER LOANS:		
Commercial	2,947,127	1,436,534
Loans secured by savings accounts	235,551	249,562
Consumer installment loans	393,605	444,776
	<u>393,605</u>	<u>444,776</u>
TOTAL LOANS RECEIVABLE HELD-FOR-INVESTMENT	470,972,442	298,097,111
LESS:		
Allowance for loan losses	3,503,329	2,234,348
Deferred loan fees	1,448,280	693,593
	<u>1,448,280</u>	<u>693,593</u>
	<u>\$ 466,020,833</u>	<u>\$ 295,169,170</u>

WSB originates adjustable and fixed interest rate loans. The adjustable rate loans have interest rate adjustment limitations and are generally indexed to the 1- or 3-year U.S. Treasury index. Future market factors may affect the correlation of the interest rate adjustment with the rates WSB pays on the short-term deposits that have been primarily utilized to fund these loans. Adjustable interest rate loans at July 31, 2004 and 2003, were \$1,798,419 and \$1,119,470, respectively.

*Allowance for Loan Losses* - Activity in the allowance for loan losses is summarized as follows:

	Years Ended July 31,		
	2004	2003	2002
BALANCE, BEGINNING OF YEAR	\$ 2,234,348	\$ 1,469,446	\$ 1,183,829
Provision charged to operations	1,395,000	1,265,000	310,000
Charge-offs	(163,584)	(506,775)	(50,215)
Recoveries of previously charged-off amounts	37,565	6,677	25,832
	<u>37,565</u>	<u>6,677</u>	<u>25,832</u>
BALANCE, END OF YEAR	<u>\$ 3,503,329</u>	<u>\$ 2,234,348</u>	<u>\$ 1,469,446</u>

WSB had one restructured loan classified as impaired as of July 31, 2004, 2003 and 2002, having a balance of \$675,311, \$696,544 and \$716,441 respectively.

	July 31,		
	2004	2003	2002
Impaired loan with a valuation allowance	\$ 675,311	\$ 696,544	\$ 716,441
Total impaired loan	675,311	696,544	716,441
Average impaired loan for the year	685,159	705,772	725,100
Allowance for loan loss related to impaired loan	13,500	13,900	14,300
Interest income on impaired loan recognized on the cash basis	44,673	46,010	47,241

Loans on which the recognition of interest has been discontinued that were not included within the scope of SFAS No. 114 amounted to approximately \$2,010,631, \$1,931,680 and \$921,580 at July 31, 2004, 2003 and 2002. If interest income had been recognized on those loans at their stated rates during the fiscal years 2004, 2003 and 2002, interest income would have been increased by approximately \$104,991, \$101,255, and \$50,154, respectively.

WSB originated nonresidential real estate loans that had an outstanding balance of \$16,066,906, \$6,660,384 and \$8,715,205 at July 31, 2004, 2003 and 2002, respectively. These loans are considered by management to have somewhat greater risk of collectibility due to the dependence on income production. Additionally, all of WSB's non-residential real estate loans were collateralized by real estate (primarily warehouse and office space) in the Washington, D.C. metropolitan area.

WSB originates and participates in land and land development loans and real estate construction loans, the proceeds of which are used by the borrower for acquisition, development, and construction purposes. Often the loan arrangements require WSB to provide, from the loan proceeds, amounts sufficient for payment of loan fees and anticipated costs during acquisition, development, or construction, including interest. This type of lending is considered by management to have higher risks. At July 31, 2004, 2003 and 2002, the undisbursed portion of such loans totaled \$130,795,360, \$92,379,213 and \$48,998,738.

*Loans Serviced for Others* - Loans serviced for others and not reflected in the consolidated statements of financial condition are \$1,252,888, \$2,436,730 and \$3,444,026 at July 31, 2004, 2003 and 2002, respectively. Servicing loans for others generally consists of collecting mortgage payments, maintaining escrow accounts, disbursing payments to investors, and foreclosure processing. Loan servicing income is recorded on the accrual basis and includes servicing fees from investors and certain charges collected from borrowers, such as late payment fees. In connection with the loans serviced for others, WSB held borrowers' escrow balances of \$14,661, \$27,657 and \$31,084 at July 31, 2004, 2003 and 2002, respectively.

WSB has made loans to certain of its executive officers and directors. These loans were made on substantially the same terms, including interest rate and collateral requirements, as those prevailing at the time for comparable transactions with unrelated customers. The risk of loss on these loans is considered to be no greater than for loans made to unrelated customers.

The following schedule summarizes changes in amounts of loans outstanding to executive officers and directors for the years ended July 31:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Balance at beginning of year	\$ 271,150	\$ 68,150	\$ -
Additions	-	283,000	68,150
Repayments	<u>271,150</u>	<u>80,000</u>	<u>-</u>
Balance at end of year	<u>\$ -</u>	<u>\$ 271,150</u>	<u>\$ 68,150</u>

### 3. MORTGAGE-BACKED SECURITIES

Mortgage-backed securities consist of the following:

	<u>July 31, 2004</u>			
	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Estimated Fair Value</u>
AVAILABLE FOR SALE:				
FNMA pass-through certificates	\$ 1,882,934	\$ 30,774	\$ -	\$ 1,913,708
FHLMC pass-through certificates	<u>230,660</u>	<u>10,814</u>	<u>-</u>	<u>241,474</u>
	<u>\$ 2,113,594</u>	<u>\$ 41,588</u>	<u>\$ -</u>	<u>\$ 2,155,182</u>
Weighted average interest rate	<u>5.60%</u>			

	<u>July 31, 2003</u>			
	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Estimated Fair Value</u>
AVAILABLE FOR SALE:				
FHLMC pass-through certificates	\$ 819,455	\$ 22,780	\$ -	\$ 842,235
	<u>\$ 819,455</u>	<u>\$ 22,780</u>	<u>\$ -</u>	<u>\$ 842,235</u>
Weighted average interest rate	<u>6.50%</u>			

Gross realized gains on available for sale securities were \$0, \$879,691 and \$1,424,414 for the years ended July 31, 2004, 2003 and 2002.

As of July 31, 2004, WSB had no mortgage-backed securities that had continuous unrealized losses for greater than 12 months.

#### 4. INVESTMENT SECURITIES

Investment securities consist of the following:

	<b>July 31, 2004</b>			
	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Estimated Fair Value</b>
HELD TO MATURITY:				
Merrill Lynch Zero Coupon Bond	\$ 1,538,860	\$ 28,445	\$ -	\$ 1,567,305
Preferred Trust Bonds	<u>4,048,700</u>	<u>46,679</u>	<u>-</u>	<u>4,095,379</u>
	<u>\$ 5,587,560</u>	<u>\$ 75,124</u>	<u>\$ -</u>	<u>\$ 5,662,684</u>

As of July 31, 2004, WSB had no investments in a single issuer that exceeded 10% of stockholders' equity.

	<b>July 31, 2003</b>			
	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Estimated Fair Value</b>
HELD TO MATURITY:				
FHLMC Zero Coupon Bond	\$ 897,253	\$ -	\$ 13,005	\$ 884,248
Merrill Lynch Zero Coupon Bond	1,419,984	-	40,154	1,379,830
Preferred Trust Bonds	<u>4,052,180</u>	<u>-</u>	<u>92,480</u>	<u>3,959,700</u>
	<u>\$ 6,369,417</u>	<u>\$ -</u>	<u>\$ 145,639</u>	<u>\$ 6,223,778</u>

Maturities for the investment securities held to maturity are as follows:

	<b>2004</b>		<b>2003</b>	
	<b>Amortized Cost</b>	<b>Estimated Fair Value</b>	<b>Amortized Cost</b>	<b>Estimated Fair Value</b>
Due in one year or less	\$ -	\$ -	\$ -	\$ -
Due after one year through five years	-	-	-	-
Due after five years through ten years	5,587,560	5,662,684	6,369,417	6,223,778
Due after ten years	<u>5,587,560</u>	<u>5,662,684</u>	<u>6,369,417</u>	<u>6,223,778</u>
Total debt securities	<u>\$ 5,587,560</u>	<u>\$ 5,662,684</u>	<u>\$ 6,369,417</u>	<u>\$ 6,223,778</u>

During fiscal year 2004, the FHLB Zero Coupon Bond was called at the coupon's call date for a total of \$897,253.

As of July 31, 2004, WSB had no investment securities that had continuous unrealized losses for greater than 12 months.

## 5. LAND HELD FOR DEVELOPMENT

WSB's wholly owned subsidiary, WSB, Inc., purchased land in Maryland to develop into single family building lots that were offered for sale to third parties. The subsidiary also builds homes on certain lots on a contract basis. During fiscal 2004, WSB, Inc. purchased one lot to construct a house on. The lot is currently being developed and planned to be completed in the next fiscal year. During fiscal 2003, WSB, Inc. purchased and sold one lot for a gross profit of \$21,297. Adjustments to accruals for estimated completion costs from lots previously sold in prior fiscal years resulted in gains of \$40,109 recognized during fiscal 2003.

Projects are carried at the lower of cost or net realizable value. The ability of the subsidiary to recover the carrying value of real estate held for development is based upon future sales. The ability to effect such sales is subject to market conditions.

Gross proceeds from the sale of lots were \$0, \$80,000 and \$1,398,050, for fiscal years ended July 31, 2004, 2003 and 2002, respectively. Related gains were \$0, \$62,076 and \$225,777 in each of those respective fiscal years.

## 6. REAL ESTATE ACQUIRED IN SETTLEMENT OF LOANS AND HELD FOR INVESTMENT

Real estate acquired in settlement of loans consists of the following:

	<u>July 31,</u>		
	<u>2004</u>	<u>2003</u>	<u>2002</u>
Single family properties	\$ 689,971	\$ 486,000	\$ 461,274
Land	-	40,526	-
Less: valuation allowance	<u>-</u>	<u>(40,000)</u>	<u>(23,941)</u>
	<u>\$ 689,971</u>	<u>\$ 486,526</u>	<u>\$ 437,333</u>

Noncash transfers from loans receivable to real estate acquired in settlement of loans were \$888,988, \$630,622 and \$21,015 for the years ended July 31, 2004, 2003 and 2002, respectively.

Activity in the valuation allowance for estimated losses on real estate acquired in settlement of loans for the years ended July 31, 2004, 2003 and 2002 was as follows:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
BALANCE, BEGINNING OF YEAR	\$ 40,000	\$ 23,941	\$ 30,000
Valuation allowance charged to operations	-	16,059	-
Charge-offs	<u>(40,000)</u>	<u>-</u>	<u>(6,059)</u>
BALANCE, END OF YEAR	<u>\$ -</u>	<u>\$ 40,000</u>	<u>\$ 23,941</u>

During fiscal 2004, WSB had no real estate property held-for-investment. During the first quarter of fiscal 2003, WSB granted a deed of conservation easement to the Maryland Environmental Trust on the real estate held for investment property, formerly a land acquisition loan, which had a carrying amount of \$506,000.

## 7. PREMISES AND EQUIPMENT

Premises and equipment consist of the following:

	<u>July 31,</u>		
	<u>2004</u>	<u>2003</u>	<u>2002</u>
Buildings	\$ 6,351,606	\$ 6,336,986	\$ 6,257,531
Land	1,038,294	1,038,294	1,038,294
Furniture and fixtures	2,625,251	2,402,931	1,922,646
Leasehold improvements	209,466	195,360	191,640
Automobiles	<u>186,811</u>	<u>227,974</u>	<u>183,553</u>
	10,411,428	10,201,545	9,593,664
Less accumulated depreciation and amortization	<u>(4,105,599)</u>	<u>(3,673,135)</u>	<u>(3,180,297)</u>
	<u>\$ 6,305,829</u>	<u>\$ 6,528,410</u>	<u>\$ 6,413,367</u>

## 8. DEPOSITS

Deposits consist of the following:

	<u>July 31,</u>			
	<u>2004</u>		<u>2003</u>	
	<u>Amount</u>	<u>Weighted Average Interest Rate</u>	<u>Amount</u>	<u>Weighted Average Interest Rate</u>
Non-interest-bearing:				
Checking accounts	<u>\$ 10,345,534</u>	- %	<u>\$ 7,007,195</u>	- %
Interest-bearing:				
NOW accounts	18,849,933	0.20	16,432,223	0.20
Savings deposits	66,953,547	1.20	60,490,415	1.19
Time Deposits	<u>282,135,930</u>	3.61	<u>207,697,274</u>	4.03
	<u>367,939,410</u>		<u>284,619,912</u>	
	<u>\$ 378,284,944</u>	2.92%	<u>\$ 291,627,107</u>	3.13%

Time deposits at July 31, 2004 mature as follows:

	<b>Amount</b>	<b>Average Interest Rate</b>
Under 6 months	\$ 40,898,326	4.68 %
6 to 12 months	68,553,463	3.24
12 to 24 months	58,753,633	3.01
24 to 36 months	22,710,300	3.44
36 to 48 months	32,203,408	3.57
48 to 60 months	<u>59,016,800</u>	3.99
	<u>\$ 282,135,930</u>	3.61 %

WSB has approximately 231 time deposit accounts exceeding \$100,000 for a total of \$144,128,445, at July 31, 2004. These funds were primarily used to fund WSB loan originations. Deposit amounts exceeding \$100,000 are not federally insured. Of this total, approximately 28 accounts are funds received through brokers. These brokered accounts consist of individual accounts issued under master certificates in the broker's name. These types of accounts meet the FDIC requirements and are federally insured.

The following is a summary of interest expense on deposits:

	<b>Year Ended July 31,</b>		
	<b>2004</b>	<b>2003</b>	<b>2002</b>
NOW accounts	\$ 300,387	\$ 276,267	\$ 281,663
Savings deposits	512,887	541,116	899,869
Time deposits	<u>8,546,851</u>	<u>7,545,181</u>	<u>7,964,106</u>
	<u>\$ 9,360,125</u>	<u>\$ 8,362,564</u>	<u>\$ 9,145,638</u>

## 9. OTHER BORROWINGS

Other Borrowings are as follows:

	<b>Year Ended July 31, 2004</b>			
	<b>Balance at year end</b>	<b>Rate at year end</b>	<b>Average balance for the year</b>	<b>Weighted average rate</b>
FHLB-advances-fixed	\$ 45,900,000	5.45%	\$ 50,873,000	5.45%
FHLB-advances-adjustable	5,000,000	1.70%	4,768,000	1.70%
FHLB-advances-daily rate credit	<u>39,000,000</u>	1.55%	<u>7,107,000</u>	1.28%
Total	<u>\$ 89,900,000</u>		<u>\$ 62,748,000</u>	

	<b>Year Ended July 31, 2003</b>			
	<b>Balance at year end</b>	<b>Rate at year end</b>	<b>Average balance for the year</b>	<b>Weighted average rate</b>
FHLB-advances-fixed	\$ 50,900,000	4.88%	\$ 48,400,000	4.87%
FHLB-advances-adjustable	10,000,000	1.14%	9,300,000	1.14%
FHLB-advances-daily rate credit	21,000,000	1.29%	12,000,000	1.29%
Reverse Repurchase Agreements	4,430,757	3.50%	1,350,000	2.50%
First Tennessee Line of Credit	10,000,000	1.25%	-	1.25%
Total	<u>\$ 96,330,757</u>		<u>\$ 71,050,000</u>	

The fixed rate advances mature as follows: \$5.0 million in April 2006; \$28.0 million in February 2010; \$10.0 million in January 2011; \$2.9 million in February 2011. During fiscal 2004, \$5.0 million was called on the respective call dates which resulted in a conversion to adjustable rate borrowings.

WSB is required to maintain collateral against FHLB advances. This collateral consists of a blanket lien on WSB's 1-to-4 family residential loan portfolio, which had a balance of \$148,732,733, \$115,001,457 and \$109,571,967 at July 31, 2004, 2003 and 2002, respectively.

During fiscal 2004, WSB repaid the Reverse Repurchase Agreement and the First Tennessee Line of Credit totaling \$14.4 million.

During the years ended July 31, 2004 and 2003, the maximum month end balance of other borrowings was \$89,900,000 and \$101,456,000, respectively.

## **10. BENEFIT PLANS**

*Profit-Sharing Plan* - WSB has a profit-sharing plan for the benefit of substantially all of its employees. The plan provides for the payment of benefits to eligible employees or their beneficiaries upon retirement or, in some cases, upon earlier termination of employment. Employer contributions to the plan are determined each year by the Board of Directors. The contribution to the profit-sharing plan was approximately \$399,009, \$308,860 and \$205,897 for the years ended July 31, 2004, 2003, and 2002, respectively.

*Stock Option Plans* - WSB has five stock option plans, which reserve shares of common stock for issuance to certain key employees and non-employee directors. The combination of these plans reserves 1,875,000 number of shares under option, of which 1,474,500 options have been granted and 400,500 options remain available for grant.

The 1988 Stock Incentive Plan (which expired on May 17, 1998) authorized the granting of options for 375,000 shares of common stock, which expire ten years after grant date. Options are exercisable at 50% one year after the date of grant and the remaining 50% two years after the date of grant. As of July 31, 2004, there are no options available for grant under this plan.

The Non-Employee Directors' Plan authorized the granting of options for 60,000 shares of common stock to four non-employee directors, who each received 3,000 options on December 20 for five consecutive years beginning 1995 through 1999 to acquire 15,000 shares each. At July 31, 2004, there were no options available for grant under this plan. The exercise price of the options granted pursuant to this plan is the fair market value of the shares on the date of grant.

The 1997 Omnibus Stock Plan ("1997 Plan"), which was approved by stockholders on November 20, 1997, authorized the grant of options for 375,000 shares of common stock. On February 18, 1998, 187,500 options were granted and on March 18, 1999, the remaining 187,500 options were granted. The grants are exercisable at 50% one year after the date of grant and the remaining 50% two years after the date of grant. On November 18, 1999, the 187,500 options granted on February 18, 1998 were cancelled. Options for 187,500 shares of common stock were granted on May 18, 2000. On November 16, 2000, 7,500 options were granted and on May 30, 2002, 7,500 additional options were granted. Options expire ten years from the date of grant. The remaining 16,500 options that were available at July 31, 2001, were granted on October 1, 2001. In October 2001, an additional 112,500 options became available due to employment termination. These options were granted on November 1, 2001. At July 31, 2004, there were 6,000 options available for grant under the 1997 Plan as a result of option cancellations that occurred due to employment termination. The exercise price of the options granted pursuant to this plan is the fair market value of the shares on the date of grant.

The 1999 Omnibus Stock Option and Incentive Plan ("1999 Plan"), which was approved by stockholders on November 18, 1999, authorized the granting of options for 750,000 shares of which 396,000 shares were granted on May 18, 2000. On November 16, 2000, an additional 225,000 options were granted. On January 19, 2001, 60,000 options were granted and on May 30, 2001, 100,500 options were granted. At July 31, 2001, there were 3,000 options available under the 1999 Plan due to cancellations. During August and September 2001, 7,500 options became available and another 90,000 in October 2001. On October 1, 2001, 9,000 options were granted. On November 1, 2001, 90,000 options were granted and on December 19, 2001, 1,500 options were granted. In July 2002, 2,250 options became available for grant due to employee termination. At July 31, 2004, there were 3,000 options available for grant under the 1999 Plan due to employee termination. The shares are exercisable at 50% one year after the date of grant and the remaining 50% two years after the date of grant. Options expire ten years from the date of grant. The exercise price of the options granted pursuant to this plan is the fair market value of the shares on the date of grant.

The 2001 Omnibus Stock Option and Incentive Plan ("2001 Plan"), which was approved by stockholders on November 21, 2001, authorized the granting of options for 750,000 shares of which 288,000 were granted on December 19, 2001, 15,000 were granted on March 20, 2002 and 75,000 were granted on November 20, 2002. At July 31, 2004, there were 19,500 options available for grant due to employee termination leaving 391,500 total options available for grant under the 2001 Plan. The shares are exercisable at 50% one year after the date of grant and the remaining 50% two years after the date of grant. Options expire ten years from date of grant. The exercise price of the options granted pursuant to this plan is the fair market value of the shares on the date of grant.

The exercise price of the options was adjusted accordingly to reflect the effect of previous stock dividends. The plans' activities are summarized as follows:

	2004		2003		2002	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding at beginning of year	1,545,675	\$2.95	1,490,925	\$2.83	1,178,175	\$2.50
Exercised	(389,200)	2.63	(14,250)	2.40	-	-
Granted	-	-	75,000	5.20	532,500	3.39
Forfeited	(12,750)	4.46	(6,000)	3.20	(219,750)	2.40
Outstanding at end of year	<u>1,143,725</u>	\$2.92	<u>1,545,675</u>	\$2.95	<u>1,490,925</u>	\$2.83

A summary of information about stock options outstanding is as follows at July 31, 2004:

Exercise Price	Options Outstanding		Shares
	Shares	Weighted Average Remaining Life (Years)	Underlying Options Currently Exercisable
\$2.2083	9,000	5.5	9,000
\$2.2083	161,000	6.3	161,000
\$2.2500	283,800	5.8	283,800
\$2.2917	31,500	6.4	31,500
\$2.5800	72,000	6.8	72,000
\$2.6667	100,500	4.9	100,500
\$3.0000	9,000	4.5	9,000
\$3.1667	13,500	7.3	13,500
\$3.2667	144,000	7.4	144,000
\$3.3333	9,000	2.5	9,000
\$3.4667	205,500	7.6	205,500
\$3.5833	9,000	1.5	9,000
\$3.9333	15,000	7.9	15,000
\$5.2920	12,675	3.8	12,675
\$5.4167	9,000	3.5	9,000
\$5.2000	59,250	8.8	28,875
	<u>1,143,725</u>	<u>6.0</u>	<u>1,113,350</u>

## 11. COMMITMENTS AND CONTINGENCIES

WSB has entered into long-term operating leases for certain premises. Some of these leases require payment of real estate taxes and other related expenses, and some contain escalation clauses that provide for increased rental payments under certain circumstances. Certain leases also contain renewal options. Rental expense under leases for the years ended July 31, 2004, 2003, and 2002, was \$428,285, \$311,904, and \$248,410, respectively.

At July 31, 2004 the minimum rental commitment for the noncancelable leases is as follows:

Year ending <u>July 31,</u>	<u>Total</u>
2005	\$ 352,789
2006	307,959
2007	244,184
2008	186,162
2009	42,256
	<u>\$1,133,350</u>

As of July 31, 2004, commitments to grant mortgage loans, standby letters of credits and financial guarantees written aggregated to \$27,934,634 of which \$9,875,990 are fixed rate loans with interest rates ranging from 4.25% to 8.50%, \$2,093,000 are adjustable rate loans that are loans held for sale, compared to 117,377,964 of which \$18,908,165 were fixed rate loans with interest rates ranging from 4.125% to 7.75% as of July 31, 2003.

During the second quarter of 2004, the Maryland Legislature passed two tax bills relating to certain payments among related entities. The first bill requires taxpayers to add back otherwise deductible interest and intangible expenses paid to related entities for tax years beginning after December 31, 2003. Some exceptions apply, including certain interest expenses deducted among related banks, so long as the transactions fall within the legislation's "safe harbor" provision. In applying the add back and safe harbor provisions, Maryland's Comptroller has been granted discretionary authority to determine whether the transaction giving rise to the payment had as a principal purpose the avoidance of tax and whether it was at arm's length. Additionally, the Comptroller's Office now has the power to reallocate or reapportion income among related entities if it determines that the entities' income is not accurately reflected on their tax returns. The second bill gives taxpayers the right to take advantage of an amnesty period. WSB is currently in the process of determining what impact, if any, this legislation will have on its operations and financial results.

## **12. STOCKHOLDERS' EQUITY AND REGULATORY MATTERS**

WSB is insured by the Federal Deposit Insurance Corporation (FDIC) Savings Association Insurance Fund (SAIF) and is regulated by the Office of Thrift Supervision (OTS). As a condition of maintaining the insurance of accounts, WSB is required to maintain certain minimum regulatory capital in accordance with a formula provided in the regulations. WSB may not pay dividends on its stock unless all such capital requirements are met. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on WSB's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, WSB must meet specific capital guidelines that involve quantitative measures of WSB's assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. WSB's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require WSB to maintain minimum amounts and ratios (set forth in the table below) of tangible and core capital (as defined in the regulations) to total adjusted assets (as defined), and of total capital (as defined) to risk-weighted assets (as defined). Management believes, as of July 31, 2004, that WSB meets all capital adequacy requirements to which it is subject.

As of July 31, 2004, the most recent notification from the OTS categorized WSB as well capitalized under the regulatory framework for prompt corrective action. To be categorized as "well-capitalized," WSB must maintain minimum core, tier 1 risk-based and total risk-based ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed WSB's category.

WSB's actual capital amounts and ratios for 2004 and 2003 are presented in the tables below:

	<b>Actual</b>		<b>Required for Capital Adequacy Purposes</b>		<b>To Be Considered Well Capitalized Under Prompt Corrective Action</b>	
	<b>Amount</b>	<b>Ratio</b>	<b>Amount</b>	<b>Ratio</b>	<b>Amount</b>	<b>Ratio</b>
<b>At July 31, 2004:</b>						
Tangible (to Tangible Assets)	\$ 48,748,699	9.35 %	\$ 7,820,176	1.50 %	N/A	N/A
Core (leverage) (to Adjusted Tangible Assets)	48,748,699	9.35 %	20,853,803	4.00 %	\$ 26,067,254	5.00 %
Tier 1 capital (to Risk Weighted Assets)	48,748,699	11.16 %	N/A	N/A	26,202,287	6.00 %
Total capital (to Risk Weighted Assets)	52,252,028	11.97 %	34,936,383	8.00 %	43,670,479	10.00 %
<b>At July 31, 2003:</b>						
Tangible (to Tangible Assets)	\$ 39,397,843	9.10 %	\$ 6,493,658	1.50 %	N/A	N/A
Core (leverage) (to Adjusted Tangible Assets)	39,397,843	9.10 %	17,316,422	4.00 %	\$ 21,645,527	5.00 %
Tier 1 capital (to Risk Weighted Assets)	39,397,843	12.66 %	N/A	N/A	18,666,286	6.00 %
Total capital (to Risk Weighted Assets)	41,632,191	13.38 %	24,888,381	8.00 %	31,110,477	10.00 %

The following table summarizes the reconciliation of stockholders' equity to regulatory capital.

	<b>July 31, 2004</b>		
	<b>Tangible Capital</b>	<b>Core Capital</b>	<b>Total Capital</b>
Total stockholders' equity	\$ 48,808,301	\$48,808,301	\$48,808,301
Nonallowable assets:			
Investment in subsidiary	(32,154)	(32,154)	(32,154)
Unrealized appreciation on available for sale securities, net of taxes	(27,448)	(27,448)	(27,448)
Additional item:			
Allowance for loan losses	<u>-</u>	<u>-</u>	<u>3,503,329</u>
Total regulatory capital	<u>\$ 48,748,699</u>	<u>\$48,748,699</u>	<u>\$52,252,028</u>

	<b>July 31, 2003</b>		
	<b>Tangible Capital</b>	<b>Core Capital</b>	<b>Total Capital</b>
Total stockholders' equity	\$39,447,175	\$39,447,176	\$39,447,176
Nonallowable assets:			
Investment in subsidiary	(34,297)	(34,298)	(34,298)
Unrealized appreciation on available for sale securities, net of taxes	(15,035)	(15,035)	(15,035)
Additional item:			
Allowance for loan losses	<u>-</u>	<u>-</u>	<u>2,234,348</u>
Total regulatory capital	<u>\$39,397,843</u>	<u>\$39,397,843</u>	<u>\$41,632,191</u>

At July 31, 2004 and 2003, tangible assets used in computing regulatory capital were \$521,345,087 and \$432,910,536, respectively, and total risk-weighted assets used in the computation were \$436,704,790 and \$311,104,767, respectively.

Management believes that, under the current regulations, WSB will continue to meet its minimum capital requirements in the coming year; however, events beyond the control of WSB, such as an increase in interest rates or a downturn in the economy in areas where WSB has many of its loans could adversely affect future earnings and, consequently, the ability of WSB to meet its future minimum capital requirements.

### 13. INCOME TAXES

The provision for income taxes consists of the following:

	Years Ended July 31,		
	<u>2004</u>	<u>2003</u>	<u>2002</u>
Current taxes:			
Federal	\$ 5,263,902	\$ 4,368,993	\$ 2,698,553
State	<u>1,132,021</u>	<u>572,299</u>	<u>158,714</u>
	<u>6,395,923</u>	<u>4,941,292</u>	<u>2,857,267</u>
Deferred taxes (credit):			
Federal	(780,231)	(1,254,723)	(255,103)
State	<u>(167,792)</u>	<u>(277,769)</u>	<u>(34,664)</u>
	<u>(948,023)</u>	<u>(1,532,492)</u>	<u>(289,767)</u>
	<u>\$ 5,447,900</u>	<u>\$ 3,408,800</u>	<u>\$ 2,567,500</u>

The provision for income taxes differs from that computed at the statutory corporate tax rate as follows:

	Years Ended July 31,					
	<u>2004</u>	Percent of <u>Pretax Income</u>	<u>2003</u>	Percent of <u>Pretax Income</u>	<u>2002</u>	Percent of <u>Pretax Income</u>
Tax at statutory rate	\$ 5,017,492	35.0 %	\$ 3,721,585	34.0 %	\$ 2,424,915	34.0 %
Increases (decreases):						
State income tax net of federal income tax benefit	430,408	3.0	198,575	1.8	142,585	2.0
Excess fair market value of donated property	<u>-</u>	<u>0.0</u>	<u>(511,360)</u>	<u>(4.7)</u>	<u>-</u>	<u>-</u>
	<u>\$ 5,447,900</u>	<u>38.0 %</u>	<u>\$ 3,408,800</u>	<u>31.1 %</u>	<u>\$ 2,567,500</u>	<u>36.0 %</u>

Deferred income tax assets and liabilities reflect the net tax effects of temporary differences between the financial reporting and the tax bases of assets and liabilities pursuant to SFAS No. 109.

The components of net deferred tax assets as of July 31, 2004 and 2003 are as follows:

	<u>July 31,</u>	
	<u>2004</u>	<u>2003</u>
Deferred tax assets:		
Deferred loan fees	\$ 2,165,691	\$ 1,291,441
Allowance for loan losses	1,352,986	862,905
Allowance for losses on real estate acquired in settlement of loans	-	15,448
Deferred compensation	132,752	516,752
Depreciation	<u>58,731</u>	<u>80,776</u>
	<u>3,710,160</u>	<u>2,767,322</u>
Deferred tax liabilities:		
Other	37,117	50,488
Unrealized appreciation on available for sale securities	16,061	8,798
Deferred rental income	<u>40,976</u>	<u>32,790</u>
	<u>94,154</u>	<u>92,076</u>
Net deferred tax assets	<u>\$ 3,616,006</u>	<u>\$ 2,675,246</u>

For federal income tax purposes, WSB through fiscal year 1996 was allowed to compute a bad debt deduction based on a percentage of taxable income before such deduction. The deduction was 8% of taxable income subject to certain limitations based on aggregate loan and savings accounts at the end of the year. If the amounts that qualify as deductions for federal income tax purposes are later used for purposes other than to absorb loan losses, they will be subject to federal income tax at the then-current corporate rate.

On August 20, 1996, federal legislation repealed the special bad debt reserve method for thrift institutions previously provided for in Section 593 of the Internal Revenue Code. The new law repeals the percentage of taxable income bad debt method that was previously available to thrift institutions. Under the new law, thrift institutions that qualify as small banks are allowed to utilize the experience method applicable to such institutions, while thrift institutions that are treated as large banks (generally, assets of over \$500 million) are required to use the specific charge-off method. The provision also required thrifts to recapture any reserves accumulated after 1987 but forgave taxes owed on reserves accumulated prior to 1988. Thrift institutions were given six years to account for any excess reserves that need to be recaptured, beginning with the first taxable year after December 31, 1995. Implementation of this law required WSB to recapture excess tax reserves arising after 1987. The final year of this recapture was fiscal 2003.

#### 14. FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK

WSB is a party to financial instruments with off-balance-sheet risk in the normal course of its business to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit, standby letters of credit, and financial guarantees.

These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the statement of financial position. The contract or notional amounts of those instruments reflect the extent of involvement WSB has in particular classes of financial instruments.

WSB's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit, standby letters of credit, and financial guarantees written is represented by the contractual notional amount of those instruments. WSB uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Unless noted otherwise, WSB does not require collateral or other security to support financial instruments with credit risk.

	<b>July 31, 2004</b>	<b>July 31, 2003</b>
	<b>Contract or</b>	<b>Contract or</b>
	<b>Notional Amount</b>	<b>Notional Amount</b>
Financial instruments whose contract amounts represent credit risk:		
Commitments to grant mortgage loans	\$ 11,968,990	\$ 18,908,165
Standby letters of credit and financial guarantees written	\$ 1,268,814	\$ 568,042
Financial instruments whose notional or contract amounts exceed the amount of credit risk:		
Forward contracts to sell mortgage loans	\$ 14,696,830	\$ 97,901,757

Commitments to grant mortgage loans, which include pending applications, are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, or pending applications will be denied, the total commitment amounts do not necessarily represent future cash requirements. Historically, approximately seventy-five percent of the agreements and pending applications are drawn upon. WSB evaluates each customer's credit-worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by WSB upon extension of credit, is based on management's credit evaluation of the counterparty.

Standby letters of credit and financial guarantees written are conditional commitments issued by WSB to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support construction borrowing. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

WSB holds cash as collateral supporting those commitments for which collateral is deemed necessary.

Forward contracts are for delayed delivery of loans in which the purchaser/seller agrees to accept/make delivery at a future date of a specified instrument, at a specified price or yield. Risks arise from the possible inability of counterparties to meet the terms of their contracts and from movements in interest rates.

## 15. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following disclosures of the estimated fair value of financial instruments are made in accordance with the requirements of SFAS No. 107, "Disclosures about Fair Value of Financial Instruments." The estimated fair value amounts have been determined by WSB using available market information and appropriate valuation methodologies. However, considerable judgment is required in interpreting market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts WSB could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

	July 31, 2004		July 31, 2003	
	Carrying Amount (000's)	Estimated Fair Value (000's)	Carrying Amount (000's)	Estimated Fair Value (000's)
<b>Assets:</b>				
Cash and cash equivalents	\$ 12,979	\$ 12,979	\$ 14,447	\$ 14,447
Loans receivable, net	480,718	481,235	393,071	392,485
Mortgage-backed securities:				
Available for sale	2,155	2,155	842	842
Held to maturity	-	-	-	-
Investment securities:				
Available for sale	-	-	-	-
Held to maturity	5,588	5,663	6,369	6,224
Investment in Federal Home Loan Bank stock	4,495	4,495	4,095	4,095
<b>Liabilities:</b>				
Deposits:				
Noninterest-bearing	10,346	10,346	7,007	7,007
Interest bearing	367,939	368,110	284,939	288,962
Other borrowings	89,900	93,030	96,331	101,432

*Cash and Cash Equivalents* - For cash and cash equivalents, the carrying amount is a reasonable estimate of fair value.

*Loans Receivable, Net* - Loans not having quoted market prices are priced using the discounted cash flow method. The discount rate used is the rate currently offered on similar products. The estimated fair value of loans held for sale is based on the terms of the related sale commitments.

*Mortgage-Backed Securities* - Fair values are based on quoted market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

*Investment Securities* - Fair values are based on quoted market prices or dealer quotes. If a quoted market price is not available, fair values are estimated using quoted market prices for similar securities.

*Investment in Federal Home Loan Bank Stock* - The carrying amount of Federal Home Loan Bank (FHLB) Stock is a reasonable estimate of fair value as FHLB stock does not have a readily available market and can only be sold back to the FHLB at its par value of \$100 per share.

*Deposits* - The fair value of non-interest bearing accounts is the amount payable on demand at the reporting date. The fair value of interest-bearing deposits is determined using the discounted cash flow method. The discount rate used is the rate currently offered on similar products.

*Commitments to Grant Loans and Standby Letters of Credit and Financial Guarantees Written* - The majority of WSB's commitments to grant loans and standby letters of credit and financial guarantees written carry current market interest rates if converted to loans. Because commitments to extend credit and letters of credit are generally unassignable by either WSB or the borrower, they only have value to WSB and the borrower and therefore it is impractical to assign any value to these commitments.

The fair value estimates presented herein are based on pertinent information available to management as of July 31, 2004 and 2003. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively reevaluated for purposes of these financial statements since that date and, therefore, current estimates of fair value may differ significantly from the amounts presented herein.

## 16. QUARTERLY DATA (Unaudited)

Summarized quarterly financial information is as follows (amounts in thousands except per share information):

<b>Year Ended July 31, 2004:</b>	<b>First Quarter</b>	<b>Second Quarter</b>	<b>Third Quarter</b>	<b>Fourth Quarter</b>
Interest income	\$ 7,422	\$ 7,508	\$ 8,154	\$ 9,327
Interest expense	2,914	2,828	2,954	3,353
Net interest income	4,508	4,680	5,200	5,974
Provision for loan losses	60	120	180	1,035
Net interest income after provision for loan losses	4,448	4,560	5,020	4,939
Earnings before income taxes	3,126	3,142	4,311	3,757
Provision for income taxes	1,159	1,198	1,651	1,440
Net earnings	1,967	1,944	2,660	2,317
Basic earnings per common share	0.28	0.28	0.37	0.32
Diluted earnings per common share	0.25	0.24	0.33	0.29
<b>Year Ended July 31, 2003:</b>	<b>First Quarter</b>	<b>Second Quarter</b>	<b>Third Quarter</b>	<b>Fourth Quarter</b>
Interest income	\$ 5,641	\$ 6,185	\$ 6,006	\$ 6,843
Interest expense	2,881	2,908	2,676	2,759
Net interest income	2,760	3,277	3,330	4,084
Provision for loan losses	90	90	90	995
Net interest income after provision for loan losses	2,670	3,187	3,240	3,089
Earnings before income taxes	1,955	2,861	2,968	3,161
Provision for income taxes	141	1,024	1,081	1,163
Net earnings	1,814	1,837	1,887	1,999
Basic earnings per common share	0.26	0.27	0.27	0.29
Diluted earnings per common share	0.24	0.24	0.25	0.25

\* \* \* \*

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.**

None.

**Item 9A. Controls and Procedures**

(a) WSB's Chief Executive Officer and Principal Financial Officer have evaluated the effectiveness of the design and operation of WSB's disclosure controls and procedures (as defined under Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based upon that evaluation, WSB's Chief Executive Officer and Principal Financial Officer have concluded that WSB's disclosure controls and procedures are adequate and effective.

(b) There were no changes in WSB's internal control over financial reporting in connection with the evaluation required by paragraph (d) of Rules 13a-15 or 15d-15 under the Exchange Act the occurred during the fourth quarter that have materially affected, or are reasonably likely to materially affect, WSB's internal control over financial reporting.

**Item 9B. Other Information**

None.

**PART III**

**Item 10. Directors and Executive Officers of the Registrant**

The text and tables under "Election of Board of Directors" and Section 16(a) Beneficial Ownership Reporting Compliance in WSB's 2004 Proxy Statement are incorporated herein by reference.

WSB has adopted a code of ethics that covers the chief executive officer, the chief financial officer, the chief accounting officer, controller, and any person serving in an equivalent position regardless of whether or not they are designated as executive officer for Regulation O purposes. WSB maintains a copy of this code on its Internet web site. The address of WSB's Internet website is [www.twsb.com](http://www.twsb.com). If WSB makes any substantive amendments to this Code of Ethics or grants any waiver from a provision of this Code, WSB will disclose the nature of such amendment or waiver on WSB's website or in a report on Form 8-K.

WSB has a separately designated audit committee. The members of WSB's audit committee are Messrs. Sullivan (Chairman), Conover, Troese and Lodge.

WSB is required to disclose whether it has an "audit committee financial expert," as defined in Item 401(h) of Regulation S-K of the Securities Exchange Act of 1934, serving on its audit committee. WSB's Board of Directors has not yet identified or nominated an appropriate director nominee to serve as the audit committee financial expert. Each of the members of the Audit Committee currently meets the independence and experience requirements of the American Stock Exchange listing standards and WSB's Audit Committee charter. To the extent

that the Audit Committee determines its needs additional financial expertise pending nomination of an audit committee financial expert, it intends to seek the assistance of a consultant with appropriate experience.

**Item 11. Executive Compensation**

The text and tables under "Executive Compensation" in WSB's 2004 Proxy Statement are incorporated herein by reference.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

(a) Except as indicated in the 2004 Proxy Statement, WSB knows of no person who on October 8, 2004, owned beneficially more than 5% of its Common Stock.

(b) The stock ownership information contained in the text and tables under "Securities Beneficially Owned" in WSB's 2004 Proxy Statement is incorporated herein by reference.

(c) WSB knows of no arrangements the operation of which may at a subsequent date result in a change of control of WSB.

(d) See "Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchase of Equity Securities -Equity Compensation Plan Information." in Part II Item 5 of this report.

**Item 13. Certain Relationships and Related Transactions**

The text under "Executive Compensation -- Certain Transactions with Management and Others" in WSB's 2004 Proxy Statement is incorporated herein by reference.

**Item 14. Principal Accounting Fees and Services**

The text under "Independent Auditors -- Summary of the fees billed to WSB by Stegman & Company for professional services and the Policy on Audit Committee Pre-Approval of Audit Services and Permissible Non-Audit Services of Independent Auditors" in WSB's 2004 Proxy Statement is incorporated herein by reference.

**PART IV**

**Item 15. Exhibits and Financial Statement Schedules**

(a)(1) The following consolidated financial statements of WSB and its subsidiaries are included in Item 8:

Report of Independent Registered Public Accounting Firm

Consolidated Statements of Financial Condition—as of July 31, 2004 and 2003

Consolidated Statements of Earnings--Years ended July 31, 2004, 2003 and 2002

Consolidated Statements of Stockholders' Equity--Years ended July 31, 2004, 2003 and 2002

Consolidated Statements of Cash Flows--Years ended July 31, 2004, 2003 and 2002

Notes to Consolidated Financial Statements

(a)(2) Financial statements schedules--none applicable or required

(a)(3) The following is an index of the exhibits included in this report:

<u>Exhibit No.</u>	<u>Item</u>
3.1	- Amended and Restated Federal Stock Charter of WSB. (Incorporated by reference from WSB's Quarterly Report on Form 10-Q for the quarter ended January 31, 1997.)
3.2	- Amended and Restated By-Laws of WSB. (Incorporated by reference from WSB's Quarterly Report on Form 10-Q for the quarter ended January 31, 1997.)
3.3	- Certificate of Amendment to Federal Stock Charter of WSB. (Incorporated by reference from WSB's Definitive Proxy Statement filing for the year ended July 31, 2001, as filed on October 22, 2001.)
10.1	- Stock Option Plan for Non-Employee Directors of WSB. (Incorporated by reference from WSB's Definitive Proxy Statement filing for the year ended July 31, 1995, as filed on October 24, 1995.)
10.2	- 1997 Omnibus Stock Plan of WSB. (Incorporated by reference from WSB's Definitive Proxy Statement filing for the year ended July 31, 1997, as filed on October 22, 1997)
10.3	- 1999 Stock Option and Incentive Plan. (Incorporated by reference from WSB's Definitive Proxy Statement filing for the year ended July 31, 1999, as filed on October 20, 1999.)
10.4	- 2001 Stock Option and Incentive Plan. (Incorporated by reference from WSB's Definitive Proxy Statement filing for the year ended July 31, 2001, as filed on October 29, 2001.)
10.5	- Supervisory Agreement dated March 19, 2004 by and between The Washington Savings Bank, F.S.B. and The Office of Thrift Supervision (Incorporated by reference from WSB's Report on Form 8K filed on March 19, 2004).
14.1	- Code of Ethics for Senior Financial Officers (Incorporated by reference from WSB's Annual Report on Form 10-K for the year ended July 31, 2003, as filed on October 24, 2003.)
21	- Subsidiaries of WSB. (Incorporated by reference from Form OC of WSB, dated April 21, 1988 and FDIC letter dated December 17, 1999.)

- 23 - Consent of Registered Public Accounting Firm (filed herewith).
- 31.1 - Rule 13a-14(a)/15d – 14(a) Certifications of CEO (filed herewith).
- 31.2 - Rule 13a-14(a)/15d –14(a) Certifications of Principal Financial Officer (filed herewith).
- 32.1 - Section 1350 Certifications (furnished herewith).

\*The registrant will furnish to each beneficial holder requesting the same a copy of each exhibit referred to above upon the payment of a reasonable fee limited to WSB's reasonable expenses in furnishing such exhibits. Such request should be directed to the Assistant Secretary at WSB's principal executive offices.

No other exhibits are required to be filed.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE WASHINGTON SAVINGS BANK, F.S.B.  
(Registrant)

**October 22, 2004**

By: /s/ William J. Harnett  
William J. Harnett  
Chairman and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacity and on the dates indicated.

Principal Executive Officer:

**October 22, 2004**

By: /s/ William J. Harnett  
William J. Harnett  
Chairman and Chief Executive Officer

Principal Financial and Accounting Officer:

**October 22, 2004**

/s/ Carol A. Ramey  
Carol A. Ramey  
Vice President and Controller

A Majority of the Board of  
Directors:

**October 22, 2004**

/s/ George Q. Conover  
George Q. Conover

**October 22, 2004**

/s/ William J. Harnett  
William J. Harnett

**October 22, 2004**

/s/ Kevin P. Huffman  
Kevin P. Huffman

**October 22, 2004**

/s/ Eric S. Lodge  
Eric S. Lodge

**October 22, 2004**

/s/ John F. Motzer  
John F. Motzer

**October 22, 2004**

/s/ Michael J. Sullivan  
Michael J. Sullivan

**October 22, 2004**

/s/ Stephen J. Troese  
Stephen J. Troese

**RULE 13a-14(a)/15d – 14(a)**  
**CERTIFICATIONS OF CHIEF EXECUTIVE OFFICER**

I, William J. Harnett, the Chief Executive Officer of The Washington Savings Bank, F.S.B., certify that:

1. I have reviewed this annual report on Form 10-K of The Washington Savings Bank, F.S.B.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 22, 2004

By: /s/ William J. Harnett  
William J. Harnett  
Chief Executive Officer

**RULE 13a-14(a)/15d – 14(a)**  
**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER**

I, Carol A. Ramey, the Vice President and Controller of The Washington Savings Bank, F.S.B., certify that:

1. I have reviewed this annual report on Form 10-K of The Washington Savings Bank, F.S.B.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 22, 2004

By: /s/ Carol A. Ramey  
Carol A. Ramey  
Vice President and Controller

**Written Statement of Chief Executive Officer and Principal Financial Officer  
Pursuant to Section 906  
of the Sarbanes-Oxley Act of 2002  
(18 U.S.C. Section 1350)**

The undersigned, the Chief Executive Officer and the Principal Financial Officer of The Washington Savings Bank, F.S.B. (the “**Company**”), each hereby certifies that, to his knowledge, on the date hereof:

- (a) the Annual Report on Form 10-K of the Company for the fiscal year ended July 31, 2004 filed on the date hereof with the Office of Thrift Supervision (the “**Report**”) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (b) information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

By: /s/ William J. Harnett  
William J. Harnett  
Chief Executive Officer  
October 22, 2004

By: /s/ Carol A. Ramey  
Carol A. Ramey  
Vice President and Controller  
October 22, 2004

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Office of Thrift Supervision or its staff upon request.