ANNUAL REPORT

DECEMBER 31, 2002

Puget Sound Financial Services, Inc.
5209 Pacific Highway E
Fife, WA. 98424-2636
(253) 922-5100

Financial REVIEW

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FINANCIAL

Highlights

Years ended December 31 (in thousands except per share data)	2002*	2001*	2000	1999
Earnings				
Total interest income	$4,271	$4,244	$3,521	$2,097
Total interest expense	1,264	1,920	1,559	762
Net interest income	3,007	2,324	1,962	1,335
Net income	921	635	548	349
PER COMMON SHARE				
Basic earnings per share	$5.99	$3.98	$3.44	$2.21
Diluted earnings per share	$5.52	$3.71	3.34	2.18
Net book value	$32.84	$27.36	23.75	20.19
AT YEAR END				
Total Assets	$64,464	$52,168	$41,576	$29,389
Total loans	44,731	39,947	31,703	22,745
Allowance for credit losses	570	501	396	284
Total deposits	56,413	47,523	37,610	26,079
Common equity	4,979	4,282	3,815	3,219
KEY PERFORMANCE RATIOS				
Return on average equity	20.23%	15.99%	15.67%	11.57%
Return on average assets	1.65%	1.32%	1.53%	1.50%
Net interest margin	5.76%	5.12%	5.86%	6.19%
Average common equity to average assets	8.31%	8.53%	9.18%	10.95%
Non-performing assets to period-end loans	.07%	.13%	.16%	0%
Allowance for loan losses to period-end loans	1.27%	1.25%	1.25%	1.25%
Net charge-offs to average loans	.08%	.06%	0%	0%
Tier 1 capital	10.18%	10.42%	11.97%	13.67%
Total risk-based capital	11.35%	11.64%	13.21%	14.87%
Leverage ratio	8.06%	8.91%	9.40%	11.26%

* Results consolidated for the parent company Puget Sound Financial Services, Inc. and its wholly owned subsidiary Fife Commercial Bank.

Basis of Presentation

The following represents management's discussion and analysis of Puget Sound Financial Services, Inc ("the Company") financial condition as of December 31, 2002, 2001 and 2000 and its results of operations for the years ended December 31, 2002, 2001 and 2000. This discussion should be read in conjunction with the consolidated financial statements and related footnotes and the 3-year summary of selected financial data.

Overview

For the year ended December 31, 2002 the Company reported net income of $921 thousand, an increase of $286 thousand, or 45% from the $635 thousand earned during 2001. Diluted earnings per share were $5.52 compared to $3.71 in 2001. Return on average assets was 1.65% for 2002, compared with 1.32% for 2001. Return on average common stockholders' equity for 2002 and 2001 was 20.23% and 15.99% respectively.

For the years ended December 31, 2000 and 1999, the Company reported net income of $548 thousand and $349 thousand respectively. Diluted earnings per share were $3.34 for 2000 and $2.18 for 1999.

Total assets were $64.5 million, $52.2 million, $41.6 million and $29.4 million at December 31 2002, 2001, 2000 and 1999 respectively.

Results of Operations

The principal source of the Company's earnings is net interest income, the difference between total interest income on earning assets such as loans and investments, and interest paid on deposits and other interest-bearing liabilities. The net interest margin is net interest income expressed as a percentage of average earning assets. The margin is affected by volume and mix of earning assets and interest-bearing liabilities, the level of interest free funding sources, interest rate environment and income tax rates. As discussed later, management actively monitors its interest rate sensitivity and seeks to balance assets and liabilities to minimize the impact of changes in the interest rate environment.

The table on the following page presents the Company's average balance sheets, interest earned or paid and the related yields and rates on major categories of the Company's earning assets and interest bearing liabilities on a tax equivalent basis for the periods indicated.

Net interest income for 2002 was $3.007 million, a $683 thousand increase from $2.324 million in 2001. The increase was primarily due to a 15.3% increase in average earning assets and a 64 basis point increase in the net interest margin. Net interest income in 2000 and 1999 was $1.962 million and $1.335 million respectively.

The net interest margin was 5.76%, 5.12%, 5.86% and 6.19% in 2002, 2001, 2000 and 1999 respectively. The decrease in margin from 1999 through 2001 was due to the asset sensitive position of the balance sheet compounded by a very rapid decrease in interest rates brought about through Federal Reserve policy decisions. Margins improved in 2002 aided by stable rates, and a shift to a slightly liability sensitive balance sheet. The Federal Reserve through its Federal Open Market Committee (FOMC) voted to decrease short term interest rates a total of 11 times in 2001 and again in November 2002. The target federal funds rate decreased from 6.50% in December 2000 to 1.75% at December 31, 2001 and 1.25% in November 2002.

Table of Average Balances, Interest Earned or Paid and Related Yields and Rates

Years ended December 31	2002			2001			2000		
(Dollars in thousands)	Avg Balance	Interest	Yields & Rates	Avg Balance	Interest	Yields & Rates	Avg Balance	Interest	Yields & Rates
Assets									
Loans [1] [2]	$41,804	$3,933	9.4%	$35,404	$3,742	10.6%	$27,869	$3,147	11.3%
Investment Securities [2]	3,573	168	4.7%	1,775	114	6.4%	685	51	7.4%
Other Earning Assets	7,017	181	2.6%	8,252	388	4.7%	5,042	323	6.4%
Total Earning Assets	52,394	4,282	8.2%	45,431	4,244	9.3%	33,596	3,521	10.5%
Non-interest Earning Assets	3,461			2,594			2,220		
Total Assets	55,855			48,025			35,816		
Liabilities & Shareholders' Equity									
Interest-bearing Checking & Savings	14,858	282	1.9%	9,735	350	3.6%	7,371	348	4.72%
Other Interest-bearing Obligations	1,460	61	4.1%	0	0	0	0	0	0
Time Deposits	26,022	921	3.5%	27,266	1,570	5.8%	19,586	1,211	6.2%
Total Interest-bearing Liabilities	42,340	1,264	2.9%	37,001	1,920	5.2%	26,957	1,559	5.8%
Demand Deposits	8,298			6,435			5,007		
Non-interest-bearing Liabilities	577			490			343		
Common Shareholders' Equity	4,640			4,099			3,509		
Total Liabilities & Shareholders' Equity	55,855			48,025			35,816		
Net Interest Income		3,018			2,324			1,962	
Net Interest Margin			5.76%			5.12%			5.86%

(1) Includes non-accrual loans and loan fees.

(2) Interest yields on loans and investments are presented on a tax equivalent basis to reflect the tax-exempt nature of certain assets.

Provision for Credit Losses

Annual fluctuations in the provision for credit losses result from management's regular assessment of the adequacy of the allowance for credit losses. The provision for credit losses for 2002 was $102 thousand, a decrease of $26 thousand, or 20.3% from the $128 thousand provision during 2001. The provision for 2000 and 1999 was $112 thousand and $140 thousand respectively. The amount of the credit loss provision to be recorded in future periods will depend on management's assessment of the adequacy of the allowance for loan losses in relation to the entire loan portfolio.

Non-interest Income

The primary sources of non-interest income consists of service charges on deposit accounts, certain other transaction related fee income and merchant processing income. Non-interest income for 2002 was $199 thousand, an increase of $13 thousand,

or 6.9% from the $186 thousand earned in 2001. The increase was principally due to an increase in fees received from the brokerage of mortgage loans through the Banks mortgage company. Fife Mortgage generated approximately $37 thousand in brokerage fees during 2002. Non-interest income for 2000 and 1999 was $141 thousand and $98 thousand respectively.

Non-interest Expense

Non-interest expense consists of salaries and benefits, occupancy, equipment and other expenses such as professional, telephone, data processing and regulatory expenses necessary for the operation of the Company. Management is committed to improving the quality of services while controlling such costs through improved efficiency. The following table presents the components of non-interest expenses for the periods indicated:

Years Ended December 31 (in thousands)	2002	2001	2000
Salaries and Employee Benefits	$980	$786	$678
Data Processing	139	127	115
Occupancy	39	33	32
Furniture & Equipment	79	81	59
Audit & Legal	62	56	55
FDIC Insurance	10	7	6
Other	389	324	213
Total Non-interest Expense	$1,698	$1,414	$1,158

Non-interest expense increased $284 thousand to $1.7 million, or 20.1% in 2002. The increase was principally due to an increase in salaries and employee benefits. Other non-interest expenses increased $65 thousand to $389 thousand, or 20.1%. Non-interest expense for 2000 was $1.2 million. Non-interest expense for 1999 was $898 thousand.

Provision for Income Taxes

The Company records a provision for income taxes currently payable and for taxes payable in the future because of differences in the timing of recognition of certain items for financial statement and income tax purposes. The effective tax rate was 34.5%, 34.4%, 34.2%, and 9.6% for 2002, 2001, 2000, and 1999 respectively.

The effective tax rate for 1999 was below statutory rates due to the application of loss carry-forwards.

FINANCIAL CONDITION

INVESTMENT OF FUNDS

Loans

At December 31, 2002, total loans were $44.7 million, an increase of $4.7 million, or 12%, from the December 31, 2001 level of $39.9 million. A significant portion of this increase is attributable to loan growth in the Company's existing markets.

General. The Company's loan mix remained relatively constant from 2000 to 2001. Real estate loans continued to be the largest category of loans, representing 61% of the total loan portfolio.

Real Estate Loans. The Company's real estate portfolio is fairly evenly divided between residential 1-4 family, commercial and construction loans. As of December 31, 2002, 36% or $9.9 million were secured by residential 1-4 family, 35% or $9.5 million were commercial real

estate and 29%, or $8.1 million were real estate construction loans.

Commercial Loans. Loans in this category include loans to retail, wholesale, manufacturing and service businesses. Commercial loans are underwritten based on the financial strength and repayment ability of the borrower, as well as the collateral securing the loans.

Consumer Loans. Loans classified as consumer include automobile, personal loans, consumer lines of credit and overdrafts. The majority of these are installment loans with fixed interest rates. The following table presents the Company's balance of each major loan category at the dates indicated:

	2002		2001		2000	
(Dollars in thousands)	Amount	Percent of Total Loans	Amount	Percent of Total Loans	Amount	Percent of Total Loans
Loan Category:						
Residential 1-4 Family	$ 9,885	22.1%	$ 9,259	23.2%	$7,013	22.1%
Commercial Real Estate	9,467	21.2%	10,768	26.9%	7,566	23.9%
Real Estate Construction	8,084	18.1%	6,772	17.0%	5,705	18.0%
Commercial	15,525	34.7%	11,392	28.5%	9,736	30.7%
Consumer	1,770	3.9%	1,756	4.4%	1,683	5.3%
Total Loans	$44,731	100.0%	$39,947	100.0%	$31,703	100.0%
Less Allowance for Credit Losses	<570>		<501>		<396>	
Total	$44,161		$39,446		$31,307	

Investments. Management maintains a high quality investment portfolio oriented towards U.S. government agency and government guaranteed mortgage-backed securities. Other invested funds consist of short-term investments in federal funds sold and FDIC insured certificates of deposits. The investments provide opportunity to structure maturities and re-pricing timetables in a flexible manner and to meet applicable requirements for pledging securities, as tools in managing its interest rate exposure and enhancing its net interest margin.

The Company's investments designated available for sale, increased $2.7 million, or 152.6% to $4.4 million at December 31, 2002, from $1.8 million at December 31, 2001. On December 31, 2002 the Company's invested funds represented 22.7% of total assets, compared to 18.1% at December 31, 2001.

Credit Policy. The Company's lending activities are guided by the general loan policies established by the Board of Directors. The Loan Committee of the Company has established loan approval limits for each loan officer of the Company. The limits established for the Company range from $25 thousand to $150, 000 per borrower. Amounts in excess of the individual lending authority are presented to the Company's Loan Committee for approval.

Although the Company has a diversified loan portfolio, the economic health of the Company's primary market area may impact the ability of many of the bank's borrowers to repay their loans. The Company has identified and implemented strategies to deal with these factors, including an emphasis on quality local loan growth and the diversification and performance of its earning asset portfolios.

Non-performing Assets. The Company follows regulatory guidelines with respect to classifying loans on a non-accrual basis. Loans are placed on non-accrual when they become past due over 90 days or when the collection of interest or principal is considered unlikely. The Company does not return a loan to accrual status until it is brought current with respect to both principal and interest and future principal payments are no longer in doubt. When a loan is placed on non-accrual status, any previously accrued and uncollected interest and late charges are reversed.

The Company considers non-performing assets to include all non-accrual loans, restructured loans defined as troubled debt restructurings under SFAS No. 15 and other real estate owned ("OREO").

Non-performing assets were $32 thousand at December 31, 2002 versus $54 thousand at December 31, 2001. The ratio of non-performing assets to total assets at December 31, 2001 was 0.05%.

Allowance for Credit Losses

The current level of the allowance for credit losses is the result of management's assessment of the risks within the portfolio based on the information revealed in credit reporting processes. The Company utilizes a risk rating system on all loans, including purchased loans, and a monthly credit review and reporting process that results in the calculation of the guideline reserves based on the risk within the portfolio. This assessment of risk takes into account the composition of the loan portfolio, previous loan experience, current economic conditions and other factors that, in management's judgment, deserve recognition.

The allowance is allocated to individual loan categories based on the relative risk characteristics of the loan portfolios. Loan category allocations are based on a monthly review of the individual loans outstanding, including outstanding commitments to lend, performance of the respective portfolios, including historical and expected delinquency and charge-off statistics. The allocated allowance increased $69 thousand from $501 thousand at December 31, 2001 to $570 thousand at December 31, 2002.

Source of Funds

Deposits

The Company's major source of funds is provided by core deposits from individuals, businesses and local government units. Core deposits consist of all non-interest-bearing deposits, interest-bearing checking and savings accounts and time deposits of less than $100,000.

The following table sets forth a summary of the deposits of the Company at the dates indicated.

December 31, (Dollars in thousands)	2002	2001	2000
Non-interest bearing	$11,552	$ 7,433	$5,375
Interest-bearing			
Savings & Checking	18,998	11,443	8,143
Time Accounts < $100,000	13,731	15,647	14,870
Time Accounts > $100,000	12,132	13,000	9,222
Total Deposits	$56,413	$47,523	$37,610

Total deposits at December 31, 2002 were $56.4 million, an increase of $8.9 million, or 18.7% from $47.5 million at December 31, 2001. The Company's core deposits as a percentage of total deposits were 78.5% and 72.6% as of December 31, 2002 and December 31,

2001 respectively. At December 31, 2002, $12.1 million or 21.5% of total deposits were in time accounts greater than $100,000. Maturities of time deposits at December 31, 2002 were (in thousands):

Maturing in 2003	$25,017
Maturing in 2004	$ 670
Maturing in 2005	$ 176
Maturing in 2006 and thereafter	$ 0

Shareholders' Equity

Total shareholders' equity increased $697 thousand, or 16.3% to $4.98 million at December 31, 2002, from $4.28 million at December 31, 2001, as a result of the retention of earnings and the issuance & repurchase of common stock. During 2002 a total of 50 shares of common stock were issued, resulting in an increase in shareholders' equity of $2 thousand. During 2002 a total of 4,967 shares of common stock were repurchased, resulting in a decrease in shareholders' equity of $260 thousand.

ASSET/LIABILITY MANAGEMENT

Liquidity Management

Liquidity management is an effort of management to provide a continuing flow of funds to meet its financial commitments, customer borrowing needs and deposit withdrawal requirements. The liquidity position of the Company is monitored by the Asset/Liability Committee of the Company. The largest category of assets representing a ready source of liquidity for the company is its short-term financial instruments, which include federal funds sold, interest-bearing deposits at other financial institutions and U.S. government agency securities maturing within one year.

Liquidity is also provided through the regularly scheduled maturities of assets. The investment portfolio contains a number of high quality issues with varying maturities and regular principal payments. Maturities in the loan portfolio also provide a steady flow of funds and strict adherence to the credit policies of the Company helps ensure the collectibility of these loans. The liquidity position of the Company is also greatly enhanced by its significant base of core deposits.

The liquidity ratio is one measure of a bank's ability to meet its current obligations and is defined as the percentage of liquid assets to deposits. Liquid assets include cash and due from banks, un-pledged investment securities with maturities of less than one year and federal funds sold. At year-end 2002, 2001, 2000, 1999 and 1998, the liquidity ratio was 37.9%, 32.1%, 24.1%, 23.0% and 23.2% respectively.

The Company also maintains available lines of federal funds borrowings, as well as seasonal borrowing privileges at the Federal Reserve Bank of San Francisco. The Company has the ability to borrow up to $2 million in federal funds from one non-affiliated financial institution.

Additionally, the Company has joined the Federal Home Loan Bank of Seattle ("FHLB"). As part of the membership, the Company purchased a modest amount of stock of FHLB and obtained advance lines of credit, which represent $6.4 million in additional funding capacity at December 31, 2002.

Interest Rate Sensitivity

Interest rate sensitivity indicates the exposure of a financial institution's earnings to future fluctuations in interest rates. Management of interest rate sensitivity is accomplished through the composition of loans and investments and by adjusting the maturities on earning assets and interest-bearing liabilities. Rate sensitivity and liquidity are related since both are affected by maturing assets and liabilities. However, interest rate sensitivity also takes into consideration those assets and liabilities with interest rates that are subject to change prior to maturity.

The Company's Asset and Liability Committee ("ALCO") attempts to structure the Company's balance sheet to provide for an approximately equal amount of rate sensitive assets and rate sensitive liabilities. In addition to facilitating liquidity needs, this strategy assists management in maintaining relative stability in net interest income despite unexpected fluctuations in interest rates. ALCO uses three methods for measuring and managing interest rates risk: Re-pricing Mismatch Analysis, Balance Sheet Simulation Modeling and Equity Fair Value Modeling.

Re-pricing Mismatch Analysis – Management performs a Re-pricing Mismatch ("Gap Analysis") analysis, which represents a point in time net position of assets and liabilities. Guidelines established by ALCO, and approved by the Company's Board of Directors, limit the impact on net interest income to 5% given a 100 basis point change in interest rates over one year. However, management believes Gap Analysis alone does not accurately measure the magnitude of changes in net interest income since changes in interest rates do not impact all categories of assets and liabilities equally or simultaneously.

Balance Sheet Simulation Modeling – Balance Sheet Simulation Modeling allows management to analyze the impact of short-term (less then 12 months) interest rate fluctuations using projected balance sheet information. The balance sheet changes are based on forecasted re-payments of loans and securities, growth in loans and deposits, and historical pricing spreads. Management uses the model to simulate the impact of immediate and longer-term shifts in the yield curve. The results of these models are reviewed by ALCO and used to develop the Company's strategies. Guidelines established by ALCO limit the impact on net interest income to 5% given a 100 basis point change in interest rates. As of December 31, 2002, the impact of such a change in interest rates would be approximately 1.2% of net interest income.

Equity Fair Value Modeling – Because Balance Sheet Simulation Modeling is dependent on accurate forecasts, its usefulness is limited to periods of one year or less. As a result, the Company uses the Equity Fair Value Modeling to measure long-term interest rate exposure. The method estimates the impact of interest rate changes on the estimated discounted future cash flows of the Company's current assets and liabilities. Guidelines established by ALCO limit the change in fair value to 5% given a 100 basis point change in interest rates. As of December 31, 2002, the impact of such a change in interest rates would be approximately 8% of equity fair value.

Based on each of these methods of measuring interest rate risk, management believes the Company is liability sensitive as of December 31, 2002 for periods of 12 months or less.

The Company does not engage in speculative use of derivative financial instruments.

Capital Management

Risk-based guidelines established by regulatory agencies require the Company to maintain minimum amounts and ratios of total and Tier 1 capital to risk-weighted assets, and of Tier 1 capital to average assets.

As of December 31, 2002, the Company is considered well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Company must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 Leverage ratios as set forth in the table on the following page.

Regulatory Capital Requirements			
(Dollars in thousands)	Tier 1 Capital	Total Risk-based Capital	Leverage
Minimum	4.00%	8.00%	4.00%
Well Capitalized	6.00%	10.00%	5.00%
Puget Sound Financial Services, Inc.			
12/31/2002	10.18%	11.35%	8.06%
12/31/2001	10.42%	11.64%	8.91%
12/31/2000	11.97%	13.21%	9.40%
12/31/1999	13.67%	14.87%	11.26%

Due to the Company's level of Tier 1 capital and substantial level of earning assets invested in low risk government agency, mortgage-backed securities and interest-bearing deposit accounts, the Company's risk-based capital ratios significantly exceed the regulatory minimums. The Company conducts an ongoing assessment of its capital needs in order to maintain an adequate level of capital to support business growth to ensure depositor protection and to facilitate corporate expansion.

This annual report contains forward-looking statements under the Private Securities Litigation Reform Act of 1995 that are subject to certain risks and uncertainties that could cause actual results to differ materially from historical earnings and those presently anticipated or projected. The Company wishes to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. Factors that could cause actual results to differ from the results discussed in the forward-looking include but are not limited to: risks related to loans and investments, including dependence on local economic conditions; competition for the Company's customers from other providers of financial services; possible adverse effects of changes in interest rates, and other risks, which risks are difficult to predict and many of which are beyond the control of the Company.

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Report

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McGladrey & Pullen
Certified Public Accountants

Independent Auditor's Report

Board of Directors
Puget Sound Financial Services, Inc.
Fife, Washington

We have audited the accompanying consolidated balance sheets of **Puget Sound Financial Services, Inc. and Subsidiary** as of December 31, 2002 and 2001, and the related consolidated statements of income, shareholders' equity and cash flows for the years then ended. 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 auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. 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 **Puget Sound Financial Services, Inc. and Subsidiary** as of December 31, 2002 and 2001, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Our audits were made for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The supplementary information is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. Such supplementary information has been subjected to the auditing procedures applied in the audits of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

McGladrey & Pullen, LLP

Tacoma, Washington
January 17, 2003

McGladrey & Pullen, LLP is an independent member firm of RSM International, an affiliation of independent accounting and consulting firms.

Consolidated

Financial

Statements

Consolidated Balance Sheets

(Dollars in Thousands)

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

	2002	2001
Assets		
Cash and due from banks	$ 3,343	$ 1,876
Interest bearing deposits at other financial institutions	7,470	5,631
Federal funds sold	2,565	1,955
Securities available for sale	4,444	1,759
Federal Home Loan Bank stock, at cost	170	76
Loans	44,731	39,947
Less allowance for credit losses	570	501
Net loans	**44,161**	**39,446**
Premises and equipment	948	969
Accrued interest receivable	303	240
Foreclosed real estate	- -	54
Bank owned life insurance	1,002	- -
Other assets	58	162
Total assets	**$64,464**	**$52,168**
Liabilities and Shareholders' Equity		
Liabilities		
Deposits:		
Demand	$11,552	$ 7,433
Savings and interest-bearing demand	18,998	11,443
Time	25,863	28,647
Total deposits	**56,413**	**47,523**
Accrued interest payable	26	53
Long-term borrowings	2,700	- -
Other liabilities	346	310
Total liabilities	**59,485**	**47,886**
Commitments and Contingencies	**- -**	**- -**
Shareholders' Equity		
Preferred stock (no par value); authorized 100,000 shares; no shares issued	- -	- -
Common stock (par value: $1); authorized 2,000,000 shares; issued and outstanding: 2002 - 151,594 shares; 2001 - 156,511 shares	151	156
Additional paid-in capital	2,637	2,890
Retained earnings	2,153	1,232
Accumulated other comprehensive income	38	4
Total shareholders' equity	**4,979**	**4,282**
Total liabilities and shareholders' equity	**$64,464**	**$52,168**

See notes to consolidated financial statements.

Consolidated Statements of Income

(Dollars in Thousands, Except Per Share Amounts)

Puget Sound Financial Services, Inc. and Subsidiary
Years Ended December 31, 2002 and 2001

	2002	2001
Interest Income		
Loans	$3,933	$3,742
Federal funds sold and deposits in banks	181	388
Securities available for sale	149	109
Stock dividends	8	5
Total interest income	**4,271**	**4,244**
Interest Expense		
Deposits	1,203	1,920
Long-term borrowings	61	- -
Total interest expense	**1,264**	**1,920**
Net interest income	**3,007**	**2,324**
Provision for Credit Losses	102	128
Net interest income after provision for credit losses	**2,905**	**2,196**
Non-Interest Income		
Service charges on deposit accounts	141	157
Net gain on sales of securities available for sale	17	1
Other operating income	41	28
Total non-interest income	**199**	**186**
Non-Interest Expense		
Salaries and employee benefits	980	786
Occupancy	39	33
Furniture and equipment	79	81
Data processing	139	127
Other	461	387
Total non-interest expense	**1,698**	**1,414**
Income before income taxes	**1,406**	**968**
Income Taxes	485	333
Net income	**$ 921**	**$ 635**
Earnings Per Share		
Basic	$5.99	$3.98
Diluted	5.52	3.71

See notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

(Dollars in Thousands)

Puget Sound Financial Services, Inc. and Subsidiary
Years Ended December 31, 2002 and 2001

	Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance at December 31, 2000	160,613	$160	$3,063	$ 597	($ 5)	$3,815
Comprehensive income:						
Net income	- -	- -	- -	635	- -	635
Other comprehensive income, net of tax:						
Change in fair value of securities	- -	- -	- -	- -	9	9
Comprehensive income						**644**
Stock issued for directors' compensation	298	- -	10	- -	- -	10
Stock repurchased	(4,400)	(4)	(183)	- -	- -	(187)
Balance at December 31, 2001	**156,511**	**156**	**2,890**	**1,232**	**4**	**4,282**
Comprehensive income:						
Net income	- -	- -	- -	921	- -	921
Other comprehensive income, net of tax:						
Change in fair value of securities	- -	- -	- -	- -	34	34
Comprehensive income						**955**
Options exercised	50	- -	2	- -	- -	2
Stock repurchased	(4,967)	(5)	(255)	- -	- -	(260)
Balance at December 31, 2002	**151,594**	**$151**	**$2,637**	**$2,153**	**$38**	**$4,979**

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(Dollars in Thousands)

Puget Sound Financial Services, Inc. and Subsidiary
Years Ended December 31, 2002 and 2001

	2002	2001
Cash Flows from Operating Activities		
Net income	$ 921	$ 635
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	102	128
Depreciation	86	69
Deferred income tax	48	17
Gain on sales of securities available for sale	(17)	(1)
Stock dividends received	(8)	(5)
Increase in accrued interest receivable	(63)	(9)
Increase (decrease) in accrued interest payable	(27)	40
Amortization of premium on securities available for sale	31	- -
Other, net	77	51
Net cash provided by operating activities	**1,150**	**925**
Cash Flows from Investing Activities		
Net increase in interest bearing deposits at other financial institutions	(1,839)	(1,550)
Net increase in federal funds sold	(610)	(280)
Activity in securities available for sale:		
Proceeds from sales	519	182
Maturities, prepayments and calls	3,607	1,444
Purchases	(6,764)	(2,303)
Purchases of Federal Home Loan Bank stock	(95)	- -
Net increase in loans made to customers	(4,817)	(8,321)
Purchases of premises and equipment	(72)	(120)
Proceeds from the sale of foreclosed real estate	56	- -
Purchase of bank owned life insurance	(1,000)	- -
Net cash used in investing activities	**(11,015)**	**(10,948)**
Cash Flows from Financing Activities		
Net increase in deposits	8,890	9,913
Proceeds from long-term borrowings	2,700	- -
Exercise of stock options	2	- -
Repurchase of common stock	(260)	(187)
Net cash provided by financing activities	**11,332**	**9,726**
Net increase (decrease) in cash and due from banks	**1,467**	**(297)**
Cash and Due from Banks		
Beginning of year	1,876	2,173
End of year	**$ 3,343**	**$ 1,876**

(continued)

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(concluded) (Dollars in Thousands)

Puget Sound Financial Services, Inc. and Subsidiary
Years Ended December 31, 2002 and 2001

	2002	2001
Supplemental Disclosures of Cash Flow Information		
Interest paid	$1,291	$1,880
Income taxes paid	520	165
Supplemental Disclosures of Non-Cash Investing and Financing Activities		
Fair value adjustment of securities available for sale, net of tax	$ 34	$ 9
Stock issued for directors' compensation	- -	10
Foreclosed real estate acquired in settlement of loans	- -	(54)

See notes to consolidated financial statements

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 1 - Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of Puget Sound Financial Services, Inc. (the Company) and its wholly owned subsidiary, Fife Commercial Bank (the Bank). All significant intercompany transactions and balances have been eliminated.

Nature of Operations

Fife Commercial Bank commenced operations on July 15, 1998. The Bank operates one branch in Fife, Washington. The Bank provides loan and deposit services to customers, who are predominately small- and middle-market businesses and middle-income individuals in western Washington.

Consolidated Financial Statement Presentation

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and practices within the banking industry. The preparation of consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities, as of the date of the balance sheet, as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for credit losses.

Certain prior year amounts have been reclassified, with no change to shareholders' equity or net income previously reported, to conform to the 2002 presentation. All dollar amounts, except per share information, are stated in thousands.

Securities Available for Sale

Securities available for sale consist of debt securities that the Bank intends to hold for an indefinite period, but not necessarily to maturity. Such securities may be sold to implement the Bank's asset/liability management strategies and in response to changes in interest rates and similar factors. Securities available for sale are reported at fair value. Unrealized gains and losses, net of the related deferred tax effect, are reported as a net amount in a separate component of shareholders' equity entitled "accumulated other comprehensive income." Realized gains and losses on securities available for sale, determined using the specific identification method, are included in earnings. Amortization of premiums and accretion of discounts are recognized in interest income over the period to maturity.

Declines in the fair value of individual securities available for sale below their cost that are other than temporary result in write-downs of the individual securities to their fair value. Such write-downs are included in earnings as realized losses.

(continued)

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 1 - Summary of Significant Accounting Policies *(continued)*

Loans

Loans are stated at the amount of unpaid principal, reduced by an allowance for credit losses. Interest on loans is accrued daily based on the principal amount outstanding.

Generally the accrual of interest on loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due or when they are past due 90 days as to either principal or interest, unless they are well secured and in the process of collection. When interest accrual is discontinued, all unpaid accrued interest is reversed against current income. If management determines that the ultimate collectibility of principal is in doubt, cash receipts on nonaccrual loans are applied to reduce the principal balance on a cash-basis method, until the loans qualify for return to accrual status. Loans are returned to accrual status when all principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for Credit Losses

The allowance for credit losses is maintained at a level considered adequate to provide for probable losses on existing loans based on evaluating known and inherent risks in the loan portfolio. The allowance is reduced by loans charged off, and increased by provisions charged to earnings and recoveries on loans previously charged off. The allowance is based on management's periodic, systematic evaluation of factors underlying the quality of the loan portfolio, including changes in the size and composition of the loan portfolio, the estimated value of any underlying collateral, actual loan loss experience, current economic conditions, and detailed analysis of individual loans for which full collectibility may not be assured. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. While management uses the best information available to make its estimates, future adjustments to the allowance may be necessary if there is a significant change in economic conditions.

When available information confirms that specific loans or portions thereof are uncollectible, these amounts are charged off against the allowance for credit losses. The existence of some or all of the following criteria will generally confirm that a loss has been incurred: the loan is significantly delinquent and the borrower has not evidenced the ability or intent to bring the loan current; the Bank has no recourse to the borrower, or if it does, the borrower has insufficient assets to pay the debt; the estimated fair value of the loan collateral is significantly below the current loan balance, and there is little or no near-term prospect for improvement.

When management determines that it is probable that a borrower will be unable to repay all amounts due according to the terms of the loan agreement, including scheduled interest payments, the loan is considered impaired. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls are generally not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of shortfall in relation to the principal and interest owed. The amount of impairment is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, when the primary source of repayment is provided by real estate collateral, at the fair value of the collateral less estimated selling costs. In addition, regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for credit losses, and may require the Bank to make additions to the allowance based on their judgment about information available to them at the time of their examinations.

The ultimate recovery of all loans is susceptible to future market factors beyond the Bank's control. These factors may result in losses or recoveries differing significantly from those provided for in the financial statements.

(continued)

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 1 - Summary of Significant Accounting Policies *(continued)*

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation, which is computed on the straight-line method over the estimated useful lives of the assets. Gains or losses on dispositions are reflected in earnings.

Foreclosed Real Estate

Real estate properties acquired through, or in lieu of, foreclosure are to be sold, and are initially recorded at the lower of cost or fair value of the properties, less estimated costs of disposal. Any write-down to fair value at the time of transfer to foreclosed real estate is charged to the allowance for credit losses. Properties are evaluated regularly to ensure that the recorded amounts are supported by their current fair values. Any subsequent reductions in carrying values, and revenue and expense from the operations of properties are charged to operations.

Transfers of Financial Assets

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

Income Taxes

Deferred tax assets and liabilities result from differences between the financial statement carrying amounts and the tax bases of assets and liabilities, and are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. The deferred tax provision represents the difference between the net deferred tax asset/liability at the beginning and end of the year. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

The Bank provides for income taxes on a separate return basis, and remits to the Company amounts currently due.

Cash Equivalents and Cash Flows

The Bank considers all amounts included in the balance sheet caption “Cash and due from banks” to be cash equivalents. Cash flows from deposits at other financial institutions, loans, federal funds sold and deposits are reported net.

(continued)

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 1 - Summary of Significant Accounting Policies *(continued)*

Stock-Based Compensation

At December 31, 2002, the Company has two stock-based compensation plans, which are described more fully in Note 13. The Company accounts for these plans under the recognition and measurement principles of APB No. 25, *Accounting for Stock Issued to Employees*, and related interpretations. Accordingly, no stock-based compensation cost is reflected in net income because all options granted under these plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The following illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123, *Accounting for Stock-Based Compensation,* for the years ended December 31 to stock-based compensation awards for the effects of all options granted:

	2002	2001
Net income, as reported	$921	$635
Less total stock-based compensation expense determined under the fair value method for all qualifying awards	(16)	(39)
Pro forma net income	**$905**	**$596**
Earnings Per Share		
Basic:		
As reported	$5.99	$3.98
Pro forma	5.89	3.73
Diluted:		
As reported	5.52	3.71
Pro forma	5.44	3.55

Earnings Per Share

Basic earnings per share exclude dilution and are computed by dividing net income by the weighted average number of common shares outstanding. Diluted earnings per share reflect the dilution that could occur if common shares were issued pursuant to the exercise of options under the Company's stock option plans.

Recent Accounting Pronouncements

In June 2001, the FASB also issued SFAS No. 143, *Accounting for Asset Retirement Obligations*. This Statement addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. This Statement is effective for all fiscal years beginning after June 15, 2002. The Company does not anticipate that the adoption of SFAS No. 143 will have a material effect on its financial position or results of operations.

(continued)

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 1 - Summary of Significant Accounting Policies *(concluded)*

Recent Accounting Pronouncements *(concluded)*

In December 2002, the Financial Accounting Standards Board issued SFAS No. 148, *Accounting for Stock-Based Compensation - Transition and Disclosure*. This Statement amends SFAS No. 123, *Accounting for Stock-Based Compensation*, to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. This Statement does not require any change from the method currently used by the Company to account for stock-based compensation, but does require more prominent disclosure in the annual consolidated financial statements about the method of accounting for such compensation and the effect of the method used on reported results. This Statement is effective for the year ended December 31, 2002. The Company has adopted the disclosure provisions of SFAS No. 148 in the accompanying consolidated financial statements and, accordingly, the disclosure requirements are set forth above under *Stock Based Compensation*.

The Financial Accounting Standards Board has issued Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*, an interpretation of SFAS Nos. 5, 57 and 107, and rescission of FASB Interpretation No. 34. This Interpretation elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The initial recognition and measurement provisions of this Interpretation are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. Implementation of these provisions is not expected to have a material impact on the Company's consolidated financial statements. The disclosure requirements of the Interpretation are effective for financial statements of interim or annual periods ending after December 15, 2002, and have been adopted in the consolidated financial statements for the year ended December 31, 2002, with no additional disclosure required.

Note 2 - Restricted Assets

Federal Reserve Board regulations require that the Bank maintain certain minimum reserve balances either in cash on hand or on deposit with the Federal Reserve Bank. The amounts of such balances for the years ended December 31, 2002 and 2001 were approximately $85 and $55, respectively.

Note 3 - Interest Bearing Deposits

Certificates of deposit at other financial institutions and deposits at the Federal Home Loan Bank of Seattle have been classified as interest bearing deposits on the balance sheets. The contractual maturities of the Bank's certificates of deposit as of December 31, 2002 are as follows:

Due in less than one year	$7,373
Due from one to five years	- -
Due from five to ten years	- -
Due after ten years	97
Total	**$7,470**

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 4 - Securities Available for Sale

Investment securities have been classified as available for sale according to management's intent. The carrying amount of securities and their approximate fair values were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2002				
Corporate bonds	$ 847	$13	$- -	$ 860
U.S. agency securities	1,717	13	- -	1,730
Mortgage-backed securities	1,297	9	- -	1,306
Obligations of states and political subdivisions	525	23	- -	548
Total	**$4,386**	**$58**	**$- -**	**$4,444**
December 31, 2001				
Corporate bonds	$ 989	$ 8	$- -	$ 997
U.S. agency securities	564	- -	2	562
Mortgage-backed securities	200	- -	- -	200
Total	**$1,753**	**$ 8**	**$ 2**	**$1,759**

The contractual maturities of securities available for sale at December 31, 2002 are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations, with or without call or prepayment penalties. Therefore, the mortgage backed securities have been classified separately in the maturity table.

	Amortized Cost	Fair Value
Due in less than one year	$ 494	$ 500
Due from one to five years	1,717	1,731
Due from five to ten years	1,163	1,180
Due after ten years	889	909
Mortgage backed securities	123	124
	$4,386	**$4,444**

Gross gains realized on sales of securities were $17 and $1 in 2002 and 2001, respectively.

Securities, carried at approximately $1,010 and $310 at December 31, 2002 and 2001, respectively, were pledged to secure public deposits and for other purposes required or permitted by law.

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 5 - Loans

Loans at December 31 consist of the following:

	2002	2001
Commercial	$15,525	$11,392
Real estate:		
Residential 1-4 family	9,885	9,259
Commercial	9,467	10,768
Construction	8,084	6,772
Consumer	1,770	1,756
Total loans	**$44,731**	**$39,947**

Changes in the allowance for credit losses for the years ended December 31 are as follows:

	2002	2001
Balance at beginning of year	$501	$396
Provision for credit losses	102	128
Charge-offs	(33)	(23)
Balance at end of year	**$570**	**$501**

Following is a summary of information pertaining to impaired loans (dollars in thousands):

	2002	2001
December 31		
Impaired loans without a valuation allowance	$ - -	$ - -
Impaired loans with a valuation allowance	32	- -
Total impaired loans	**$32**	**$- -**
Valuation allowance related to impaired loans	**$20**	**$- -**

The average impaired loan balance for 2002 was $41. No interest was recognized on impaired loans in 2002 or 2001.

The Bank had no loans 90 days past due and still accruing interest at December 31, 2002 or 2001.

Certain related parties of the Bank, principally Bank directors and their associates, were loan customers of the Bank in the ordinary course of business during 2002 and 2001. Total loans outstanding at December 31, 2002 and 2001 to key officers and directors were $3,958 and $3,345, respectively. During 2002, advances totaled $3,489 and repayments totaled $2,876 on these loans.

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 6 - Premises and Equipment

The components of premises and equipment at December 31 are as follows:

	2002	2001
Land	$ 168	$ 168
Building	718	718
Furniture	87	80
Equipment	187	146
	1,160	**1,112**
Less accumulated depreciation	212	143
Total premises and equipment	**$ 948**	**$ 969**

Note 7 - Deposits

The composition of deposits at December 31 is as follows:

	2002	2001
Demand deposits, non-interest bearing	$11,552	$ 7,433
NOW and money market accounts	16,876	10,495
Savings deposits	2,122	948
Time certificates, $100,000 or more	12,132	13,000
Other time certificates	13,731	15,647
Total	**$56,413**	**$47,523**

Scheduled maturities of certificates of deposit for future years ending December 31 are as follows:

2003	$25,017
2004	670
2005	176
	$25,863

Note 8 - Long-Term Borrowings

Long-term borrowings at December 31, 2002 represent advances from the Federal Home Loan Bank of Seattle bearing interest at 3.44% to 4.79% and maturing: 2004 - $500; 2005 - $200; 2006 - $300 and 2007 - $1,700. The Bank has pledged $8,718 of securities and loans as collateral for these borrowings at December 31, 2002.

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 9 - Employee Benefits

The Company has a 401(k) plan which covers substantially all employees who have completed three months or more of service. Company contributions to the plan may include a discretionary match as determined by the Board of Directors. For the years ended December 31, 2002 and 2001, Company contributions to the plan were 3% of eligible employee compensation plus an additional 2% match of employee contributions. Total contributions in 2002 and 2001 were $80 and $58, respectively.

Note 10 - Deferred Compensation Agreements

In December 2002, the Bank established a non-qualified deferred compensation agreement with the Board of Directors under which, as determined at the beginning of each plan year, the directors may defer a portion or all of their director fees. Amounts deferred will earn interest at a rate to be determined annually. No expenses were incurred with this plan during 2002. Amounts deferred will be paid to the directors after their retirement from the Board.

Also in December 2002, the Board of Directors approved a non-qualified deferred compensation agreement with certain key employees. These employees may elect, at the beginning of each year, to defer a percentage of their compensation. Amounts deferred will earn interest at a rate to be determined annually, and will be paid to the employees at retirement. No expenses were incurred with this plan during 2002.

Benefits to directors and employees may be funded by life insurance policies purchased by the Company, which had a cash surrender value of $1,002 at December 31, 2002.

Note 11 - Income Taxes

Income taxes are comprised of the following for the years ended December 31:

	2002	2001
Current	$437	$316
Deferred	48	17
Total income taxes	**$485**	**$333**

The following is a reconciliation between the statutory and the effective federal income tax rate for the years ended December 31:

	2002 **Amount**	**Percent of Pre-tax Income**	2001 **Amount**	**Percent of Pre-tax Income**
Income tax at statutory rates	$492	35.0%	$339	35.0%
Increase (decrease) resulting from:				
Tax exempt income	(7)	(.5)	- -	- -
Other	- -	- -	(6)	(.6)
Total income tax expense	**$485**	**34.5%**	**$333**	**34.4%**

(continued)

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 11 - Income Taxes *(concluded)*

The tax effects of temporary differences that give rise to significant portions of deferred tax assets and liabilities at December 31 are:

	2002	2001
Deferred Tax Assets		
Allowance for credit losses	$153	$119
Pre-opening expenses	5	16
Total deferred tax assets	**158**	**135**
Deferred Tax Liabilities		
Accumulated depreciation	47	33
Deferred income	235	197
Cash basis reporting	82	63
Unrealized gain on securities available for sale	20	2
Total deferred tax liabilities	**384**	**295**
Net deferred tax liabilities	**$226**	**$160**

Note 12 - Commitments and Contingencies

The Bank is party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit. These instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheets.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments. A summary of the Bank's commitments at December 31 is as follows:

	2002	2001
Commitments to extend credit:		
Real estate secured	$3,523	$2,528
Other	2,408	1,478
Total commitments to extended credit	**$5,931**	**$4,006**

(continued)

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 12 - Commitments and Contingencies *(concluded)*

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank estimates that approximately 75% of loan commitments are drawn upon by customers. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the party. Collateral held varies, but may include accounts receivable, inventory, property and equipment, residential real estate, and income-producing commercial properties.

The Bank has agreements with correspondent banks for lines of credit totaling $2,000, none of which was used at December 31, 2002, and a credit line with the Federal Home Loan Bank of Seattle totaling 10% of assets, $2,700 of which was used at December 31, 2002.

Because of the nature of its activities, the Company is subject to various pending and threatened legal actions which arise in the ordinary course of business. In the opinion of management, liabilities arising from these claims, if any, will not have a material effect on the financial position of the Company.

Note 13 - Stock Options Plans

Under the Company's employee stock option plan, the Company may grant options for up to 22,500 shares (6,200 remain available for grant at December 31, 2002) of its common stock to certain key employees. The exercise price of each option equals the fair market value of the Company's stock on the date of grant, and an option's maximum term is ten years. Under the director plan, the Company may grant options for up to 9,000 shares (1,000 remain available for grant at December 31, 2002) of its common stock to its directors. The exercise price equals the fair market value of the Company's stock on the date of grant, and an option's maximum term is ten years. Under both plans, options vest 20% on the date of grant and 20% on the anniversary of the grant for four succeeding years.

No stock options were granted during 2002 or 2001.

A summary of the status of the Company's stock option plans as of December 31 is presented below:

	2002		2001	
	Shares	**Weighted Average Exercise Price**	**Shares**	**Weighted Average Exercise Price**
Outstanding at beginning of year	24,500	$20.51	24,500	$20.51
Granted	- -	- -	- -	- -
Exercised	(50)	26.28	- -	- -
Forfeited	(200)	26.28	- -	- -
Outstanding at end of year	**24,250**	**$20.45**	**24,500**	**$20.51**
Options exercisable at year-end	21,950		17,200	

(continued)

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 13 - Stock Options Plans *(concluded)*

The following summarizes information about stock options outstanding and exercisable at December 31, 2002:

Exercise Price	Number Outstanding	Contractual Life (Years)	Weighted Average Remaining Number Exercisable
$20.00	22,500	6.0	20,900
26.28	1,750	7.8	1,050
	24,250		**21,950**

Note 14 - Regulatory Matters

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of Tier 1 capital (as defined in the regulations) to total average assets (as defined), and minimum ratios of Tier 1 and total capital (as defined) to risk-weighted assets (as defined).

As of December 31, 2002, the most recent notification from the Bank's regulator categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the table below. There are no conditions or events since that notification that management believes have changed the institution's category.

(continued)

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 14 - Regulatory Matters *(concluded)*

The Company's and the Bank's actual capital amounts and ratios are also presented in the table. Management believes, as of December 31, 2002, that the Bank meets all capital requirements to which it is subject.

	Actual		Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2002						
Tier 1 capital (to average assets):						
Consolidated	$4,941	8.06%	$2,451	4.00%	N/A	N/A
Bank	4,926	8.04	2,451	4.00	$3,067	5.00%
Tier 1 capital (to risk-weighted assets):						
Consolidated	4,941	10.18	1,942	4.00	N/A	N/A
Bank	4,926	10.14	1,942	4.00	2,194	6.00
Total capital (to risk-weighted assets):						
Consolidated	5,511	11.35	3,885	8.00	N/A	N/A
Bank	5,496	11.32	3,885	8.00	4,856	10.00
December 31, 2001						
Tier 1 capital (to average assets):						
Consolidated	$4,278	8.91%	$1,921	4.00%	N/A	N/A
Bank	4,255	8.86	1,921	4.00	$2,401	5.00%
Tier 1 capital (to risk-weighted assets):						
Consolidated	4,278	10.42	1,643	4.00	N/A	N/A
Bank	4,255	10.36	1,643	4.00	2,464	6.00
Total capital (to risk-weighted assets):						
Consolidated	4,779	11.64	3,285	8.00	N/A	N/A
Bank	4,756	11.58	3,285	8.00	4,106	10.00

Note 15 - Earnings Per Share Disclosures

Following is information regarding the calculation of basic and diluted earnings per share for the years indicated:

	Net Income (Numerator)	Shares (Denominator)	Per Share Amount
Year Ended December 31, 2002			
Basic earnings per share:			
Net income	$921	153,744	$5.99
Effect of dilutive securities:			
Options	- -	13,047	(.47)
Diluted earnings per share:			
Net income	**$921**	**166,791**	**$5.52**

(continued)

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 15 - Earnings Per Share Disclosures *(concluded)*

	Net Income (Numerator)	Shares (Denominator)	Per Share Amount
Year Ended December 31, 2001			
Basic earnings per share:			
Net income	$635	159,685	$3.98
Effect of dilutive securities:			
Options	- -	11,612	(.27)
Diluted earnings per share:			
Net income	**$635**	**171,297**	**$3.71**

Note 16 - Directors' Compensation

In early 2001 members of the Bank's Board of Directors received shares of stock for each meeting attended. The stock was issued in lieu of cash compensation based on its fair market value.

Note 17 - Condensed Financial Information - Parent Company Only

Condensed Balance Sheets - December 31

	2002	2001
Assets		
Cash	$ 10	$ 13
Investment in Bank	4,963	4,259
Other assets	6	10
Total assets	**$4,979**	**$4,282**
Shareholders' Equity	**$4,979**	**$4,282**

(continued)

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 17 - Condensed Financial Information - Parent Company Only *(concluded)*

Condensed Statements of Income - Years Ended December 31

	2002	2001
Dividend Income from the Bank	$262	$236
Expenses	12	35
Income before income taxes	**250**	**201**
Income Tax Benefit	- -	10
Income before undistributed income of the Bank	**250**	**211**
Equity in Undistributed Income of the Bank	671	424
Net income	**$921**	**$635**

Condensed Statements of Cash Flows - Years Ended December 31

Operating Activities		
Net income	$921	$635
Adjustments to reconcile net income to net cash provided:		
Equity in undistributed income of the Bank	(671)	(424)
Other - net	5	(11)
Net cash provided by operating activities	**255**	**200**
Financing Activities		
Repurchase of common stock	(260)	(187)
Exercise of stock options	2	- -
Net cash used in financing activities	**(258)**	**(187)**
(Increase) decrease in cash	**(3)**	**13**
Cash		
Beginning of year	13	- -
End of year	**$ 10**	**$ 13**

Puget Sound Financial Services, Inc. and Subsidiary
December 31, 2002 and 2001

Note 18 - Comprehensive Income

Net unrealized gains include, net of tax, $69 of unrealized gains arising during 2002 and $15 of unrealized gains arising during 2001, less reclassification adjustments of $17 and $1 for gains included in net income in 2002 and 2001, respectively, as follows:

	Before-Tax Amount	Tax Benefit (Expense)	Net-of-Tax Amount
Year Ended December 31, 2002			
Unrealized holding gains arising during the year	$69	($24)	$45
Reclassification adjustments for gains realized in net income	(17)	(6)	(11)
Net unrealized gains	**$52**	**($18)**	**$34**
Year Ended December 31, 2001			
Unrealized holding gains arising during the year	$15	($5)	$10
Reclassification adjustments for gains realized in net income	(1)	- -	(1)
Net unrealized gains	**$14**	**($5)**	**$ 9**

Supplementary Information

Average Balances and Net Interest Income
(Dollars in Thousands)

Fife Commercial Bank
Years Ended December 31, 2002 and 2001

	2002			2001		
	Average Balance	**Interest Income (Expense)**	**Average Rate**	**Average Balance**	**Interest Income (Expense)**	**Average Rate**
Assets						
Earning assets:						
Loans	$41,804	$3,933	9.4%	$35,404	$3,742	10.6%
Federal funds sold and deposits in banks	7,017	181	2.6	8,252	388	4.7
Investment securities:						
Taxable	3,134	135	4.3	1,775	114	6.4
Tax exempt	439	33*	7.5	- -	- -	- -
Total investments	**3,573**			**1,775**		
Total earning assets/ interest income	**52,394**	**4,282**	**8.2%**	**45,431**	**4,244**	**9.3%**
Cash and due from banks	2,632			1,755		
Premises and equipment - net	967			929		
Other assets	385			349		
Allowance for credit losses	(523)			(439		
Total assets	**$55,855**			**$48,025**		
Liabilities and Shareholder's Equity						
Interest bearing liabilities:						
Deposits:						
Savings and interest-bearing demand	$14,858	(282)	1.9%	$ 9,735	(350)	3.6%
Time	26,022	(921)	3.5	27,266	(1,570)	5.8
Total interest bearing deposits	**40,880**	**(1,203)**	**2.9**	**37,001**	**(1,920)**	**5.2**
Long-term borrowings	1,460	(61)	4.1	- -	- -	- -
Total interest bearing liabilities/interest expense	**42,340**	**(1,264)**	**2.9%**	**37,001**	**(1,920)**	**5.2%**
Demand deposits	8,298			6,435		
Other liabilities	577			490		
Shareholder's equity	4,640			4,099		
Total liabilities and shareholder's equity	**$55,855**			**$48,025**		
Net interest income		**$3,018**			**$2,324**	
Net Interest Income as a Percentage of Average Earning Assets						
Interest income			8.2%			9.3%
Interest expense			2.4			4.2
Net interest income			**5.8%**			**5.1%**

* *Tax equivalent basis*

See independent auditor's report.