

WASHINGTON TRUST BANCORP INC  
Form 10-Q  
November 09, 2007

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

**FORM 10-Q**

(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended **SEPTEMBER 30, 2007** or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from \_\_\_\_\_ to \_\_\_\_\_.

**Commission file number: 000-13091**

**WASHINGTON TRUST BANCORP, INC.**

**(Exact name of registrant as specified in its charter)**

**RHODE ISLAND**

(State or other jurisdiction of incorporation or organization)

**05-0404671**

(I.R.S. Employer Identification No.)

**23 BROAD STREET  
WESTERLY, RHODE ISLAND**  
(Address of principal executive offices)

**02891**  
(Zip Code)

**(401) 348-1200**  
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes       No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer      
Accelerated filer            
Non-accelerated filer              Accelerated filer         

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes       No

The number of shares of common stock of the registrant outstanding as of October 31, 2007 was 13,351,231.

---

**FORM 10-Q**  
**WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES**  
For the Quarter Ended September 30, 2007

**TABLE OF CONTENTS**

|  | Page<br>Number |
|--|----------------|
| <u>PART I. Financial Information</u>   |                |
| <u>Item 1. Financial Statements</u>  |                |
| <u>Consolidated Balance Sheets</u><br><u>September 30, 2007 (as restated) and December 31, 2006</u>  | 3              |
| <u>Consolidated Statements of Income</u><br><u>Three and Nine Months (as restated) Ended September 30,</u><br><u>2007 (as restated) and 2006</u> | 4              |
| <u>Consolidated Statements of Cash Flows</u><br><u>Nine Months Ended September 30, 2007 (as restated) and</u><br><u>2006</u>                     | 5              |
| <u>Condensed Notes to Consolidated Financial Statements</u>  | 7              |
| <u>Report of Independent Registered Public Accounting Firm</u>   | 24             |
| <u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of</u><br><u>Operations</u>                                   | 25             |
| <u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>  | 38             |
| <u>Item 4. Controls and Procedures</u>   | 38             |
| <u>PART II. Other Information</u>  |                |
| <u>Item 1. Legal Proceedings</u>   | 38             |
| <u>Item 1A. Risk Factors</u>   | 38             |
| <u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>   | 39             |
| <u>Item 6. Exhibits</u>  | 40             |
| <u>Signatures</u>  | 41             |
| <u>Exhibit 15.1 Letter re: Unaudited Interim Financial Information</u>   |                |

Exhibit 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

Exhibit 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

Exhibit 32.1 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley act of 2002

-2-

---

**PART I. FINANCIAL INFORMATION**  
**ITEM 1. FINANCIAL STATEMENTS**  
**WASHINGTON TRUST BANCORP, INC. AND**  
**SUBSIDIARIES**

(Dollars in thousands)

**CONSOLIDATED BALANCE SHEETS (Unaudited)**

|   | As Restated<br>September 30,<br>2007 | December 31,<br>2006 |
|---|--------------------------------------|----------------------|
| <b>Assets:</b>  |                                      |                      |
| Cash and due from banks   | \$ 31,521                            | \$ 54,337            |
| Federal funds sold  | 21,975                               | 16,425               |
| Other short-term investments  | 1,516                                | 1,147                |
| Mortgage loans held for sale  | 2,095                                | 2,148                |
| Securities:   |                                      |                      |
| Available for sale, at fair value; amortized cost \$691,836 in 2007 and \$525,966 in 2006           | 688,709                              | 526,396              |
| Held to maturity, at cost; fair value \$175,369 in 2006   | —                                    | 177,455              |
| Total securities  | 688,709                              | 703,851              |
| Federal Home Loan Bank stock, at cost   | 28,727                               | 28,727               |
| Loans:  |                                      |                      |
| Commercial and other  | 650,023                              | 587,397              |
| Residential real estate   | 578,816                              | 588,671              |
| Consumer  | 285,654                              | 283,918              |
| Total loans   | 1,514,493                            | 1,459,986            |
| Less allowance for loan losses  | 19,472                               | 18,894               |
| Net loans   | 1,495,021                            | 1,441,092            |
| Premises and equipment, net   | 25,790                               | 24,307               |
| Accrued interest receivable   | 12,030                               | 11,268               |
| Investment in bank-owned life insurance   | 40,936                               | 39,770               |
| Goodwill  | 50,479                               | 44,558               |
| Identifiable intangible assets, net   | 11,759                               | 12,816               |
| Other assets  | 21,204                               | 18,719               |
| Total assets  | \$ 2,431,762                         | \$ 2,399,165         |
| <b>Liabilities:</b>   |                                      |                      |
| Deposits:   |                                      |                      |
| Demand deposits   | \$ 182,830                           | \$ 186,533           |
| NOW accounts  | 172,378                              | 175,479              |
| Money market accounts   | 312,257                              | 286,998              |
| Savings accounts  | 189,157                              | 205,998              |
| Time deposits   | 799,265                              | 822,989              |
| Total deposits  | 1,655,887                            | 1,677,997            |
| Dividends payable   | 2,676                                | 2,556                |
| Federal Home Loan Bank advances   | 502,265                              | 474,561              |
| Junior subordinated debentures  | 22,681                               | 22,681               |
| Other borrowings  | 36,403                               | 14,684               |
| Accrued expenses and other liabilities  | 33,953                               | 33,630               |
| Total liabilities   | 2,253,865                            | 2,226,109            |
| <b>Shareholders' Equity:</b>  |                                      |                      |
| Common stock of \$.0625 par value; authorized 30,000,000 shares; issued 13,492,110 in 2007 and 2006 | 843                                  | 843                  |

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

|   |              |              |
|---|--------------|--------------|
| Paid-in capital   | 34,821       | 35,893       |
| Retained earnings   | 151,537      | 141,548      |
| Accumulated other comprehensive loss                                      | (5,587)      | (3,515)      |
| Treasury stock, at cost; 141,646 shares in 2007 and 62,432 shares in 2006 | (3,717)      | (1,713)      |
| Total shareholders' equity  | 177,897      | 173,056      |
| Total liabilities and shareholders' equity                                | \$ 2,431,762 | \$ 2,399,165 |

The accompanying notes are an integral part of these consolidated financial statements.

-3-

**WASHINGTON TRUST BANCORP, INC. AND  
SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF  
INCOME (Unaudited)**

**(Dollars and shares in thousands,  
except per share amounts)**

| Periods ended September 30,  | Three Months  |               | As Restated<br>Nine Months |               |
|--|---------------|---------------|----------------------------|---------------|
|  | 2007          | 2006          | 2007                       | 2006          |
| <b>Interest income:</b>  |               |               |                            |               |
| Interest and fees on loans   | \$ 25,032     | \$ 23,430     | \$ 73,380                  | \$ 68,457     |
| <b>Interest on securities:</b>   |               |               |                            |               |
| Taxable  | 7,565         | 8,493         | 23,196                     | 25,553        |
| Nontaxable   | 781           | 405           | 2,208                      | 1,104         |
| Dividends on corporate stock and Federal Home Loan Bank stock          | 669           | 1,197         | 2,072                      | 2,124         |
| Interest on federal funds sold and other short-term investments        | 275           | 252           | 650                        | 517           |
| <b>Total interest income</b>   | <b>34,322</b> | <b>33,777</b> | <b>101,506</b>             | <b>97,755</b> |
| <b>Interest expense:</b>   |               |               |                            |               |
| Deposits   | 13,140        | 12,473        | 39,332                     | 33,872        |
| Federal Home Loan Bank advances  | 5,243         | 5,011         | 15,323                     | 16,115        |
| Junior subordinated debentures   | 338           | 338           | 1,014                      | 1,014         |
| Other  | 291           | 89            | 730                        | 256           |
| <b>Total interest expense</b>  | <b>19,012</b> | <b>17,911</b> | <b>56,399</b>              | <b>51,257</b> |
| <b>Net interest income</b>   | <b>15,310</b> | <b>15,866</b> | <b>45,107</b>              | <b>46,498</b> |
| Provision for loan losses  | 300           | 300           | 900                        | 900           |
| <b>Net interest income after provision for loan losses</b>             | <b>15,010</b> | <b>15,566</b> | <b>44,207</b>              | <b>45,598</b> |
| <b>Noninterest income:</b>   |               |               |                            |               |
| <b>Wealth management services:</b>                                     |               |               |                            |               |
| Trust and investment advisory fees                                     | 5,336         | 4,727         | 15,626                     | 14,036        |
| Mutual fund fees   | 1,386         | 1,229         | 4,000                      | 3,573         |
| Financial planning, commissions and other service fees                 | 456           | 509           | 1,915                      | 2,033         |
| <b>Wealth management services</b>                                      | <b>7,178</b>  | <b>6,465</b>  | <b>21,541</b>              | <b>19,642</b> |
| Service charges on deposit accounts                                    | 1,214         | 1,312         | 3,559                      | 3,667         |
| Merchant processing fees   | 2,252         | 2,125         | 5,285                      | 4,828         |
| Income from bank-owned life insurance                                  | 376           | 389           | 1,166                      | 1,014         |
| Net gains on loan sales and commissions on loans originated for others | 431           | 417           | 1,205                      | 1,029         |
| Net realized (losses) gains on securities                              | –             | (365)         | 336                        | 459           |
| Other income   | 399           | 440           | 1,129                      | 1,111         |
| <b>Total noninterest income</b>  | <b>11,850</b> | <b>10,783</b> | <b>34,221</b>              | <b>31,750</b> |
| <b>Noninterest expense:</b>  |               |               |                            |               |
| Salaries and employee benefits   | 10,098        | 9,651         | 30,195                     | 29,100        |
| Net occupancy  | 1,021         | 934           | 3,076                      | 2,906         |
| Equipment  | 871           | 872           | 2,564                      | 2,552         |
| Merchant processing costs  | 1,916         | 1,796         | 4,493                      | 4,090         |
| Outsourced services  | 556           | 490           | 1,610                      | 1,504         |
| Advertising and promotion  | 466           | 371           | 1,467                      | 1,489         |
| Legal, audit and professional fees                                     | 444           | 563           | 1,298                      | 1,342         |
| Amortization of intangibles  | 341           | 398           | 1,057                      | 1,209         |
| Debt prepayment penalties  | –             | –             | 1,067                      | –             |

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

|   |          |          |           |           |
|---|----------|----------|-----------|-----------|
| Other   | 1,599    | 1,536    | 5,354     | 5,403     |
| Total noninterest expense                     | 17,312   | 16,611   | 52,181    | 49,595    |
| Income before income taxes                    | 9,548    | 9,738    | 26,247    | 27,753    |
| Income tax expense                            | 2,992    | 3,160    | 8,234     | 8,925     |
| Net income                                    | \$ 6,556 | \$ 6,578 | \$ 18,013 | \$ 18,828 |
| Weighted average shares outstanding - basic   | 13,323.6 | 13,436.6 | 13,358.1  | 13,414.6  |
| Weighted average shares outstanding - diluted | 13,564.1 | 13,726.3 | 13,612.7  | 13,708.2  |
| Per share information:                        |          |          |           |           |
| Basic earnings per share                      | \$ 0.49  | \$ 0.49  | \$ 1.35   | \$ 1.40   |
| Diluted earnings per share                    | \$ 0.48  | \$ 0.48  | \$ 1.32   | \$ 1.37   |
| Cash dividends declared per share             | \$ 0.20  | \$ 0.19  | \$ 0.60   | \$ 0.57   |

The accompanying notes are an integral part of these consolidated financial statements.

-4-



**WASHINGTON TRUST  
BANCORP, INC. AND  
SUBSIDIARIES**

(Dollars in thousands)

**CONSOLIDATED STATEMENTS OF CASH  
FLOWS (Unaudited)**

| Nine months ended September 30,   | As Restated<br>2007 | 2006      |
|---|---------------------|-----------|
| <b>Cash flows from operating activities:</b>                                      |                     |           |
| Net income  | \$ 18,013           | \$ 18,828 |
| Adjustments to reconcile net income to net cash provided by operating activities: |                     |           |
| Provision for loan losses   | 900                 | 900       |
| Depreciation of premises and equipment  | 2,209               | 2,287     |
| Loss on disposal of premises and equipment  | 23                  | -         |
| Net amortization of premium and discount  | 466                 | 1,070     |
| Net amortization of intangibles   | 1,057               | 1,209     |
| Share-based compensation  | 427                 | 535       |
| Non-cash charitable contribution  | 520                 | 513       |
| Earnings from bank-owned life insurance   | (1,166)             | (1,014)   |
| Net gains on loan sales   | (1,205)             | (1,029)   |
| Net realized gains on sales of securities   | (336)               | (459)     |
| Proceeds from sales of loans  | 47,313              | 29,395    |
| Loans originated for sale   | (46,496)            | (31,076)  |
| Increase in accrued interest receivable, excluding purchased interest             | (731)               | (724)     |
| Increase in other assets  | (1,211)             | (2,483)   |
| Increase in accrued expenses and other liabilities                                | 533                 | 2,233     |
| Other, net  | (3)                 | 10        |
| Net cash provided by operating activities   | 20,313              | 20,195    |
| <b>Cash flows from investing activities:</b>                                      |                     |           |
| Purchases of:   |                     |           |
| Mortgage-backed securities available for sale                                     | (143,774)           | (31,820)  |
| Other investment securities available for sale                                    | (39,290)            | (58,561)  |
| Other investment securities held to maturity                                      | (12,882)            | (17,682)  |
| Proceeds from sale of:  |                     |           |
| Mortgage-backed securities available for sale                                     | 47,938              | 45,249    |
| Other investment securities available for sale                                    | 10,160              | 12,251    |
| Mortgage-backed securities held to maturity                                       | 38,501              | -         |
| Other investment securities held to maturity                                      | 21,698              | -         |
| Maturities and principal payments of:   |                     |           |
| Mortgage-backed securities available for sale                                     | 50,042              | 69,613    |
| Other investment securities available for sale                                    | 14,957              | 1,999     |
| Mortgage-backed securities held to maturity                                       | 3,191               | 12,873    |
|   | 20,490              | 8,490     |

|   | Other investment securities held<br>to maturity |           |
|---|---|-----------|
| Remittance of Federal Home Loan Bank stock                                  | –   | 3,000     |
| Net increase in loans   | (48,704)  | (1,557)   |
| Purchases of loans, including purchased interest                            | (5,841)   | (25,309)  |
| Purchases of premises and equipment   | (3,715)   | (2,619)   |
| Purchases of bank-owned life insurance                                      | –   | (8,000)   |
| Payment of deferred acquisition obligation                                  | (6,720)   | –         |
| Net cash (used in) provided by investing activities                         | (53,949)  | 7,927     |
| <b>Cash flows from financing activities:</b>                                |   |           |
| Net (decrease) increase in deposits   | (22,110)  | 60,929    |
| Net increase in other borrowings  | 22,518  | 559       |
| Proceeds from Federal Home Loan Bank advances                               | 532,463   | 382,529   |
| Repayment of Federal Home Loan Bank advances                                | (504,729)                                       | (463,668) |
| Purchases of treasury stock, including deferred compensation plan activity  | (5,211)   | (117)     |
| Proceeds from the issuance of common stock under dividend reinvestment plan | –   | 911       |
| Proceeds from the exercise of share options                                 | 989   | 611       |
| Tax benefit from share option exercises                                     | 723   | 259       |
| Cash dividends paid   | (7,904)   | (7,513)   |
| Net cash provided by (used in) financing activities                         | 16,739  | (25,500)  |
| Net (decrease) increase in cash and cash equivalents                        | (16,897)  | 2,622     |
| Cash and cash equivalents at beginning of year                              | 71,909  | 66,163    |
| Cash and cash equivalents at end of period                                  | \$ 55,012                                       | \$ 68,785 |

The accompanying notes are an integral part of these consolidated financial statements.

**WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)**

**(Dollars in thousands)**  
**(Continued)**

|   |                     | As Restated |        |
|---|---------------------|-------------|--------|
|   |                     | 2007        | 2006   |
| Nine months ended September 30,                               |                     |             |        |
| <b>Noncash Investing and Financing Activities:</b>            |                     |             |        |
| Loans charged off   |                     | \$ 553      | \$ 325 |
| Increase to deferred acquisition obligation                   |                     | 5,921       | 4,595  |
| Held to maturity securities transferred to available for sale |                     | 162,997     | –      |
| <b>Supplemental Disclosures:</b>                              |                     |             |        |
|   | Interest payments   | 56,792      | 50,868 |
|   | Income tax payments | 8,965       | 10,327 |

The accompanying notes are an integral part of these consolidated financial statements.

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES  
CONDENSED NOTES TO CONSOLIDATED FINANCIAL  
STATEMENTS**

**General**

Washington Trust Bancorp, Inc. (the “Bancorp”) is a publicly-owned registered bank holding company and financial holding company. The Bancorp owns all of the outstanding common stock of The Washington Trust Company (the “Bank”), a Rhode Island chartered commercial bank founded in 1800. Through its subsidiaries, the Bancorp offers a complete product line of financial services to individuals and businesses including commercial, residential and consumer lending, retail and commercial deposit products, and wealth management services through its branch offices in Rhode Island, Massachusetts and southeastern Connecticut, ATMs, and its Internet web site ([www.washtrust.com](http://www.washtrust.com)).

**(1) Basis of Presentation**

The consolidated financial statements include the accounts of the Bancorp and its subsidiaries (collectively, the “Corporation” or “Washington Trust”). All significant intercompany transactions have been eliminated. Certain prior year amounts have been reclassified to conform to the current year classification. Such reclassifications have no effect on previously reported net income or shareholders’ equity.

The accounting and reporting policies of the Corporation conform to U.S. generally accepted accounting principles (“GAAP”) and to general practices of the banking industry. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and revenues and expenses for the period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to near-term change are the determination of the allowance for loan losses and tax estimates.

In the opinion of management, the accompanying consolidated financial statements reflect all adjustments (consisting of normal recurring adjustments) and disclosures necessary to present fairly the Corporation’s financial position as of September 30, 2007 and December 31, 2006, respectively, and the results of operations and cash flows for the interim periods presented. Interim results are not necessarily reflective of the results of the entire year. The unaudited consolidated financial statements of the Corporation presented herein have been prepared pursuant to the rules of the Securities and Exchange Commission (“SEC”) for quarterly reports on Form 10-Q and do not include all of the information and note disclosures required by GAAP. The accompanying consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in Washington Trust’s Annual Report on Form 10-K for the year ended December 31, 2006.

On October 30, 2007, we announced that we identified accounting errors related to sales of certain held-to-maturity investment securities conducted in the second quarter of 2007. Based on our assessment of the provisions of Statement of Financial Accounting Standards No. 159, “The Fair Value Option for Financial Assets and Liabilities” (“SFAS No. 159”), on April 12, 2007 we had decided to implement early adoption of SFAS No. 159. In connection with this, we selected the fair value option for certain U.S. Government sponsored agency and mortgage-backed securities with lower coupons and slower prepayment characteristics in the held-to-maturity portfolio totaling approximately \$61.9 million. A portfolio restructuring plan was also undertaken to reduce interest rate risk and improve net interest margin, which included the sale of these securities. On Friday April 13, 2007 we executed sale trades for these held-to-maturity securities. At the time of the sales transactions the historical amortized cost basis of the sold securities exceeded the total sales price by \$1.7 million. On Monday April 16, 2007 additional information became available regarding clarifications of the interpretation of the application of SFAS No. 159 by applicable regulatory and accounting industry bodies that led us to conclude that the application of SFAS No. 159 to our transactions might be inconsistent with the intent and spirit of SFAS No. 159. Consequently, we decided not to early-adopt SFAS No. 159.

In connection with that decision, we were able to promptly execute purchase trade transactions for the identical securities prior to the sales settlement date for approximately \$49.9 million of the \$61.9 million total, with the intent that, in substance, the sale transaction would be offset for these securities. The reacquired securities were retained in the held-to-maturity portfolio at the original pre-sale amortized cost and a \$1.4 million loss on the sale of the reacquired securities was not recognized. The sale and reacquisition of the \$49.9 million in held-to-maturity securities as well as certain other investing and financing transactions conducted in connection with the portfolio restructuring strategy were similarly treated in an offset manner and these transaction amounts were incorrectly omitted from the

-7-

---

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

**(Continued)**

consolidated statement of cash flows for the period ended June 30, 2007; the correction for these other investing and financing transactions had no effect on net income. For the reacquired securities, the reacquisition price exceeded the selling price by \$153 thousand and an expense of this amount was recognized in other noninterest expense in the second quarter of 2007. Also in the second quarter of 2007, a realized securities loss in the amount of \$261 thousand was recognized on the securities that were sold but not reacquired. We discussed the accounting treatment described above with KPMG LLP, our independent registered public accounting firm, in connection with its quarterly review process.

Based on a recent review of these transactions, in consultation with KPMG, we have determined that the offsetting of the April 13, 2007 sales and subsequent reacquisition of identical securities was incorrect and that the sale transactions should have been recognized with a \$1.4 million realized securities loss and corresponding reduction in the carrying value of the reacquired securities.

Also, we have determined that the remaining held-to-maturity portfolio should have been reclassified to the available-for-sale category. This reclassification has been recognized as of April 13, 2007. Accordingly, the effect on the June 30, 2007 consolidated balance sheet was to reclassify the portfolio of held-to-maturity securities to the available-for-sale category, which resulted in a \$1.6 million reduction in shareholders' equity. We will not be able to classify securities in the held-to-maturity category for a period of two years from the April 13, 2007 sales date as a result of this action.

The correction to reduce the cost basis of the reacquired securities results in a change to the accretion of discount for these securities, which is recognized in interest income until their maturity dates. The resulting additional amount of accretion income recognized on these securities was \$79 thousand in each of the quarters ended June 30, 2007 and September 30, 2007.

For the quarter ended June 30, 2007, the accounting corrections for these transactions, including recognition of the realized loss on the sales transactions and other related changes, result in an after-tax reduction in net income of \$828 thousand, or 6 cents per diluted share, from \$6.3 million, or 46 cents per diluted share, to \$5.5 million, or 40 cents per diluted share. For the six-month period ended June 30, 2007 the accounting corrections result in a reduction in net income from \$12.3 million, or 90 cents per diluted share, to \$11.5 million, or 84 cents per diluted share.

All applicable amounts related to this restatement have been reflected in this Form 10-Q, including the Consolidated Financial Statements and Notes thereto.

On October 24, 2007, management, in consultation with KPMG, concluded that the Corporation's interim financial statements for the period ended June 30, 2007 should be restated and that the Corporation's financial statements for the quarter ended June 30, 2007 should no longer be relied upon. The Audit Committee of our Board of Directors has thoroughly reviewed this matter and, on October 26, 2007, approved management's conclusion.

The Corporation will file an amended Form 10-Q for the quarter ended June 30, 2007 reflecting the necessary adjustments with the SEC as soon as practicable. The Corporation will also file an amended Form 10-Q for the quarter ended March 31, 2007 with the SEC as soon as practicable to add a subsequent event footnote to disclose the second quarter 2007 transactions described above.

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

The following tables summarize the effect of the restatement adjustments on the consolidated financial statements as of and for the three and six months ended June 30, 2007:

**Consolidated Balance Sheet** (unaudited)

As of June 30, 2007

| (Dollars in thousands)                     | As         |            |             |
|--|------------|------------|-------------|
|  | Reported   | Adjustment | As Restated |
| Available for sale securities              | \$ 525,688 | \$ 150,516 | \$ 676,204  |
| Held to maturity securities                | 154,171    | (154,171)  | —           |
| Total securities                           | 679,859    | (3,655)    | 676,204     |
| Other assets                               | 21,063     | 1,237      | 22,300      |
| Total assets                               | 2,396,300  | (2,418)    | 2,393,882   |
| Retained earnings                          | 148,485    | (828)      | 147,657     |
| Accumulated other comprehensive loss       | (6,519)    | (1,590)    | (8,109)     |
| Shareholders' equity                       | 173,606    | (2,418)    | 171,188     |
| Total liabilities and shareholders' equity | 2,396,300  | (2,418)    | 2,393,882   |

**Consolidated Statement of Income** (unaudited)

Three Months Ended June 30, 2007

| (Dollars in thousands, except per share amounts)    | As       |            |             |
|---|----------|------------|-------------|
|   | Reported | Adjustment | As Restated |
| Interest income on taxable securities               | \$ 7,709 | \$ 130     | \$ 7,839    |
| Interest expense on Federal Home Loan Bank advances | 5,063    | 49         | 5,112       |
| Net interest income                                 | 14,846   | 81         | 14,927      |
| Net interest income after provision for loan losses | 14,546   | 81         | 14,627      |
| Net realized gains (losses) on securities           | 705      | (1,405)    | (700)       |
| Total noninterest income                            | 12,528   | (1,405)    | 11,123      |
| Other noninterest expense                           | 2,274    | (115)      | 2,159       |
| Total noninterest expense                           | 17,875   | (115)      | 17,760      |
| Income before taxes                                 | 9,199    | (1,209)    | 7,990       |
| Income tax expense                                  | 2,889    | (381)      | 2,508       |
| Net income  | 6,310    | (828)      | 5,482       |
| Basic earnings per share                            | \$ 0.47  | \$ (0.06)  | \$ 0.41     |
| Diluted earnings per share                          | \$ 0.46  | \$ (0.06)  | \$ 0.40     |

**Consolidated Statement of Income** (unaudited)

Six Months Ended June 30, 2007

| (Dollars in thousands, except per share amounts)    | As        |            |             |
|---|-----------|------------|-------------|
|   | Reported  | Adjustment | As Restated |
| Interest income on taxable securities               | \$ 15,501 | \$ 130     | \$ 15,631   |
| Interest expense on FHLB advances                   | 10,031    | 49         | 10,080      |
| Net interest income                                 | 29,716    | 81         | 29,797      |
| Net interest income after provision for loan losses | 29,116    | 81         | 29,197      |
| Net realized gains on securities                    | 1,741     | (1,405)    | 336         |
| Total noninterest income                            | 23,776    | (1,405)    | 22,371      |
| Other noninterest expense                           | 3,870     | (115)      | 3,755       |
| Total noninterest expense                           | 34,984    | (115)      | 34,869      |
| Income before taxes                                 | 17,908    | (1,209)    | 16,699      |

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

|                    |         |           |         |
|--------------------|---------|-----------|---------|
| Income tax expense | 5,623   | (381)     | 5,242   |
| Net income         | 12,285  | (828)     | 11,457  |
| Basic earnings     | \$ 0.92 | \$ (0.06) | \$ 0.86 |
| Diluted earnings   | \$ 0.90 | \$ (0.06) | \$ 0.84 |

-9-

---



**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

**Consolidated Statement of Cash Flows** (unaudited)**Six Months Ended June 30, 2007**

| (Dollars in thousands)  | As        |            |             |
|---|-----------|------------|-------------|
|   | Reported  | Adjustment | As Restated |
| <b>Cash flows from operating activities:</b>                                      |           |            |             |
| Net income  | \$ 12,285 | \$ (828)   | \$ 11,457   |
| Adjustments to reconcile net income to net cash provided by operating activities: |           |            |             |
| Net amortization of premium and discount  | 433       | (79)       | 354         |
| Net realized gains on sales of securities   | (1,741)   | 1,405      | (336)       |
| Increase in other assets  | (607)     | (380)      | (987)       |
| Net cash provided by operating activities   | 9,434     | 118        | 9,552       |
| <b>Cash flows from investing activities:</b>                                      |           |            |             |
| Purchases of:   |           |            |             |
| Mortgage-backed securities available for sale                                     | (29,065)  | (84,584)   | (113,649)   |
| Other investment securities available for sale                                    | (18,865)  | (15,031)   | (33,896)    |
| Mortgage-backed securities held to maturity                                       | -         | -          | -           |
| Other investment securities held to maturity                                      | (16,011)  | 3,129      | (12,882)    |
| Proceeds from sale of:  |           |            |             |
| Mortgage-backed securities available for sale                                     | -         | 47,938     | 47,938      |
| Other investment securities available for sale                                    | 9,438     | -          | 9,438       |
| Mortgage-backed securities held to maturity                                       | 1,954     | 36,547     | 38,501      |
| Other investment securities held to maturity                                      | 9,815     | 11,883     | 21,698      |
| Maturities and principal payments of:   |           |            |             |
| Mortgage-backed securities available for sale                                     | 29,542    | 3,041      | 32,583      |
| Other investment securities available for sale                                    | 5,982     | 450        | 6,432       |
| Mortgage-backed securities held to maturity                                       | 6,232     | (3,041)    | 3,191       |
| Other investment securities held to maturity                                      | 20,940    | (450)      | 20,490      |
| Net cash used in investing activities   | (19,376)  | (118)      | (19,494)    |
| <b>Cash flows from financing activities:</b>                                      |           |            |             |
| Proceeds from Federal Home Loan Bank advances                                     | 344,719   | 47,000     | 391,719     |
| Repayment of Federal Home Loan Bank advances                                      | (350,433) | (47,000)   | (397,433)   |
| Net cash provided by financing activities   | (3,951)   | -          | (3,951)     |
| Net decrease in cash and cash and cash equivalents                                | (13,893)  | -          | (13,893)    |

**(2) New Accounting Pronouncements**

In February 2006, the Financial Accounting Standards Board ("FASB") issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments - an amendment of FASB Statements No. 133 and 140" ("SFAS No. 155"). SFAS No. 155 eliminates the exemption from applying SFAS No. 133 to interests in securitized financial assets so that similar instruments are accounted for similarly regardless of the form of the instruments. SFAS No. 155 also allows a preparer to elect fair value measurement at acquisition, at issuance, or when a previously recognized financial instrument is subject to a remeasurement event, on an instrument-by-instrument basis, in cases in which a derivative would otherwise have to be bifurcated. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. Provisions of SFAS No. 155 may be applied to instruments that an entity holds at the date of adoption on an instrument-by-instrument basis. Prior periods should not be restated. The adoption of SFAS No. 155 did not have a material impact on the Corporation's financial

position or results of operations.

In March 2006, the FASB issued SFAS No. 156, “Accounting for Servicing of Financial Assets – an amendment of FASB Statement No. 140” (“SFAS No. 156”). SFAS No. 156 requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value. SFAS No. 156 permits, but does not require, the subsequent measurement of servicing assets and servicing liabilities at fair value. An entity that used derivative instruments to mitigate the risks inherent in servicing assets and servicing liabilities is required to account for those derivative instruments at fair value. SFAS No. 156 is effective as of the beginning of the first fiscal year that begins

-10-

---

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

**(Continued)**

after September 15, 2006. The adoption of SFAS No. 156 did not have a material impact on the Corporation's financial position or results of operations.

Effective January 1, 2007, the Corporation adopted the provisions of FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109" ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, "Accounting for Income Taxes." FIN 48 also prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. In addition, FIN 48 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The adoption of FIN 48 did not have a material impact on the Corporation's financial position or results of operations.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS No. 157"). This Statement defines fair value, establishes a framework for measuring fair value and expands disclosures of fair value measurements. SFAS No. 157 applies to the accounting principles that currently use fair value measurement, and does not require any new fair value measurements. The expanded disclosures focus on the inputs used to measure fair value as well as the effect of the fair value measurements on earnings. SFAS No. 157 is effective as of the beginning of the first fiscal year beginning after November 15, 2007 and interim periods within that fiscal year. The Corporation believes the adoption of SFAS No. 157 will not have a material impact on the Corporation's financial position or results of operations.

In September 2006, the FASB issued SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Post Retirement Plans (an amendment of FASB Statements No. 87, 88, 106 and 132R)" ("SFAS No. 158"). The recognition and disclosure provisions of SFAS No. 158 were adopted by the Corporation for the fiscal year ended December 31, 2006. Upon adoption, the funded status of an employer's postretirement benefit plan was recognized in the statement of financial position and the changes in funded status of the defined benefit plan, including actuarial gains and losses and prior service costs and credits were recognized in comprehensive income. The requirement to measure the plan's assets and obligations as of the employers fiscal year end is effective for fiscal years ending after December 15, 2008. The Corporation is currently evaluating the impact the measurement date provisions of SFAS No. 158 will have on its consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159. SFAS No. 159 permits entities to choose to measure eligible items at fair value at specified election dates. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings at each subsequent reporting date. The fair value option (i) may be applied instrument-by-instrument with certain exceptions, (ii) is irrevocable (unless a new election date occurs) and (iii) is applied only to entire instruments and not to portions of instruments. SFAS No. 159 is effective as of the beginning of the first fiscal year that begins after November 15, 2007. Early adoption was permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elected to apply the provisions of SFAS No. 157, "Fair Value Instruments." Based on our assessment of the provisions of SFAS 159, on April 12, 2007 we decided to implement early adoption of SFAS 159. In connection with this adoption, we selected the fair value option for certain U.S. Government sponsored agency and mortgage-backed securities with lower coupons and slower prepayment characteristics in the held-to-maturity portfolio totaling approximately \$61.9 million. A portfolio restructuring plan was also undertaken to reduce interest rate risk and improve net interest margin, which included the sale of these securities. On Friday April 13, 2007 we executed sale trades for these held-to-maturity securities. At the time of the sales transactions the historical amortized cost basis of the sold securities exceeded the total sales price by \$1.7 million. On Monday April 16, 2007 additional information became available regarding clarifications of the

interpretation of the application of SFAS 159 by applicable regulatory and accounting industry bodies that led us to conclude that the application of SFAS 159 to our transactions might be inconsistent with the intent and spirit of SFAS 159. Consequently, we decided not to early-adopt SFAS 159. See further discussion regarding the restatement in Note 1 and Note 3 to the Consolidated Financial Statements.

-11-

---

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

**(3) Securities**

Securities available for sale are summarized as follows:

| (Dollars in thousands)   | Amortized<br>Cost | Unrealized<br>Gains | Unrealized<br>Losses | Fair<br>Value |
|--|-------------------|---------------------|----------------------|---------------|
| <b>September 30, 2007 (As Restated)</b>  |                   |                     |                      |               |
| U.S. Treasury obligations and obligations<br>of U.S. government-sponsored agencies | \$ 173,396        | \$ 1,381            | \$ (89)              | \$ 174,688    |
| Mortgage-backed securities issued by<br>U.S. government-sponsored agencies         | 369,718           | 1,099               | (4,858)              | 365,959       |
| States and political subdivision   | 80,640            | 85                  | (746)                | 79,979        |
| Trust preferred securities   | 38,010            | –                   | (2,410)              | 35,600        |
| Corporate bonds  | 16,954            | 38                  | (28)                 | 16,964        |
| Corporate stocks   | 13,118            | 3,120               | (719)                | 15,519        |
| Total  | 691,836           | 5,723               | (8,850)              | 688,709       |
| <b>December 31, 2006</b>   |                   |                     |                      |               |
| U.S. Treasury obligations and obligations<br>of U.S. government-sponsored agencies | 157,383           | 778                 | (876)                | 157,285       |
| Mortgage-backed securities issued by<br>U.S. government-sponsored agencies         | 298,038           | 923                 | (5,174)              | 293,787       |
| Trust preferred securities   | 30,571            | 208                 | (205)                | 30,574        |
| Corporate bonds  | 24,998            | 83                  | (47)                 | 25,034        |
| Corporate stocks   | 14,976            | 4,915               | (175)                | 19,716        |
| Total  | \$ 525,966        | \$ 6,907            | \$ (6,477)           | \$ 526,396    |

Securities held to maturity are summarized as follows:

| (Dollars in thousands)   | Amortized<br>Cost | Unrealized<br>Gains | Unrealized<br>Losses | Fair<br>Value |
|--|-------------------|---------------------|----------------------|---------------|
| <b>December 31, 2006</b>   |                   |                     |                      |               |
| U.S. Treasury obligations and obligations<br>of U.S. government-sponsored agencies | \$ 42,000         | \$ –                | \$ (422)             | \$ 41,578     |
| Mortgage-backed securities issued by<br>U.S. government-sponsored agencies         | 69,340            | 440                 | (1,604)              | 68,176        |
| States and political subdivisions  | 66,115            | 88                  | (588)                | 65,615        |
| Total  | \$ 177,455        | \$ 528              | \$ (2,614)           | \$ 175,369    |

In connection with a planned early adoption of SFAS No. 159, the Corporation sold twelve held to maturity securities with an amortized cost of \$61.9 million on April 13, 2007. The Corporation subsequently decided not to early-adopt SFAS No. 159 and realized securities losses of \$1.7 million were recognized in the second quarter of 2007 (as restated). In addition, the remaining held-to-maturity portfolio was reclassified to the available-for-sale category as of the April 13, 2007 sale date of the securities. The Corporation will not be able to classify securities in the held-to-maturity category for a period of two years from the April 13, 2007 sales date as a result of this action. See additional discussion regarding the restatement in Note 1 to the Consolidated Financial Statements.

Securities available for sale with a fair value of \$528.9 million and securities available for sale and held to maturity with a fair value of \$557.4 million were pledged in compliance with state regulations concerning trust powers and to secure Treasury Tax and Loan deposits, borrowings, and certain public deposits at September 30, 2007 and December 31, 2006, respectively. In addition, securities available for sale with a fair value of \$8.3 million and securities available for sale and held to maturity with a fair value of \$9.6 million were collateralized for the discount window at the Federal Reserve Bank at September 30, 2007 and December 31, 2006, respectively. There were no borrowings with the Federal Reserve Bank at either date. Securities available for sale with a fair value of \$1.9 million and \$2.1 million were designated in a rabbi trust for a nonqualified retirement plan at September 30, 2007 and

-12-

---

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES** (Continued)  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2006. As of September 30, 2007, securities available for sale with a fair value of \$21.5 million were pledged as collateral to secure securities sold under agreements to repurchase.

At September 30, 2007 and December 31, 2006, the securities portfolio included \$3.1 million and \$1.7 million of net pretax unrealized losses, respectively. Included in these net amounts were gross unrealized losses amounting to \$8.9 million and \$9.1 million at September 30, 2007 and December 31, 2006, respectively.

The following tables summarize, for all securities in an unrealized loss position at September 30, 2007 and December 31, 2006, respectively, the aggregate fair value and gross unrealized loss by length of time those securities have been continuously in an unrealized loss position.

| (Dollars in thousands)<br>(As Restated)   | Less than 12 Months |            |                   | 12 Months or Longer |            |                   | Total |            |                   |
|---|---------------------|------------|-------------------|---------------------|------------|-------------------|-------|------------|-------------------|
|   | #                   | Fair Value | Unrealized Losses | #                   | Fair Value | Unrealized Losses | #     | Fair Value | Unrealized Losses |
| <b>At September 30, 2007</b>  |                     |            |                   |                     |            |                   |       |            |                   |
| U.S. Treasury obligations and obligations of U.S. government-sponsored agencies |                     | -\$        | -\$               | 5                   | \$ 27,162  | \$ 89             | 5     | \$ 27,162  | \$ 89             |
| Mortgage-backed securities issued by U.S. government-sponsored agencies         | 19                  | 79,778     | 704               | 62                  | 185,462    | 4,154             | 81    | 265,240    | 4,858             |
| States and political subdivisions   | 69                  | 57,400     | 567               | 13                  | 8,134      | 179               | 82    | 65,534     | 746               |
| Trust preferred securities  | 8                   | 24,572     | 1,381             | 5                   | 11,029     | 1,029             | 13    | 35,601     | 2,410             |
| Corporate bonds   | 2                   | 6,120      | 18                | 1                   | 2,993      | 10                | 3     | 9,113      | 28                |
| Subtotal, debt securities   | 98                  | 167,870    | 2,670             | 86                  | 234,780    | 5,461             | 184   | 402,650    | 8,131             |
| Corporate stocks  | 6                   | 6,632      | 620               | 3                   | 938        | 99                | 9     | 7,570      | 719               |
| Total temporarily impaired securities   | 104                 | \$ 174,502 | \$ 3,290          | 89                  | \$ 235,718 | \$ 5,560          | 193   | \$ 410,220 | \$ 8,850          |

| (Dollars in thousands)  | Less than 12 Months |            |                   | 12 Months or Longer |            |                   | Total |            |                   |
|---|---------------------|------------|-------------------|---------------------|------------|-------------------|-------|------------|-------------------|
|   | #                   | Fair Value | Unrealized Losses | #                   | Fair Value | Unrealized Losses | #     | Fair Value | Unrealized Losses |
| <b>At December 31, 2006</b>   |                     |            |                   |                     |            |                   |       |            |                   |
| U.S. Treasury obligations and obligations of U.S. government-sponsored agencies | 8                   | \$ 52,751  | \$ 211            | 14                  | \$ 94,393  | \$ 1,087          | 22    | \$ 147,144 | \$ 1,298          |
| Mortgage-backed securities issued by U.S. government-sponsored agencies         | 7                   | 20,620     | 122               | 69                  | 240,457    | 6,656             | 76    | 261,077    | 6,778             |
| States and political subdivisions   | 61                  | 45,948     | 419               | 12                  | 6,747      | 169               | 73    | 52,695     | 588               |
| Trust preferred securities  | -                   | -          | -                 | 7                   | 14,840     | 205               | 7     | 14,840     | 205               |

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

|  |    |            |        |     |            |          |     |            |          |
|--|----|------------|--------|-----|------------|----------|-----|------------|----------|
| Corporate bonds                          | 2  | 6,130      | 34     | 1   | 3,006      | 13       | 3   | 9,136      | 47       |
| Subtotal, debt securities                | 78 | 125,449    | 786    | 103 | 359,443    | 8,130    | 181 | 484,892    | 8,916    |
| Corporate stocks                         | 5  | 5,823      | 110    | 4   | 1,494      | 65       | 9   | 7,317      | 175      |
| Total temporarily<br>impaired securities | 83 | \$ 131,272 | \$ 896 | 107 | \$ 360,937 | \$ 8,195 | 190 | \$ 492,209 | \$ 9,091 |

-13-

---



**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

For those debt securities whose amortized cost exceeds fair value, the primary cause is related to the movement of interest rates. The Corporation believes that the nature and duration of impairment on its debt security holdings are primarily a function of interest rate movements and changes in investment spreads, and does not consider full repayment of principal on the reported debt obligations to be at risk. The Corporation has the ability and intent to hold these investments to full recovery of the cost basis. The debt securities in an unrealized loss position at September 30, 2007 consisted of 184 debt security holdings. The largest loss percentage of any single holding was 11.45% of its amortized cost.

Causes of conditions whereby the fair value of corporate stock equity securities is less than cost include the timing of purchases and changes in valuation specific to individual industries or issuers. The relationship between the level of market interest rates and the dividend rates paid on individual equity securities may also be a contributing factor. The Corporation believes that the nature and duration of impairment on its equity securities holdings are considered to be a function of general financial market movements and industry conditions. The equity securities in an unrealized loss position at September 30, 2007 consisted of 9 holdings of financial and commercial entities.

**(4) Loan Portfolio**

The following is a summary of loans:

| (Dollars in thousands)               | September 30, 2007  |             | December 31, 2006   |             |
|--------------------------------------|---------------------|-------------|---------------------|-------------|
|                                      | Amount              | %           | Amount              | %           |
| <b>Commercial:</b>                   |                     |             |                     |             |
| Mortgages (1)                        | \$ 276,995          | 18%         | \$ 282,019          | 19%         |
| Construction and development (2)     | 48,899              | 3%          | 32,233              | 2%          |
| Other (3)                            | 324,129             | 22%         | 273,145             | 19%         |
| <b>Total commercial</b>              | <b>650,023</b>      | <b>43%</b>  | <b>587,397</b>      | <b>40%</b>  |
| <b>Residential real estate:</b>      |                     |             |                     |             |
| Mortgages (4)                        | 566,776             | 37%         | 577,522             | 39%         |
| Homeowner construction               | 12,040              | 1%          | 11,149              | 1%          |
| <b>Total residential real estate</b> | <b>578,816</b>      | <b>38%</b>  | <b>588,671</b>      | <b>40%</b>  |
| <b>Consumer:</b>                     |                     |             |                     |             |
| Home equity lines                    | 139,732             | 9%          | 145,676             | 10%         |
| Home equity loans                    | 99,798              | 7%          | 93,947              | 6%          |
| Other                                | 46,124              | 3%          | 44,295              | 4%          |
| <b>Total consumer</b>                | <b>285,654</b>      | <b>19%</b>  | <b>283,918</b>      | <b>20%</b>  |
| <b>Total loans (5)</b>               | <b>\$ 1,514,493</b> | <b>100%</b> | <b>\$ 1,459,986</b> | <b>100%</b> |

(1) Amortizing mortgages, primarily secured by income producing property.

(2) Loans for construction of residential and commercial properties and for land development.

(3) Loans to businesses and individuals, a substantial portion of which are fully or partially collateralized by real estate.

(4) A substantial portion of these loans is used as qualified collateral for FHLB borrowings (See Note 8 for additional discussion of FHLB borrowings).

(5) Net of unamortized loan origination fees, net of costs, totaling \$92 thousand and \$277 thousand at September 30, 2007 and December 31, 2006, respectively. Also includes \$130 thousand and \$342 thousand of premium, net of

discount, on purchased loans at September 30, 2007 and December 31, 2006, respectively.

-14-

---

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

**(5) Allowance for Loan Losses**

The following is an analysis of the allowance for loan losses:

(Dollars in thousands)

| Periods ended September 30,                | Three Months |           | Nine Months |           |
|--|--------------|-----------|-------------|-----------|
|  | 2007         | 2006      | 2007        | 2006      |
| Balance at beginning of period             | \$ 19,327    | \$ 18,480 | \$ 18,894   | \$ 17,918 |
| Provision charged to expense               | 300          | 300       | 900         | 900       |
| Recoveries of loans previously charged off | 27           | 39        | 231         | 152       |
| Loans charged off                          | (182)        | (174)     | (553)       | (325)     |
| Balance at end of period                   | \$ 19,472    | \$ 18,645 | \$ 19,472   | \$ 18,645 |

**(6) Goodwill and Other Intangibles**

The changes in the carrying value of goodwill and other intangible assets for the nine months ended September 30, 2007 are as follows:

**Goodwill**

(Dollars in thousands)

|   | Commercial<br>Banking<br>Segment | Wealth                           | Total     |
|---|----------------------------------|----------------------------------|-----------|
|   |                                  | Management<br>Service<br>Segment |           |
| Balance at December 31, 2006            | \$ 22,591                        | \$ 21,967                        | \$ 44,558 |
| Additions to goodwill during the period | —                                | 5,921                            | 5,921     |
| Impairment recognized                   | —                                | —                                | —         |
| Balance at September 30, 2007           | \$ 22,591                        | \$ 27,888                        | \$ 50,479 |

During the third quarter of 2007, the Corporation recognized a liability of \$5.9 million, with a corresponding increase in goodwill, related to the acquisition of Weston Financial Group, Inc. (“Weston Financial”) in August 2005. This amount represents the 2007 obligation under the terms of the acquisition agreement, which provides for a contingent payment earn-out in each year during the three-year period ending December 31, 2008.

**Other Intangible Assets**

|                               | Core                  | Advisory<br>Contracts | Non-compet | Total     |
|-------------------------------|-----------------------|-----------------------|------------|-----------|
|                               | Deposit<br>Intangible |                       | Agreements |           |
| Balance at December 31, 2006  | \$ 650                | \$ 11,937             | \$ 229     | \$ 12,816 |
| Amortization                  | 109                   | 911                   | 37         | 1,057     |
| Balance at September 30, 2007 | \$ 541                | \$ 11,026             | \$ 192     | \$ 11,759 |

Amortization of intangible assets for the nine months ended September 30, 2007 totaled \$1.1 million. Estimated annual amortization expense of current intangible assets with finite useful lives, absent any impairment or change in estimated useful lives, is summarized below.

(Dollars in thousands)

|                                 | Core<br>Deposits | Advisory<br>Contracts | Non-compet<br>Agreements | Total |
|---------------------------------|------------------|-----------------------|--------------------------|-------|
| Estimated amortization expense: |                  |                       |                          |       |

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

|                  |    |     |    |       |    |    |    |       |
|------------------|----|-----|----|-------|----|----|----|-------|
| 2007 (full year) | \$ | 140 | \$ | 1,194 | \$ | 49 | \$ | 1,383 |
| 2008             |    | 120 |    | 1,111 |    | 49 |    | 1,280 |
| 2009             |    | 120 |    | 1,040 |    | 49 |    | 1,209 |
| 2010             |    | 120 |    | 922   |    | 49 |    | 1,091 |
| 2011             |    | 120 |    | 768   |    | 33 |    | 921   |

-15-

---

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

The components of intangible assets at September 30, 2007 are as follows:

(Dollars in thousands)

|                          | Core<br>Deposits | Advisory<br>Contracts | Non-compete<br>Agreements | Total     |
|--------------------------|------------------|-----------------------|---------------------------|-----------|
| Gross carrying amount    | \$ 2,997         | \$ 13,657             | \$ 1,147                  | \$ 17,801 |
| Accumulated amortization | 2,456            | 2,631                 | 955                       | 6,042     |
| Net amount               | \$ 541           | \$ 11,026             | \$ 192                    | \$ 11,759 |

**(7) Income Taxes**

Effective January 1, 2007, the Corporation adopted FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"). The adoption of FIN 48 did not result in any adjustment to retained earnings as of January 1, 2007.

As of the adoption date, the Corporation had gross tax affected unrecognized tax benefits of \$1.2 million. If recognized, this amount would be recorded as a component of income tax expense. There have been no significant changes to this during the nine months ended September 30, 2007.

The Corporation recognizes potential accrued interest related to unrecognized tax benefits in income tax expense in the Consolidated Statements of Income. As of the adoption date of January 1, 2007, accrued interest amounted to \$70 thousand. To the extent interest is not assessed with respect to uncertain tax positions, amounts accrued will be reduced and reflected as a reduction of the overall income tax provision. Penalties, if incurred, would be recognized as a component of income tax expense.

The Corporation files income tax returns in the U.S. federal jurisdiction and various state jurisdictions. The Corporation is no longer subject to U.S. federal income tax examinations by tax authorities for years before 2003. With a few exceptions, the Corporation is no longer subject to state income tax examinations by tax authorities for years before 2000.

**(8) Borrowings****Federal Home Loan Bank Advances**

Advances payable to the Federal Home Loan Bank ("FHLB") are summarized as follows:

(Dollars in thousands)

|               | September 30,<br>2007 | December 31,<br>2006 |
|---------------|-----------------------|----------------------|
| FHLB advances | \$ 502,265            | \$ 474,561           |

During the first quarter of 2007, the Corporation prepaid \$26.5 million in advances payable to the FHLB resulting in a debt prepayment penalty charge, recorded in noninterest expense, of \$1.1 million. See additional discussion in Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations," under the caption "Noninterest Expense."

In addition to outstanding advances, the Corporation also has access to an unused line of credit amounting to \$8.0 million at September 30, 2007. Under an agreement with the FHLB, the Corporation is required to maintain qualified collateral, free and clear of liens, pledges, or encumbrances that, based on certain percentages of book and market values, has a value equal to the aggregate amount of the line of credit and outstanding advances ("FHLB

borrowings”). The FHLB maintains a security interest in various assets of the Corporation including, but not limited to, residential mortgages loans, U.S. government or agency securities, U.S. government-sponsored agency securities, and amounts maintained on deposit at the FHLB. The Corporation maintained qualified collateral in excess of the amount required to collateralize the line of credit and outstanding advances at September 30, 2007. Included in the collateral were securities available for sale with a fair value of \$402.4 million and securities available for sale and held to maturity with a fair value of \$451.5 million that were specifically pledged to secure FHLB borrowings at September 30, 2007 and December 31, 2006, respectively. Unless there is an event of default under the agreement

-16-

---

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

with the FHLB, the Corporation may use, encumber or dispose of any portion of the collateral in excess of the amount required to secure FHLB borrowings, except for that collateral that has been specifically pledged.

**Other Borrowings**

The following is a summary of other borrowings:

| (Dollars in thousands)                      | September 30,<br>2007 | December<br>31,<br>2006 |
|---|-----------------------|-------------------------|
| Treasury, Tax and Loan demand note balance  | \$ 6,742              | \$ 3,863                |
| Deferred acquisition obligations            | 9,772                 | 10,372                  |
| Securities sold under repurchase agreements | 19,500                | -                       |
| Other                                       | 389                   | 449                     |
| Other borrowings                            | \$ 36,403             | \$ 14,684               |

In the first quarter of 2007, securities sold under repurchase agreements of \$19.5 million were executed. The securities sold under agreements to repurchase are callable at the issuer's option, at one time only, in one year and mature in five years. The securities underlying the agreements are held in safekeeping by the counterparty in the name of the Corporation and are repurchased when the agreement matures. Accordingly, these underlying securities are included in securities available for sale and the obligations to repurchase such securities are reflected as a liability.

The Stock Purchase Agreement for the August 2005 acquisition of Weston Financial provides for the payment of contingent purchase price amounts based on operating results in each of the years in the three-year earn-out period ending December 31, 2008. Contingent payments are added to goodwill and recorded as deferred acquisition liabilities at the time the payments are determinable beyond a reasonable doubt. Deferred acquisition obligations amounted to \$9.8 million at September 30, 2007 compared to \$10.4 million at December 31, 2006. During the third quarter of 2007 the Corporation recognized a liability of \$5.9 million, representing the 2007 portion of the earn-out period. In the first quarter of 2007 the Corporation paid approximately \$6.7 million, which represented the 2006 earn-out payment.

**(9) Shareholders' Equity****Stock Repurchase Plan:**

Under the Corporation's 2006 Stock Repurchase Plan, 185,400 shares of stock were repurchased at a total cost of \$4.8 million during the nine months ended September 30, 2007. In addition, 14,785 shares were acquired in the same period pursuant to the Nonqualified Deferred Compensation Plan.

-17-

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

**Regulatory Capital Requirements:**

The following table presents the Corporation's and the Bank's actual capital amounts and ratios at September 30, 2007 and December 31, 2006, as well as the corresponding minimum regulatory amounts and ratios:

| (Dollars in thousands)                             | Actual     |        | For Capital Adequacy<br>Purposes |       | To Be Well Capitalized<br>Under Prompt Corrective<br>Action Provisions |        |
|--|------------|--------|----------------------------------|-------|--|--------|
|  | Amount     | Ratio  | Amount                           | Ratio | Amount   | Ratio  |
| <b>As of September 30,<br/>2007: (As Restated)</b> |            |        |                                  |       |  |        |
| Total Capital (to<br>Risk-Weighted Assets):        |            |        |                                  |       |  |        |
| Corporation  | \$ 163,269 | 10.43% | \$ 125,220                       | 8.00% | \$ 156,525   | 10.00% |
| Bank   | \$ 170,327 | 10.89% | \$ 125,141                       | 8.00% | \$ 156,426   | 10.00% |
| Tier 1 Capital (to<br>Risk-Weighted Assets):       |            |        |                                  |       |  |        |
| Corporation  | \$ 142,621 | 9.11%  | \$ 62,610                        | 4.00% | \$ 93,915  | 6.00%  |
| Bank   | \$ 149,691 | 9.57%  | \$ 62,570                        | 4.00% | \$ 93,856  | 6.00%  |
| Tier 1 Capital (to Average<br>Assets): (1)         |            |        |                                  |       |  |        |
| Corporation  | \$ 142,621 | 6.11%  | \$ 93,330                        | 4.00% | \$ 116,662   | 5.00%  |
| Bank   | \$ 149,691 | 6.42%  | \$ 93,282                        | 4.00% | \$ 116,602   | 5.00%  |
| <b>As of December 31,<br/>2006:</b>                |            |        |                                  |       |  |        |
| Total Capital (to<br>Risk-Weighted Assets):        |            |        |                                  |       |  |        |
| Corporation  | \$ 161,076 | 10.96% | \$ 117,538                       | 8.00% | \$ 146,922   | 10.00% |
| Bank   | \$ 168,235 | 11.46% | \$ 117,465                       | 8.00% | \$ 146,832   | 10.00% |
| Tier 1 Capital (to<br>Risk-Weighted Assets):       |            |        |                                  |       |  |        |
| Corporation  | \$ 140,568 | 9.57%  | \$ 58,769                        | 4.00% | \$ 88,153  | 6.00%  |
| Bank   | \$ 147,738 | 10.06% | \$ 58,733                        | 4.00% | \$ 88,099  | 6.00%  |
| Tier 1 Capital (to Average<br>Assets): (1)         |            |        |                                  |       |  |        |
| Corporation  | \$ 140,568 | 6.01%  | \$ 93,487                        | 4.00% | \$ 116,858   | 5.00%  |
| Bank   | \$ 147,738 | 6.32%  | \$ 93,437                        | 4.00% | \$ 116,797   | 5.00%  |

(1) Leverage ratio

The Corporation's capital ratios at September 30, 2007 place the Corporation in the "well-capitalized" category according to regulatory standards.

**(10) Financial Instruments with Off-Balance Sheet Risk and Derivative Financial Instruments**



The Corporation is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers and to manage the Corporation's exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit, standby letters of credit, financial guarantees, and commitments to originate and commitments to sell fixed rate mortgage loans. These instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the Corporation's Consolidated Balance Sheets. The contract or notional amounts of these instruments reflect the extent of involvement the Corporation has in particular classes of financial instruments. The Corporation uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The contractual and notional amounts of financial instruments with off-balance sheet risk are as follows:

-18-

---

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

| (Dollars in thousands)   | September 30,<br>2007 | December 31,<br>2006 |
|--|-----------------------|----------------------|
| Financial instruments whose contract amounts represent credit risk:            |                       |                      |
| Commitments to extend credit:  |                       |                      |
| Commercial loans   | \$ 151,229            | \$ 122,376           |
| Home equity lines  | 179,300               | 185,483              |
| Other loans  | 26,814                | 10,671               |
| Standby letters of credit  | 8,941                 | 9,401                |
| Financial instruments whose notional amounts exceed the amount of credit risk: |                       |                      |
| Forward loan commitments:  |                       |                      |
| Commitments to originate fixed rate mortgage loans to be sold                  | 2,870                 | 2,924                |
| Commitments to sell fixed rate mortgage loans                                  | 4,966                 | 5,066                |

**Commitments to Extend Credit**

Commitments to extend credit are agreements to lend to a customer as long as there are no violations of any conditions established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Each borrower's creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained is based on management's credit evaluation of the borrower.

**Standby Letters of Credit**

Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Under the standby letters of credit, the Corporation is required to make payments to the beneficiary of the letters of credit upon request by the beneficiary contingent upon the customer's failure to perform under the terms of the underlying contract with the beneficiary. Standby letters of credit extend up to five years. At September 30, 2007 and December 31, 2006, the maximum potential amount of undiscounted future payments, not reduced by amounts that may be recovered, totaled \$8.9 million and \$9.4 million, respectively. At September 30, 2007 and December 31, 2006, there was no liability to beneficiaries resulting from standby letters of credit. Fee income on standby letters of credit for the nine months ended September 30, 2007 and 2006 totaled \$75 thousand and \$86 thousand, respectively.

At September 30, 2007, a substantial portion of the standby letters of credit were supported by pledged collateral. The collateral obtained is determined based on management's credit evaluation of the customer. Should the Corporation be required to make payments to the beneficiary, repayment from the customer to the Corporation is required.

**Forward Loan Commitments**

Commitments to originate and commitments to sell fixed rate mortgage loans are derivative financial instruments. Accordingly, the fair value of these commitments is recognized in other assets on the balance sheet and changes in fair value of such commitments are recorded in current earnings in the income statement. The carrying value of such commitments as of September 30, 2007 and December 31, 2006 and the respective changes in fair values for the nine months ended September 30, 2007 and 2006 were insignificant.

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

**(11) Defined Benefit Pension Plans****Components of Net Periodic Benefit Costs:**

(Dollars in thousands)

|                                    | Qualified<br>Pension Plan |          | Non-Qualified<br>Retirement Plans |        |
|------------------------------------|---------------------------|----------|-----------------------------------|--------|
|                                    | 2007                      | 2006     | 2007                              | 2006   |
| Nine months ended September 30,    |                           |          |                                   |        |
| Service cost                       | \$ 1,508                  | \$ 1,551 | \$ 259                            | \$ 264 |
| Interest cost                      | 1,386                     | 1,238    | 389                               | 351    |
| Expected return on plan assets     | (1,488)                   | (1,350)  | -                                 | -      |
| Amortization of transition asset   | (4)                       | (4)      | -                                 | -      |
| Amortization of prior service cost | (25)                      | (26)     | 47                                | 46     |
| Recognized net actuarial loss      | 140                       | 238      | 163                               | 160    |
| Net periodic benefit cost          | \$ 1,517                  | \$ 1,647 | \$ 858                            | \$ 821 |

**Assumptions:**

The measurement date and weighted-average assumptions used to determine net periodic benefit cost for the nine months ended September 30, 2007 and 2006 were as follows:

|  | Qualified<br>Pension Plan |                           | Non-Qualified<br>Retirement Plans |                           |
|--|---------------------------|---------------------------|-----------------------------------|---------------------------|
|  | 2007<br>Sept. 30,<br>2006 | 2006<br>Sept. 30,<br>2005 | 2007<br>Sept. 30,<br>2006         | 2006<br>Sept. 30,<br>2005 |
| Measurement date                         |                           |                           |                                   |                           |
| Discount rate                            | 5.90%                     | 5.50%                     | 5.90%                             | 5.50%                     |
| Expected long-term return on plan assets | 8.25%                     | 8.25%                     | -                                 | -                         |
| Rate of compensation increase            | 4.25%                     | 4.25%                     | 4.25%                             | 4.25%                     |

As discussed in Note 2, the SFAS No. 158 requirement to measure the plan's assets and obligations as of the employer's fiscal year end is effective December 31, 2008.

**Employer Contributions:**

The Corporation previously disclosed in its financial statements for the year ended December 31, 2006 that it expected to contribute \$1.3 million to its qualified pension plan and \$369 thousand in benefit payments to its non-qualified retirement plans in 2007. During the nine month period ended September 30, 2007, approximately \$1.9 million of contributions were made to the qualified pension plan and no further contributions are expected for 2007. The increase in the qualified pension plan contribution over the amount estimated at December 31, 2006 was the result of further analysis by the Corporation and included an additional discretionary contribution in excess of statutory requirements. During the nine month period ended September 30, 2007, \$251 thousand in benefit payments have been made to the non-qualified retirement plans. The Corporation presently anticipates contributing an additional \$84 thousand in benefit payments to the non-qualified retirement plans in 2007.

-20-

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES** (Continued)  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(12) Business Segments**

Washington Trust segregates financial information in assessing its results among two operating segments: Commercial Banking and Wealth Management Services. The amounts in the Corporate column include activity not related to the segments, such as the investment securities portfolio, wholesale funding activities and administrative units. The Corporate column is not considered to be an operating segment. The methodologies and organizational hierarchies that define the business segments are periodically reviewed and revised. Results may be restated, when necessary, to reflect changes in organizational structure or allocation methodology. The following tables present the statement of operations and total assets for Washington Trust's reportable segments.

(Dollars in thousands)

|                                       | Commercial Banking |           | Wealth Management Services |        | Corporate |         | Consolidated Total |           |
|---------------------------------------|--------------------|-----------|----------------------------|--------|-----------|---------|--------------------|-----------|
|                                       | 2007               | 2006      | 2007                       | 2006   | 2007      | 2006    | 2007               | 2006      |
| Three months ended                    |                    |           |                            |        |           |         |                    |           |
| September 30,                         |                    |           |                            |        |           |         |                    |           |
| Net interest income (expense) \$      | 13,797             | 13,371    | (18)                       | (23)   | 1,531     | 2,518   | 15,310             | 15,866    |
| Noninterest income                    | 4,295              | 4,262     | 7,178                      | 6,465  | 377       | 56      | 11,850             | 10,783    |
| Total income                          | 18,092             | 17,633    | 7,160                      | 6,442  | 1,908     | 2,574   | 27,160             | 26,649    |
| Provision for loan losses             | 300                | 300       | —                          | —      | —         | —       | 300                | 300       |
| Depreciation and amortization expense | 618                | 551       | 423                        | 416    | 45        | 204     | 1,086              | 1,171     |
| Other noninterest expenses            | 10,076             | 9,461     | 4,420                      | 4,204  | 1,730     | 1,775   | 16,226             | 15,440    |
| Total noninterest expenses            | 10,994             | 10,312    | 4,843                      | 4,620  | 1,775     | 1,979   | 17,612             | 16,911    |
| Income before income taxes            | 7,098              | 7,321     | 2,317                      | 1,822  | 133       | 595     | 9,548              | 9,738     |
| Income tax expense (benefit)          | 2,495              | 2,558     | 898                        | 719    | (401)     | (117)   | 2,992              | 3,160     |
| Net income \$                         | 4,603              | 4,763     | 1,419                      | 1,103  | 534       | 712     | 6,556              | 6,578     |
| Total assets at period end            | 1,587,328          | 1,521,785 | 44,254                     | 38,934 | 800,180   | 842,547 | 2,431,762          | 2,403,266 |
| Expenditures for long-lived assets    | 123                | 461       | 38                         | 72     | 81        | 49      | 242                | 582       |

(Dollars in thousands)

|  | Commercial Banking | Wealth Management | Corporate | Consolidated Total |
|--|--------------------|-------------------|-----------|--------------------|
|--|--------------------|-------------------|-----------|--------------------|

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

| Nine months ended<br>September 30,    | Services  |           |          |          |                       |          |                       |           |
|---------------------------------------|-----------|-----------|----------|----------|-----------------------|----------|-----------------------|-----------|
|                                       | 2007      | 2006      | 2007     | 2006     | (As Restated)<br>2007 | 2006     | (As Restated)<br>2007 | 2006      |
| Net interest income (expense) \$      | 40,411    | \$ 40,381 | \$ (46)  | \$ (74)  | \$ 4,742              | \$ 6,191 | \$ 45,107             | \$ 46,498 |
| Noninterest income                    | 11,058    | 10,586    | 21,541   | 19,642   | 1,622                 | 1,522    | 34,221                | 31,750    |
| Total income                          | 51,469    | 50,967    | 21,495   | 19,568   | 6,364                 | 7,713    | 79,328                | 78,248    |
| Provision for loan losses             | 900       | 900       | -        | -        | -                     | -        | 900                   | 900       |
| Depreciation and amortization expense | 1,841     | 1,684     | 1,292    | 1,260    | 133                   | 552      | 3,266                 | 3,496     |
| Other noninterest expenses            | 28,363    | 27,146    | 13,332   | 12,988   | 7,220                 | 5,965    | 48,915                | 46,099    |
| Total noninterest expenses            | 31,104    | 29,730    | 14,624   | 14,248   | 7,353                 | 6,517    | 53,081                | 50,495    |
| Income before income taxes            | 20,365    | 21,237    | 6,871    | 5,320    | (989)                 | 1,196    | 26,247                | 27,753    |
| Income tax expense (benefit)          | 7,158     | 7,402     | 2,661    | 2,097    | (1,585)               | (574)    | 8,234                 | 8,925     |
| Net income                            | \$ 13,207 | \$ 13,835 | \$ 4,210 | \$ 3,223 | \$ 596                | \$ 1,770 | \$ 18,013             | \$ 18,828 |
| Total assets at period end            | 1,587,328 | 1,521,785 | 44,254   | 38,934   | 800,180               | 842,547  | 2,431,762             | 2,403,266 |
| Expenditures for long-lived assets    | 3,326     | 1,975     | 200      | 432      | 189                   | 212      | 3,715                 | 2,619     |

-21-

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

Management uses certain methodologies to allocate income and expenses to the business lines. A funds transfer pricing methodology is used to assign interest income and interest expense to each interest-earning asset and interest-bearing liability on a matched maturity funding basis. Certain indirect expenses are allocated to segments. These include support unit expenses such as technology and processing operations and other support functions. Taxes are allocated to each segment based on the effective rate for the period shown.

**Commercial Banking**

The Commercial Banking segment includes commercial, commercial real estate, residential and consumer lending activities; mortgage banking, secondary market and loan servicing activities; deposit generation; merchant credit card services; cash management activities; and direct banking activities, which include the operation of ATMs, telephone and internet banking services and customer support and sales.

**Wealth Management Services**

Wealth Management Services includes asset management services provided for individuals and institutions; personal trust services, including services as executor, trustee, administrator, custodian and guardian; corporate trust services, including services as trustee for pension and profit sharing plans; and other financial planning and advisory services.

**Corporate**

Corporate includes the Treasury Unit, which is responsible for managing the wholesale investment portfolio and wholesale funding needs. It also includes income from bank-owned life insurance as well as administrative and executive expenses not allocated to the business lines and the residual impact of methodology allocations such as funds transfer pricing offsets.

**(13) Comprehensive Income**

(Dollars in thousands)

| Nine months ended September 30,  | (As<br>Restated)<br>2007 | 2006             |
|--|--------------------------|------------------|
| Net income   | \$ 18,013                | \$ 18,828        |
| Unrealized holding (gains) losses on securities available for sale, net of \$1,127 income tax benefit in 2007 (as restated) and \$170 income tax benefit in 2006                                 | (2,093)                  | 740              |
| Reclassification adjustments for gains arising during the period, net of \$148 income tax expense in 2007 (as restated) and \$321 income tax expense in 2006                                     | (188)                    | (137)            |
| Change in funded status of defined benefit plans related to the amortization of net actuarial losses, net prior service credit and net transition asset, net of \$165 income tax expense in 2007 | 209                      | -                |
| <b>Total comprehensive income</b>  | <b>\$ 15,941</b>         | <b>\$ 19,431</b> |

**WASHINGTON TRUST BANCORP INC. AND SUBSIDIARIES**  
**CONDENSED NOTES TO CONSOLIDATED FINANCIAL**  
**STATEMENTS**

(Continued)

**(14) Earnings Per Share**

Basic earnings per share (“EPS”) is calculated by dividing net income by the weighted average common stock outstanding, excluding options and other equity instruments. The dilutive effect of options, nonvested share units, non vested share awards and other items is calculated using the treasury stock method for purposes of weighted average dilutive shares. Diluted EPS is computed by dividing net income by the average number of common stock and common stock equivalents outstanding.

(Dollars and shares in thousands, except per share amounts)

| Periods ended September 30,     | Three Months |          | Nine Months<br>(As Restated) |           |
|---------------------------------|--------------|----------|------------------------------|-----------|
|                                 | 2007         | 2006     | 2007                         | 2006      |
| Net income                      | \$ 6,556     | \$ 6,578 | \$ 18,013                    | \$ 18,828 |
| Weighted average basic shares   | 13,323.6     | 13,436.6 | 13,358.1                     | 13,414.6  |
| Dilutive effect of:             |              |          |                              |           |
| Options                         | 190.2        | 242.1    | 211.1                        | 252.5     |
| Other                           | 50.3         | 47.6     | 43.5                         | 41.1      |
| Weighted average diluted shares | 13,564.1     | 13,726.3 | 13,612.7                     | 13,708.2  |
| Earnings per share:             |              |          |                              |           |
| Basic                           | \$ 0.49      | \$ 0.49  | \$ 1.35                      | \$ 1.40   |
| Diluted                         | \$ 0.48      | \$ 0.48  | \$ 1.32                      | \$ 1.37   |

**(15) Litigation**

The Corporation is involved in various claims and legal proceedings arising out of the ordinary course of business. Management is of the opinion, based on its review with counsel of the development of such matters to date, that the ultimate disposition of such matters will not materially affect the consolidated financial position or results of operations of the Corporation.

-23-

With respect to the unaudited consolidated financial statements of Washington Trust Bancorp, Inc. and Subsidiaries at September 30, 2007 and for the three and nine months ended September 30, 2007 and 2006, KPMG LLP has made a review (based on the standards of the Public Company Accounting Oversight Board (United States)) and not an audit, set forth in their separate report dated November 9, 2007 appearing below. That report does not express an opinion on the interim unaudited consolidated financial information. KPMG LLP has not carried out any significant or additional audit tests beyond those which would have been necessary if their report had not been included. Accordingly, such report is not a "report" or "part of the Registration Statement" within the meaning of Sections 7 and 11 of the Securities Act of 1933, as amended, and the liability provisions of Section 11 of the Securities Act do not apply.

### **Report of Independent Registered Public Accounting Firm**

The Board of Directors and Shareholders  
Washington Trust Bancorp, Inc.:

We have reviewed the accompanying consolidated balance sheet of Washington Trust Bancorp, Inc. and Subsidiaries (the "Corporation") as of September 30, 2007, the related consolidated statements of income for the three-and nine-month periods ended September 30, 2007 and 2006, and the related consolidated statements of cash flows for the nine-month periods ended September 30, 2007 and 2006. These consolidated financial statements are the responsibility of the Corporation's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the consolidated financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with standards established by the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Washington Trust Bancorp, Inc. and Subsidiaries as of December 31, 2006, and the related consolidated statements of income, changes in shareholders' equity and cash flows for the year then ended (not presented herein); and in our report dated March 12, 2007, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the consolidated balance sheet as of December 31, 2006, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

KPMGLLP

Providence, Rhode Island  
November 9, 2007



## **ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

### **Forward-Looking Statements**

This report contains certain statements that may be considered "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements, other than statements of historical facts, including statements regarding our strategy, effectiveness of investment programs, evaluations of future interest rate trends and liquidity, expectations as to growth in assets, deposits and results of operations, success of acquisitions, future operations, market position, financial position, and prospects, plans, goals and objectives of management are forward-looking statements. The actual results, performance or achievements of the Corporation could differ materially from those projected in the forward-looking statements as a result of, among other factors, changes in general national or regional economic conditions, changes in interest rates, reductions in the market value of wealth management assets under administration, reductions in loan demand, reductions in deposit levels necessitating increased borrowing to fund loans and investments, changes in loan default and charge-off rates, changes in the size and nature of the Corporation's competition, changes in legislation or regulation and accounting principles, policies and guidelines, unanticipated consequences of the restatement; the review and audit by our independent auditor of our 2007 financial statements; the consequences of the reclassification of the held-to-maturity securities portfolio to the available-for-sale category; the financial impact of the foregoing; and changes in the assumptions used in making such forward-looking statements. The Corporation assumes no obligation to update forward-looking statements or update the reasons actual results, performance or achievements could differ materially from those provided in the forward-looking statements, except as required by law.

### **Critical Accounting Policies**

Accounting policies involving significant judgments and assumptions by management that have, or could have, a material impact on the carrying value of certain assets and impact income are considered critical accounting policies. The Corporation's accounting and reporting policies comply with GAAP and conform to general practices within the banking industry. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. The financial position and results of operations can be affected by these estimates and assumptions, which are important in understanding the reported results. Management has discussed the development and the selection of critical accounting policies with the Audit Committee of our board of directors. As discussed in our 2006 Annual Report on Form 10-K, we have identified the allowance for loan losses, accounting for acquisitions and review of goodwill and intangible assets for impairment, other-than-temporary impairment of investment securities, defined benefit pension obligations, interest income recognition, and tax estimates as critical accounting policies. There have been no significant changes in the methods or assumptions used in the accounting policies that require material estimates and assumptions.

### **Recent Events**

In June 2007, Washington Trust opened its 17<sup>th</sup> branch located in Cranston, Rhode Island. This branch office is the second location in Cranston.

### **Results of Operations**

#### **Overview**

As discussed in Note 1 to the Consolidated Financial Statements, the Corporation has determined that its interim financial statements for the period ended June 30, 2007 should be restated and that the Corporation's financial statements for the quarter ended June 30, 2007 should no longer be relied upon. This restatement was solely related to accounting errors in connection with sales of certain held-to-maturity investment securities conducted in the second quarter of 2007.

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

The Corporation will file an amended Form 10-Q for the quarter ended June 30, 2007 reflecting the necessary adjustments with the SEC as soon as practicable. The Corporation will also file an amended Form 10-Q for the quarter ended March 31, 2007 with the SEC as soon as practicable to add a subsequent event footnote to disclose the second quarter 2007 transactions described above.

For the quarter ended June 30, 2007, the accounting corrections for these transactions, including recognition of the realized loss on the sales transactions and other related changes, result in an after-tax reduction in net income of \$828 thousand, or 6 cents per diluted share, from \$6.3 million, or 46 cents per diluted share, to \$5.5 million, or 40 cents per diluted share. For the six-month period ended June 30, 2007 the accounting corrections result in a reduction in net

-25-

---

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

income from \$12.3 million, or 90 cents per diluted share, to \$11.5 million, or 84 cents per diluted share. All applicable amounts related to this restatement have been reflected herein and in our Consolidated Financial Statements included in this Form 10-Q. See additional discussion regarding the restatement in Note 1 and Note 3 to the Consolidated Financial Statements.

Net income for the third quarter of 2007 was \$6.6 million, or 48 cents per diluted share, substantially the same as the amounts reported for the third quarter of 2006. The returns on average equity and average assets for the quarter ended September 30, 2007 were 14.99% and 1.10%, respectively, compared to 15.62% and 1.09%, respectively, for the same period in 2006.

Including the effect of the restatement, net income for the nine months ended September 30, 2007 amounted to \$18.0 million, down \$815 thousand, or 4.3%, from the same period in 2006. The Corporation earned \$1.32 per share on a diluted basis for the nine months ended September 30, 2007, compared to \$1.37 per diluted share for the same period a year ago. See Note 1 to the Consolidated Financial Statements for further information regarding the restatement.

For the nine months ended September 30, 2007, the returns on average equity and average assets were 13.74% and 1.01%, respectively, compared to 15.33% and 1.04%, respectively, for the comparable period in 2006.

Selected financial highlights are presented in the table below.

(Dollars in thousands, except per share amounts)

| Periods ended September 30,                     | Three Months |          | Nine Months<br>(As Restated) |           |
|---|--------------|----------|------------------------------|-----------|
|   | 2007         | 2006     | 2007                         | 2006      |
| <b>Earnings:</b>                                |              |          |                              |           |
| Net income                                      | \$ 6,556     | \$ 6,578 | \$ 18,013                    | \$ 18,828 |
| Diluted earnings per share                      | 0.48         | 0.48     | 1.32                         | 1.37      |
| Dividends declared per common share             | 0.20         | 0.19     | 0.60                         | 0.57      |
| <b>Select Ratios:</b>                           |              |          |                              |           |
| Return on average assets                        | 1.10%        | 1.09%    | 1.01%                        | 1.04%     |
| Return on average shareholders equity           | 14.99%       | 15.62%   | 13.74%                       | 15.33%    |
| Interest rate spread (taxable equivalent basis) | 2.42%        | 2.51%    | 2.42%                        | 2.49%     |
| Net interest margin (taxable equivalent basis)  | 2.81%        | 2.86%    | 2.79%                        | 2.82%     |

**Net Interest Income**

Net interest income is the difference between interest earned on loans and securities and interest paid on deposits and other borrowings, and continues to be the primary source of Washington Trust's operating income. Net interest income is affected by the level of interest rates, changes in interest rates and changes in the amount and composition of interest-earnings assets and interest-bearing liabilities. Included in interest income are loan prepayment fees and certain other fees, such as late charges.

Net interest income for the third quarter of 2007 amounted to \$15.3 million, down \$556 thousand, or 3.5%, from the same quarter a year ago. Net interest income for the three months ended September 30, 2006 included a catch-up for the delayed second quarter 2006 dividend on the Corporation's investment in Federal Home Loan Bank of Boston ("FHLBB") stock of approximately \$450 thousand. Excluding the impact of the additional FHLBB dividend, net interest income for the third quarter of 2007 was down 0.7% from the same quarter in 2006. For the nine months ended September 30, 2007, net interest income declined \$1.4 million, or 3.0%, from the same period in 2006. The

decline in net interest income was due to the fact that rates paid on deposits and borrowings have risen faster than earning asset yields and a higher rate of growth was experienced in higher cost deposit categories. In addition, the average balance of total interest-earnings assets have declined somewhat in 2007 compared to 2006.

The following discussion presents net interest income on a fully taxable equivalent (“FTE”) basis by adjusting income and yields on tax-exempt loans and securities to be comparable to taxable loans and securities. For more information see the section entitled “Average Balances / Net Interest Margin - Fully Taxable Equivalent (FTE) Basis” below.

-26-

---

FTE net interest income for the quarter ended September 30, 2007 decreased \$431 thousand, or 2.7%, from the third quarter of 2006, and for the nine months ended September 30, 2007, declined \$1.0 million, or 2.2%, from the same period a year earlier. The net interest margin (FTE net interest income as a percentage of average interest-earnings assets) for the three months ended September 30, 2007 was 2.81%, down 5 basis points from the same period a year earlier. Excluding the 8 basis point impact of the additional FHLBB dividend recorded in the third quarter of 2006, net interest margin for the third quarter of 2007 was 3 basis points higher than the same period a year earlier. Net interest margin for the nine months ended September 30, 2007 was 2.79%, down 3 basis points from 2.82% for the same period a year ago. Included in net interest income in 2007 was interest recovery of \$322 thousand received in the first quarter on a previously charged off loan. This interest recovery accounted for 3 basis points of the net interest margin for the nine months ended September 30, 2007.

Average interest-earning assets for the three and nine months ended September 30, 2007 decreased \$21.4 million and \$31.6 million, respectively, from the amounts reported for the same periods last year. This decrease was mainly due to reductions in the securities portfolio, offset in part by growth in the loan portfolio. Total average loans for the three and nine months ended September 30, 2007 increased \$70.0 million and \$58.0 million, respectively, from the comparable 2006 periods. The yield on total loans for the three and nine months ended September 30, 2007 increased 11 and 19 basis points, respectively, from the comparable 2006 periods. Loan prepayment and other fees included in interest income for the three and nine months ended September 30, 2007 were \$61 thousand and \$253 thousand, respectively, compared to \$119 thousand and \$579 thousand for the same periods in 2006, respectively. Total average securities for the three and nine months ended September 30, 2007 decreased \$91.3 million and \$89.6 million, respectively. The relatively flat yield curve made reinvestment of maturing balances unattractive relative to funding costs during these periods. The FTE rate of return on securities for the three and nine months ended September 30, 2007 increased 14 and 44 basis points from the comparable 2006 periods. The increase in the total yield on securities reflects a combination of higher yields on variable rate securities tied to short-term interest rates, sale or runoff of lower yielding securities and higher marginal rates on reinvestment of cash flows relative to the prior year. The Corporation continues to consider appropriate strategies to manage rising funding costs and more slowly increasing investment yields given the relatively flat yield curve.

For the three and nine months ended September 30, 2007, average interest-bearing liabilities declined \$31.0 million and \$35.0 million, respectively, from the amounts reported for the comparable periods last year. The Corporation experienced growth in money market and other borrowed funds, and declines in NOW accounts, time deposits and FHLB advances. The decline in time deposits resulted from decreases in average brokered certificates of deposit, which are utilized by the Corporation as part of its overall funding program along with FHLB advances and other sources. Average brokered certificates of deposit for the three and nine months ended September 30, 2007 decreased \$64.3 million and \$55.6 million, respectively. The average rate paid on brokered certificates of deposit for the three and nine months ended September 30, 2007 was relatively unchanged from the comparable periods in 2006. The average balance of FHLB advances for the three and nine months ended September 30, 2007 decreased \$11.6 million and \$58.2 million, respectively, while the average rate paid on FHLB advances increased 30 and 28 basis points, respectively, from the same periods a year ago.

-27-

---

**Average Balances / Net Interest Margin - Fully Taxable Equivalent (FTE) Basis**

The following tables present average balance and interest rate information. Tax-exempt income is converted to a fully taxable equivalent ("FTE") basis using the statutory federal income tax rate. For dividends on corporate stocks, the 70% federal dividends received deduction is also used in the calculation of tax equivalency. Unrealized gains (losses) on available for sale securities are excluded from the average balance and yield calculations. Nonaccrual and renegotiated loans, as well as interest earned on these loans (to the extent recognized in the Consolidated Statements of Income) are included in amounts presented for loans.

Three months ended  
September 30,

| (Dollars in thousands)                                 | 2007               |           |                | 2006               |           |                |
|--|--------------------|-----------|----------------|--------------------|-----------|----------------|
|  | Average<br>Balance | Interest  | Yield/<br>Rate | Average<br>Balance | Interest  | Yield/<br>Rate |
| <b>Assets:</b>   |                    |           |                |                    |           |                |
| Residential real estate loans                          | \$ 584,223         | \$ 7,886  | 5.35%          | \$ 588,488         | \$ 7,596  | 5.12%          |
| Commercial and other loans                             | 635,435            | 12,203    | 7.62%          | 564,804            | 10,990    | 7.72%          |
| Consumer loans   | 282,472            | 4,988     | 7.01%          | 278,864            | 4,898     | 6.97%          |
| Total loans  | 1,502,130          | 25,077    | 6.62%          | 1,432,156          | 23,484    | 6.51%          |
| Federal funds sold and<br>other short-term investments | 21,375             | 275       | 5.10%          | 20,132             | 252       | 4.96%          |
| Taxable debt securities                                | 582,152            | 7,565     | 5.16%          | 706,319            | 8,493     | 4.77%          |
| Nontaxable debt securities                             | 80,998             | 1,145     | 5.61%          | 42,842             | 622       | 5.76%          |
| Corporate stocks and FHLB<br>stock                     | 42,129             | 748       | 7.03%          | 48,704             | 1,289     | 10.50%         |
| Total securities                                       | 726,654            | 9,733     | 5.31%          | 817,997            | 10,656    | 5.17%          |
| Total interest-earning assets                          | 2,228,784          | 34,810    | 6.20%          | 2,250,153          | 34,140    | 6.02%          |
| Non interest-earning assets                            | 161,578            |           |                | 160,883            |           |                |
| Total assets   | \$ 2,390,362       |           |                | \$ 2,411,036       |           |                |
| <b>Liabilities and Shareholders' Equity:</b>           |                    |           |                |                    |           |                |
| NOW accounts   | \$ 166,271         | \$ 70     | 0.17%          | \$ 174,740         | \$ 78     | 0.18%          |
| Money market accounts                                  | 300,329            | 2,950     | 3.90%          | 281,559            | 2,584     | 3.64%          |
| Savings deposits                                       | 194,439            | 646       | 1.32%          | 191,232            | 327       | 0.68%          |
| Time deposits  | 817,379            | 9,474     | 4.60%          | 868,487            | 9,484     | 4.33%          |
| FHLB advances  | 468,384            | 5,243     | 4.44%          | 480,033            | 5,011     | 4.14%          |
| Junior subordinated debentures                         | 22,681             | 338       | 5.91%          | 22,681             | 338       | 5.91%          |
| Other borrowed funds                                   | 25,857             | 291       | 4.47%          | 7,624              | 89        | 4.66%          |
| Total interest-bearing liabilities                     | 1,995,340          | 19,012    | 3.78%          | 2,026,356          | 17,911    | 3.51%          |
| Demand deposits  | 188,495            |           |                | 192,626            |           |                |
| Other liabilities                                      | 31,640             |           |                | 23,589             |           |                |
| Shareholders' equity                                   | 174,887            |           |                | 168,465            |           |                |
| Total liabilities and<br>shareholders' equity          | \$ 2,390,362       |           |                | \$ 2,411,036       |           |                |
| Net interest income (FTE)                              |                    | \$ 15,798 |                |                    | \$ 16,229 |                |
| Interest rate spread                                   |                    |           | 2.42%          |                    |           | 2.51%          |
| Net interest margin                                    |                    |           | 2.81%          |                    |           | 2.86%          |

Interest income amounts presented in the preceding table include the following adjustments for taxable equivalency:

(Dollars in thousands)

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

| Three months ended September 30, | 2007  | 2006  |
|----------------------------------|-------|-------|
| Commercial and other loans       | \$ 45 | \$ 54 |
| Nontaxable debt securities       | 364   | 217   |
| Corporate stocks                 | 79    | 92    |

-28-

---

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

Nine months ended  
September 30,

|   | 2007<br>(As Restated) |           |                | 2006               |           |                |
|---|-----------------------|-----------|----------------|--------------------|-----------|----------------|
| (Dollars in thousands)                                    | Average<br>Balance    | Interest  | Yield/<br>Rate | Average<br>Balance | Interest  | Yield/<br>Rate |
| <b>Assets:</b>  |                       |           |                |                    |           |                |
| Residential real estate<br>loans                          | \$ 588,808            | \$ 23,471 | 5.33%          | \$ 589,635         | \$ 22,505 | 5.10%          |
| Commercial and other<br>loans                             | 612,886               | 35,306    | 7.70%          | 563,284            | 32,294    | 7.67%          |
| Consumer loans  | 282,154               | 14,724    | 6.98%          | 272,960            | 13,819    | 6.77%          |
| Total loans   | 1,483,848             | 73,501    | 6.62%          | 1,425,879          | 68,618    | 6.43%          |
| Federal funds sold and<br>other short-term<br>investments | 17,302                | 650       | 5.03%          | 14,416             | 517       | 4.79%          |
| Taxable debt securities                                   | 604,303               | 23,196    | 5.13%          | 727,175            | 25,553    | 4.70%          |
| Nontaxable debt<br>securities                             | 76,578                | 3,238     | 5.65%          | 39,254             | 1,697     | 5.78%          |
| Corporate stocks and<br>FHLB stock                        | 42,796                | 2,310     | 7.21%          | 49,723             | 2,393     | 6.44%          |
| Total securities  | 740,979               | 29,394    | 5.30%          | 830,568            | 30,160    | 4.86%          |
| Total interest-earning<br>assets                          | 2,224,827             | 102,895   | 6.18%          | 2,256,447          | 98,778    | 5.85%          |
| Non interest-earning<br>assets                            | 163,803               |           |                | 155,006            |           |                |
| Total assets  | \$ 2,388,630          |           |                | \$ 2,411,453       |           |                |
| <b>Liabilities and<br/>Shareholders' Equity:</b>          |                       |           |                |                    |           |                |
| NOW accounts  | \$ 168,217            | \$ 202    | 0.16%          | \$ 174,156         | \$ 225    | 0.17%          |
| Money market accounts                                     | 295,876               | 8,630     | 3.90%          | 247,979            | 6,026     | 3.25%          |
| Savings deposits  | 198,845               | 2,017     | 1.36%          | 197,035            | 888       | 0.60%          |
| Time deposits   | 828,976               | 28,483    | 4.59%          | 863,831            | 26,733    | 4.14%          |
| FHLB advances   | 468,956               | 15,323    | 4.37%          | 527,108            | 16,115    | 4.09%          |
| Junior subordinated<br>debentures                         | 22,681                | 1,014     | 5.98%          | 22,681             | 1,014     | 5.98%          |
| Other borrowed funds                                      | 21,521                | 730       | 4.53%          | 7,331              | 256       | 4.67%          |
| Total interest-bearing<br>liabilities                     | 2,005,072             | 56,399    | 3.76%          | 2,040,121          | 51,257    | 3.36%          |
| Demand deposits   | 177,713               |           |                | 185,088            |           |                |
| Other liabilities   | 31,072                |           |                | 22,517             |           |                |
| Shareholders' equity                                      | 174,773               |           |                | 163,727            |           |                |
| Total liabilities and<br>shareholders' equity             | \$ 2,388,630          |           |                | \$ 2,411,453       |           |                |
| Net interest income<br>(FTE)                              |                       | \$ 46,496 |                |                    | \$ 47,521 |                |
| Interest rate spread                                      |                       |           | 2.42%          |                    |           | 2.49%          |
| Net interest margin                                       |                       |           | 2.79%          |                    |           | 2.82%          |

Interest income amounts presented in the preceding table include the following adjustments for taxable equivalency:

(Dollars in thousands)



Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

| Nine months ended September 30, | 2007   | 2006   |
|---------------------------------|--------|--------|
| Commercial and other loans      | \$ 121 | \$ 161 |
| Nontaxable debt securities      | 1,030  | 593    |
| Corporate stocks                | 238    | 269    |

---

-29-

The following table presents certain information on a FTE basis regarding changes in our interest income and interest expense for the periods indicated. The net change attributable to both volume and rate has been allocated proportionately.

| (Dollars in thousands)                              | Three months ended          |          |          | (As Restated)               |            |            |
|---|-----------------------------|----------|----------|-----------------------------|------------|------------|
|   | September 30, 2007 vs. 2006 |          |          | September 30, 2007 vs. 2006 |            |            |
|   | Increase (decrease) due to  |          |          | Increase (decrease) due to  |            |            |
|   | Volume                      | Rate     | Net Chg  | Volume                      | Rate       | Net Chg    |
| <b>Interest on interest-earning assets:</b>         |                             |          |          |                             |            |            |
| Residential real estate loans                       | \$ (55)                     | \$ 345   | \$ 290   | \$ (32)                     | \$ 998     | \$ 966     |
| Commercial and other loans                          | 1,358                       | (145)    | 1,213    | 2,884                       | 128        | 3,012      |
| Consumer loans                                      | 62                          | 28       | 90       | 471                         | 434        | 905        |
| Federal funds sold and other short-term investments | 16                          | 7        | 23       | 107                         | 26         | 133        |
| Taxable debt securities                             | (1,581)                     | 653      | (928)    | (4,563)                     | 2,206      | (2,357)    |
| Nontaxable debt securities                          | 539                         | (16)     | 523      | 1,580                       | (39)       | 1,541      |
| Corporate stocks and FHLB stock                     | (157)                       | (384)    | (541)    | (354)                       | 271        | (83)       |
| Total interest income                               | 182                         | 488      | 670      | 93                          | 4,024      | 4,117      |
| <b>Interest on interest-bearing liabilities:</b>    |                             |          |          |                             |            |            |
| NOW accounts  | (4)                         | (4)      | (8)      | (9)                         | (14)       | (23)       |
| Money market accounts                               | 177                         | 189      | 366      | 1,279                       | 1,325      | 2,604      |
| Savings deposits                                    | 5                           | 314      | 319      | 9                           | 1,120      | 1,129      |
| Time deposits                                       | (579)                       | 569      | (10)     | (1,101)                     | 2,851      | 1,750      |
| FHLB advances                                       | (124)                       | 356      | 232      | (1,851)                     | 1,059      | (792)      |
| Junior subordinated debentures                      | -                           | -        | -        | -                           | -          | -          |
| Other borrowed funds                                | 206                         | (4)      | 202      | 482                         | (8)        | 474        |
| Total interest expense                              | (319)                       | 1,420    | 1,101    | (1,191)                     | 6,333      | 5,142      |
| Net interest income                                 | \$ 501                      | \$ (932) | \$ (431) | \$ 1,284                    | \$ (2,309) | \$ (1,025) |

### Provision and Allowance for Loan Losses

The Corporation's loan loss provision charged to earnings amounted to \$300 thousand and \$900 thousand for the three and nine months ended September 30, 2007, respectively, consistent with the amounts recorded in 2006. The allowance for loan losses was \$19.5 million, or 1.29% of total loans, at September 30, 2007, compared to \$18.6 million, or 1.31%, at September 30, 2006. See additional discussion under the caption "Asset Quality" for further information on the Allowance for Loan Losses.

### Noninterest Income

Noninterest income is an important source of revenue for Washington Trust. Noninterest income as a percent of total revenues (net interest income plus noninterest income) increased from 40.5% in the third quarter of 2006 to 43.6% in the third quarter of 2007. Total noninterest income for the third quarter of 2007 increased \$1.1 million, or 9.9%, from the same quarter a year ago. For the nine months ended September 30, 2007, total noninterest income increased \$2.5 million, or 7.8%, from the comparable 2006 period.

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

The following table presents a noninterest income comparison for the three and nine months ended September 30, 2007 and 2006:

| (Dollars in thousands)   | Three Months |           |          |        | Nine Months |           |          |       |
|--|--------------|-----------|----------|--------|-------------|-----------|----------|-------|
|  |              |           | \$       | %      |             |           | \$       | %     |
| Periods ended  | 2007         | 2006      | Chg      | Chg    | 2007        | 2006      | Chg      | Chg   |
| <b>Noninterest income:</b>   |              |           |          |        |             |           |          |       |
| Wealth management services:  |              |           |          |        |             |           |          |       |
| Trust and investment advisory fees                                     | \$ 5,336     | \$ 4,727  | \$ 609   | 13%    | \$ 15,626   | \$ 14,036 | \$ 1,590 | 11%   |
| Mutual fund fees   | 1,386        | 1,229     | 157      | 13%    | 4,000       | 3,573     | 427      | 12%   |
| Financial planning, commissions and other service fees                 | 456          | 509       | (53)     | (10%)  | 1,915       | 2,033     | (118)    | (6%)  |
| Wealth management services   | 7,178        | 6,465     | 713      | 11%    | 21,541      | 19,642    | 1,899    | 10%   |
| Service charges on deposit accounts                                    | 1,214        | 1,312     | (98)     | (8%)   | 3,559       | 3,667     | (108)    | (3%)  |
| Merchant processing fees   | 2,252        | 2,125     | 127      | 6%     | 5,285       | 4,828     | 457      | 10%   |
| Income from BOLI   | 376          | 389       | (13)     | (3%)   | 1,166       | 1,014     | 152      | 15%   |
| Net gains on loan sales and commissions on loans originated for others | 431          | 417       | 14       | 3%     | 1,205       | 1,029     | 176      | 17%   |
| Other income   | 399          | 440       | (41)     | (9%)   | 1,129       | 1,111     | 18       | 2%    |
| Subtotal   | 11,850       | 11,148    | 702      | 6%     | 33,885      | 31,291    | 2,594    | 8%    |
| Net realized (losses) gains on securities (1)                          | –            | (365)     | 365      | (100%) | 336         | 459       | (123)    | (27%) |
| Total noninterest income (1)   | \$ 11,850    | \$ 10,783 | \$ 1,067 | 10%    | \$ 34,221   | \$ 31,750 | \$ 2,471 | 8%    |

(1) Net realized (losses) gains on sales of securities and total noninterest income for the nine months ended September 30, 2007 reflects the restatement of second quarter 2007 results. Reference is made to Note 1 and Note 3 of the Consolidated Financial Statements.

Wealth management revenues for the three and nine months ended September 30, 2007 increased by 11.0% and 9.7%, respectively, over the same periods in 2006. Revenue from wealth management services is largely dependent on the value of assets under administration and is closely tied to the performance of the financial markets. Assets under administration totaled \$4.113 billion at September 30, 2007, up \$418.1 million, or 11.3%, during the nine months ended September 30, 2007 and up \$562.0 million, or 15.8%, from September 30, 2006. Financial market appreciation

as well as successful business development efforts and customer cash flows contributed to the growth. The following table presents the changes in wealth management assets under administration for the three and nine month periods ended September 30, 2007:

| (Dollars in thousands)             | Three<br>Months | Nine<br>Months |
|------------------------------------|-----------------|----------------|
| Periods ended September 30,        | 2007            | 2007           |
| Balance at the beginning of period | \$ 3,948,390    | \$ 3,694,813   |
| Net market appreciation and income | 122,424         | 284,149        |
| Net customer cash flows            | 42,104          | 133,956        |
| Balance at the end of period       | \$ 4,112,918    | \$ 4,112,918   |

Merchant processing fees for the three and nine months ended September 30, 2007 increased 6.0% and 9.5%, respectively, from the corresponding periods a year ago due to increases in the volume of transactions processed for existing and new customers. Merchant processing fees represent charges to merchants for credit card transactions processed.

Included in noninterest income were net realized gains on sales of securities of \$336 thousand and \$459 thousand, respectively, for the nine month periods ended September 30, 2007 and 2006. These amounts included \$397 thousand and \$381 thousand of gains recognized in the second quarter of 2007 and 2006, respectively, resulting from the Corporation's annual contribution of appreciated equity securities to the Corporation's charitable foundation in 2007 and 2006, respectively. The cost of the annual contributions, which was included in noninterest expenses, amounted to \$520 thousand and \$513 thousand for the second quarter of 2007 and 2006, respectively. Net realized securities gains of \$195 thousand were recognized in the second quarter of 2007 from certain debt and equity securities that were called prior to maturity by the issuers. In addition, sales of debt and equity securities in the second quarter of 2007 resulted in net

-31-

---

realized losses of \$256 thousand. See Note 1 and Note 3 to the Consolidated Financial Statements for additional discussion on sales of securities and the restatement.

### Noninterest Expense

Noninterest expenses amounted to \$17.3 million for the third quarter of 2007, up \$701 thousand, or 4.2%, from the same quarter a year ago. For the nine months ended September 30, 2007, noninterest expense totaled \$52.2 million, up \$2.6 million, or 5.2%. During the first quarter of 2007, the Corporation prepaid \$26.5 million in higher cost advances from FHLBB, resulting in a debt prepayment penalty charge, recorded in noninterest expense, of \$1.1 million. The source of funds for the paydowns was maturities of investments as well as other borrowings. Excluding debt prepayment penalty expense, noninterest expenses increased \$1.5 million, or 3.1%, over the same nine-month period last year.

The following table presents a noninterest expense comparison for the three and nine months ended September 30, 2007 and 2006:

| (Dollars in thousands)             | Three Months |           |        |       | Nine Months |           |          |       |
|------------------------------------|--------------|-----------|--------|-------|-------------|-----------|----------|-------|
|                                    |              |           | \$     | %     |             |           | \$       | %     |
| Periods ended                      |              |           |        |       |             |           |          |       |
| September 30,                      | 2007         | 2006      | Chg    | Chg   | 2007        | 2006      | Chg      | Chg   |
| <b>Noninterest expense:</b>        |              |           |        |       |             |           |          |       |
| Salaries and employee benefits     | \$ 10,098    | \$ 9,651  | \$ 447 | 5%    | \$ 30,195   | \$ 29,100 | \$ 1,095 | 4%    |
| Net occupancy                      | 1,021        | 934       | 87     | 9%    | 3,076       | 2,906     | 170      | 6%    |
| Equipment                          | 871          | 872       | (1)    | —     | 2,564       | 2,552     | 12       | 1%    |
| Merchant processing costs          | 1,916        | 1,796     | 120    | 7%    | 4,493       | 4,090     | 403      | 10%   |
| Outsourced services                | 556          | 490       | 66     | 14%   | 1,610       | 1,504     | 106      | 7%    |
| Advertising and promotion          | 466          | 371       | 95     | 26%   | 1,467       | 1,489     | (22)     | (2%)  |
| Legal, audit and professional fees | 444          | 563       | (119)  | (21%) | 1,298       | 1,342     | (44)     | (3%)  |
| Amortization of intangibles        | 341          | 398       | (57)   | (14%) | 1,057       | 1,209     | (152)    | (13%) |
| Debt prepayment penalties          | —            | —         | —      | —     | 1,067       | —         | 1,067    | 100%  |
| Other (1)                          | 1,599        | 1,536     | 63     | 4%    | 5,354       | 5,403     | (49)     | (1%)  |
| Total noninterest expense (1)      | \$ 17,312    | \$ 16,611 | \$ 701 | 4%    | \$ 52,181   | \$ 49,595 | \$ 2,586 | 5%    |

(1) Other and total noninterest expense for the nine months ended September 30, 2007 reflects the restatement of second quarter 2007 results. Reference is made to Note 1 and Note 3 of the Consolidated Financial Statements.

Salaries and employee benefit expense, the largest component of noninterest expense, totaled \$10.1 million and \$30.2 million, respectively, for the three and nine months ended September 30, 2007, up \$447 thousand and \$1.1 million, respectively, from the same periods in 2006. The increase was primarily attributable to increases in salaries and wages and performance-based compensation plans.

Merchant processing costs for the three and nine months ended September 30, 2007 increased \$120 thousand and \$403 thousand from the comparable periods in 2006 due to increases in the volume of transactions processed for existing and new customers. Merchant processing costs represent third-party costs incurred that are directly attributable to handling merchant credit card transactions.

Legal, audit and professional fees for the three months ended September 30, 2007 decreased \$119 thousand, or 21.1%, from the same period last year primarily due to decreased consulting expenses.

Debt prepayment penalty expense, resulting from the first quarter 2007 prepayment of \$26.5 million in higher cost advances from the FHLBB, amounted to \$1.1 million for the nine months ended September 30, 2007.

**Income Taxes**

Income tax expense amounted to \$3.0 million and \$8.2 million, respectively, for the three and nine months ended September 30, 2007 as compared to \$3.2 million and \$8.9 million, respectively for the same periods in 2006. The Corporation's effective tax rate for the three and nine months ended September 30, 2007 was 31.3% and 31.4%, respectively, down slightly from 32.5% and 32.2%, respectively, for the same periods in 2006, primarily due to higher average balances in nontaxable state and municipal debt obligations. These rates differed from the federal rate of 35% due to the benefits of tax-exempt income, the dividends received deduction and income from BOLI.

-32-

---

## **Financial Condition**

### **Summary**

Total assets amounted to \$2.432 billion at September 30, 2007, up \$32.6 million from December 31, 2006, with total loans increasing by \$54.5 million and the investment securities portfolio decreasing by \$15.1 million. Total liabilities were up \$27.8 million during the nine months ended September 30, 2007, with other borrowings increasing by \$21.7 million, FHLB advances increasing by \$27.7 million and total deposits decreasing by \$22.1 million. Shareholders' equity totaled \$177.9 million at September 30, 2007, compared to \$173.1 million at December 31, 2006.

### **Securities**

Washington Trust's securities portfolio is managed to generate interest income, to implement interest rate risk management strategies, and to provide a readily available source of liquidity for balance sheet management. At September 30, 2007 the securities portfolio totaled \$688.7 million, down \$15.1 million from December 31, 2006 due to sales and maturities. Included in the investment securities portfolio at September 30, 2007 were mortgage-backed securities with a fair value of \$366.0 million. All of the Corporation's mortgage-backed securities are issued by U.S. Government sponsored agencies. See Note 1 and Note 3 to the Consolidated Financial Statements for additional discussion on sales of securities and the restatement.

The net unrealized losses on securities available for sale amounted to \$3.1 million at September 30, 2007. At December 31, 2006 net unrealized losses on securities available for sale and held to maturity amounted to \$1.7 million. The increase in unrealized losses for the nine months ended September 30, 2007 was primarily attributable to the effect an increase in the intermediate to long term rates had on the Corporation's securities portfolio. See Note 3 to the Consolidated Financial Statements for detail of unrealized gains and losses on securities.

### **Federal Home Loan Bank Stock**

The Corporation is required to maintain a level of investment in FHLB stock that currently is based on the level of its FHLB advances. As of September 30, 2007 and 2006, the Corporation's investment in FHLB stock totaled \$28.7 million.

### **Loans**

Total loans grew by \$54.5 million, or 3.7%, in the nine months ended September 30, 2007 and amounted to \$1.5 billion. Commercial loans increased \$62.6 million, or 10.7%, during the first nine months of 2007. Consumer loan demand continued to be very modest increasing by \$1.7 million, or 0.6%, from the balance at December 31, 2006. Residential loans have declined by \$9.9 million, or 1.7%, during the nine months ended September 30, 2007.

### **Asset Quality**

#### **Allowance for Loan Losses**

Establishing an appropriate level of allowance for loan losses necessarily involves a high degree of judgment. The Corporation uses a methodology to systematically measure the amount of estimated loan loss exposure inherent in the loan portfolio for purposes of establishing a sufficient allowance for loan losses. For a more detailed discussion on the allowance for loan losses, see additional information in Item 7 under the caption "Application of Critical Accounting Policies and Estimates" of Washington Trust's Annual Report on Form 10-K for the fiscal year ended December 31, 2006.

The allowance for loan losses is management's best estimate of the probable loan losses incurred as of the balance sheet date. The allowance is increased by provisions charged to earnings and by recoveries of amounts previously charged off, and is reduced by charge-offs on loans.

At September 30, 2007, the allowance for loan losses was \$19.5 million, or 1.29% of total loans, and 728% of total nonaccrual loans. This compares with an allowance of \$18.9 million, or 1.29% of total loans, and 694% of nonaccrual

loans at December 31, 2006. Loan charge-offs, net of recoveries, amounted to \$322 thousand and \$173 thousand, respectively, for the nine months ended September 30, 2007 and 2006.

-33-

---



**Nonperforming Assets**

Nonperforming assets are summarized in the following table:

| (Dollars in thousands)                               | September 30,<br>2007 | December<br>31,<br>2006 |
|--|-----------------------|-------------------------|
| Nonaccrual loans 90 days or more past due            | \$ 1,725              | \$ 1,470                |
| Nonaccrual loans less than 90 days past due          | 948                   | 1,253                   |
| Total nonaccrual loans                               | 2,673                 | 2,723                   |
| Other real estate owned, net                         | -                     | -                       |
| Total nonperforming assets                           | \$ 2,673              | \$ 2,723                |
| Nonaccrual loans as a percentage of total loans      | 0.18%                 | 0.19%                   |
| Nonperforming assets as a percentage of total assets | 0.11%                 | 0.11%                   |
| Allowance for loan losses to nonaccrual loans        | 728.47%               | 693.87%                 |
| Allowance for loan losses to total loans             | 1.29%                 | 1.29%                   |

There were no accruing loans 90 days or more past due at September 30, 2007 or December 31, 2006.

Impaired loans consist of all nonaccrual commercial loans. At September 30, 2007, the recorded investment in impaired loans was \$1.7 million, which had a related allowance of \$9 thousand. Also during the nine months ended September 30, 2007, interest income recognized on impaired loans amounted to approximately \$374 thousand. Interest income on impaired loans is recognized on a cash basis only.

The following is an analysis of nonaccrual loans by loan category:

| (Dollars in thousands)       | September 30,<br>2007 | December 31,<br>2006 |
|------------------------------|-----------------------|----------------------|
| Residential real estate      | \$ 731                | \$ 721               |
| Commercial:                  |                       |                      |
| Mortgages                    | 1,099                 | 981                  |
| Construction and development | -                     | -                    |
| Other                        | 581                   | 831                  |
| Consumer                     | 262                   | 190                  |
| Total nonaccrual loans       | \$ 2,673              | \$ 2,723             |

Total 30 day+ delinquencies amounted to \$5.9 million, or 0.39% of total loans, at September 30, 2007, compared to \$7.2 million, or 0.49% of total loans, at December 31, 2006, and \$4.0 million, or 0.28% of total loans, at September 30, 2006. The Corporation has never offered a sub-prime or Alt-A residential mortgage loan program. Total residential mortgage and consumer loan 30 day+ delinquencies amounted to \$3.6 million, or 0.42% of these loans, at September 30, 2007, compared to \$1.4 million, or 0.16% of these loans, at December 31, 2006. Total 90 day+ delinquencies in the residential mortgage and consumer loans portfolios amounted to \$302 thousand (one loan) and \$76 thousand (two loans), respectively, as of September 30, 2007.

**Deposits**

Deposits totaled \$1.656 billion at September 30, 2007, down \$22.1 million, or 1.3%, from December 31, 2006. Excluding brokered certificates of deposit, in-market deposits were up \$23.5 million, or 1.6%, during the nine months ended September 30, 2007.

In the first nine months of 2007, demand deposits decreased \$3.7 million, or 2.0%, NOW account balances were down \$3.1 million, or 1.8%, savings deposits declined \$16.8 million, or 8.2%, and money market account balances

increased \$25.3 million, or 8.8%. Time deposits (including brokered certificates of deposit) were down \$23.7 million, or 2.9%, from the balance at December 31, 2006. The Corporation utilizes brokered time deposits as part of its overall funding program along with other sources. Brokered time deposits amounted to \$130.0 million at September 30, 2007, down \$45.6 million, or 26.0%, from December 31, 2006. Excluding the brokered time deposits, time deposits rose \$21.9 million, or 3.4%, in the first nine months of 2007 due mainly to growth in consumer and commercial certificates of deposit.

-34-

---

## Borrowings

The Corporation utilizes advances from the FHLB as well as other borrowings as part of its overall funding strategy. FHLB advances are used to meet short-term liquidity needs, to purchase securities and to purchase loans from other institutions. FHLB advances increased \$27.7 million during the nine months ended September 30, 2007. See Note 8 to the Consolidated Financial Statements for additional information on borrowings.

## Liquidity and Capital Resources

Liquidity is the ability of a financial institution to meet maturing liability obligations and customer loan demand. Washington Trust's primary source of liquidity is deposits. Deposits (demand, NOW, money market, savings and time deposits) funded approximately 70% of total average assets in the first nine months of 2007. Other sources of funding include discretionary use of purchased liabilities (e.g., FHLB term advances and other borrowings), cash flows from the Corporation's securities portfolios and loan repayments. In addition, securities designated as available for sale may be sold in response to short-term or long-term liquidity needs.

The Corporation's Asset/Liability Committee ("ALCO") establishes and monitors internal liquidity measures to manage liquidity exposure. Liquidity remained well within target ranges established by the ALCO during the first nine months of 2007.

For the nine months ended September 30, 2007, net cash provided by financing activities amounted to \$16.7 million. In the first quarter of 2007, \$19.5 million in securities sold under repurchase agreements were executed and \$26.5 million in FHLB advances were prepaid. See additional discussion on borrowings in the Condensed Notes to Consolidated Financial Statements. Net cash used in investing activities totaled \$53.9 million for the nine months ended September 30, 2007 and was used primarily to fund loan growth. Net cash provided by operating activities amounted to \$20.3 million for the nine months ended September 30, 2007, and was generated primarily by net income. See the Corporation's Consolidated Statements of Cash Flows for further information about sources and uses of cash.

Total shareholders' equity amounted to \$177.9 million at September 30, 2007, up \$4.8 million since December 31, 2006. The increase in retained earnings reflects the Corporation's net income of \$18.0 million offset in part by dividends declared of \$8.0 million. The dividend represented a \$0.20 per share dividend, an increase from the \$0.19 per share rate paid throughout 2006, making 2007 the fifteenth consecutive year with a dividend increase. Under the Corporation's 2006 Stock Repurchase Plan, 185,400 shares were repurchased at a total cost of \$4.8 million during the nine months ended September 30, 2007.

The ratio of total equity to total assets amounted to 7.3% at September 30, 2007, up from 7.2% at December 31, 2006. Book value per share as of September 30, 2007 and December 31, 2006 amounted to \$13.33 and \$12.89, respectively. The tangible book value per share was \$8.66 at September 30, 2007, compared to \$8.61 at the end of 2006.

## Contractual Obligations and Commitments

The Corporation has entered into numerous contractual obligations and commitments. The following table summarizes our contractual cash obligation and other commitments at September 30, 2007.

(Dollars in thousands)

|                                 | Total      | Payments Due by Period |            |            | After<br>5 Years |
|---------------------------------|------------|------------------------|------------|------------|------------------|
|                                 |            | Less Than<br>1 Year    | 1-3 Years  | 4-5 Years  |                  |
| <b>Contractual Obligations:</b> |            |                        |            |            |                  |
| FHLB advances (1)               | \$ 502,265 | \$ 147,282             | \$ 175,822 | \$ 116,699 | \$ 62,462        |
| Junior subordinated debentures  | 22,681     | –                      | –          | –          | 22,681           |
| Operating lease obligations     | 5,231      | 1,068                  | 1,817      | 1,001      | 1,345            |

Edgar Filing: WASHINGTON TRUST BANCORP INC - Form 10-Q

|                                    |            |            |            |            |           |
|------------------------------------|------------|------------|------------|------------|-----------|
| Software licensing arrangements    | 1,405      | 947        | 362        | 96         | –         |
| Treasury, tax and loan demand note | 6,742      | 6,742      | –          | –          | –         |
| Deferred acquisition obligations   | 9,772      | 7,887      | 1,885      | –          | –         |
| Other borrowed funds               | 19,889     | 27         | 61         | 19,572     | 229       |
| Total contractual obligations      | \$ 567,985 | \$ 163,953 | \$ 179,947 | \$ 137,368 | \$ 86,717 |

(1) All FHLB advances are shown in the period corresponding to their scheduled maturity.

-35-

---

| (Dollars in thousands)       | Amount of Commitment Expiration – Per Period |                     |                  |                  |                   |
|------------------------------|--|---------------------|------------------|------------------|-------------------|
|                              | Total  | Less Than<br>1 Year | 1-3 Years        | 4-5 Years        | After<br>5 Years  |
| <b>Other Commitments:</b>    |  |                     |                  |                  |                   |
| Commercial loans             | \$ 151,229                                   | \$ 82,182           | \$ 31,831        | \$ 8,087         | \$ 29,129         |
| Home equity lines            | 179,300                                      | 425                 | 4,394            | 6,769            | 167,712           |
| Other loans                  | 26,814                                       | 24,338              | 1,784            | 692              | –                 |
| Standby letters of credit    | 8,941  | 8,841               | 100              | –                | –                 |
| Forward loan commitments to: |  |                     |                  |                  |                   |
| Originate loans              | 2,870  | 2,870               | –                | –                | –                 |
| Sell loans                   | 4,966  | 4,966               | –                | –                | –                 |
| <b>Total commitments</b>     | <b>\$ 374,120</b>                            | <b>\$ 123,622</b>   | <b>\$ 38,109</b> | <b>\$ 15,548</b> | <b>\$ 196,841</b> |

See additional discussion in Note 10 to the Consolidated Financial Statements for more information regarding the nature and business purpose of financial instruments with off-balance sheet risk and derivative financial instruments.

### Off-Balance Sheet Arrangements

For the nine months ended September 30, 2007, Washington Trust engaged in no off-balance sheet transactions reasonably likely to have a material effect on the consolidated financial condition.

### Asset/Liability Management and Interest Rate Risk

The ALCO is responsible for establishing policy guidelines on liquidity and acceptable exposure to interest rate risk. Interest rate risk is the risk of loss to future earnings due to changes in interest rates. The objective of the ALCO is to manage assets and funding sources to produce results that are consistent with Washington Trust's liquidity, capital adequacy, growth, risk and profitability goals.

The ALCO manages the Corporation's interest rate risk using income simulation to measure interest rate risk inherent in the Corporation's on-balance sheet and off-balance sheet financial instruments at a given point in time by showing the effect of interest rate shifts on net interest income over a 12-month horizon, the month 13 to month 24 horizon and a 60-month horizon. The simulations assume that the size and general composition of the Corporation's balance sheet remain static over the simulation horizons, with the exception of certain deposit mix shifts from low-cost core savings to higher-cost time deposits in selected interest rate scenarios. Additionally, the simulations take into account the specific repricing, maturity, call options, and prepayment characteristics of differing financial instruments that may vary under different interest rate scenarios. The characteristics of financial instrument classes are reviewed periodically by the ALCO to ensure their accuracy and consistency.

The ALCO reviews simulation results to determine whether the Corporation's exposure to a decline in net interest income remains within established tolerance levels over the simulation horizons and to develop appropriate strategies to manage this exposure. As of September 30, 2007 and December 31, 2006, net interest income simulations indicated that exposure to changing interest rates over the simulation horizons remained within tolerance levels established by the Corporation. The Corporation defines maximum unfavorable net interest income exposure to be a change of no more than 5% in net interest income over the first 12 months, no more than 10% over the second 12 months, and no more than 10% over the full 60-month simulation horizon. All changes are measured in comparison to the projected net interest income that would result from an "unchanged" rate scenario where both interest rates and the composition of the Corporation's balance sheet remain stable for a 60-month period. In addition to measuring the change in net interest income as compared to an unchanged interest rate scenario, the ALCO also measures the trend of both net interest income and net interest margin over a 60-month horizon to ensure the stability and adequacy of this source of earnings in different interest rate scenarios.

The ALCO reviews a variety of interest rate shift scenario results to evaluate interest risk exposure, including scenarios showing the effect of steepening or flattening changes in the yield curve shape as well as parallel changes in interest rates. Because income simulations assume that the Corporation's balance sheet will remain static over the simulation horizon, the results do not reflect adjustments in strategy that the ALCO could implement in response to rate shifts.

The following table sets forth the estimated change in net interest income from an unchanged interest rate scenario over the periods indicated for parallel changes in market interest rates using the Corporation's on and off-balance sheet

---

financial instruments as of September 30, 2007 and December 31, 2006. Interest rates are assumed to shift by a parallel 100 or 200 basis points upward or 100 basis points downward over the periods indicated, except for core savings deposits, which are assumed to shift by lesser amounts due to their relative historical insensitivity to market interest rate movements. Further, deposits are assumed to have certain minimum rate levels below which they will not fall. It should be noted that the rate scenarios shown do not necessarily reflect the ALCO's view of the "most likely" change in interest rates over the periods indicated.

|                               | September 30, 2007 |                | December 31, 2006 |                |
|-------------------------------|--------------------|----------------|-------------------|----------------|
|                               | Months 1 - 12      | Months 13 - 24 | Months 1 - 12     | Months 13 - 24 |
| 100 basis point rate decrease | -2.53%             | -2.83%         | -1.63%            | -2.47%         |
| 100 basis point rate increase | -1.67%             | -5.42%         | -1.18%            | -5.03%         |
| 200 basis point rate increase | -1.12%             | -8.63%         | -0.78%            | -8.01%         |

The ALCO estimates that the exposure of net interest income to falling rates as compared to an unchanged rate scenario results from a more rapid decline in earning asset yields compared to rates paid in deposits. If rates were to fall and remain low for a sustained period, certain core savings and time deposit rates could decline more slowly and by a lesser amount than other market rates. Asset yields would likely decline more rapidly than deposit costs as current asset holdings mature or reprice, since cash flow from mortgage-related prepayments and redemption of callable securities would increase as market rates fall.

The moderately neutral exposure of net interest income to rising rates in Year 1 as compared to an unchanged rate scenario results from a relative balance between anticipated increases in asset yields and funding costs over the near term. For simulation purposes, core savings deposit rate changes are anticipated to lag other market rates in both timing and magnitude. The ALCO's estimate of interest rate risk exposure to rising rate environments, including those involving changes to the shape of the yield curve, incorporates certain assumptions regarding the shift in mix from low-cost core savings deposits to higher-cost deposit categories, which has characterized a shift in funding mix during the most recent rising interest rate cycle. This shift begins to affect net interest income exposure to rising rates in Year 1 and continues into Year 2 of rising simulations.

The negative exposure of net interest income to rising rates in Year 2 as compared to an unchanged rate scenario is primarily attributable to an increase in funding costs associated with retail deposits. Increases in interest rates have created greater growth in rate-sensitive money market and time deposits than growth in other lower-cost deposit categories. The ALCO remodeling process assumes that this shift in deposit mix towards higher cost deposit categories would continue if interest rates were to increase, and that this assumption accurately reflects historical operating conditions in rising rate cycles. Although asset yields would also increase in a rising interest rate environment, the cumulative impact of relative growth in the rate-sensitive higher cost deposit category suggests that by Year 2 of rising interest rate scenarios, the increase in the Corporation's cost of funds could result in a relative decline in net interest margin compared to an unchanged rate scenario.

While the ALCO reviews simulation assumptions and back-tests simulation results to ensure that they are reasonable and current, income simulation may not always prove to be an accurate indicator of interest rate risk or future net interest margin. Over time, the repricing, maturity and prepayment characteristics of financial instruments and the composition of the Corporation's balance sheet may change to a different degree than estimated. Simulation modeling assumes a static balance sheet, with the exception of certain modeled deposit mix shifts from low-cost core savings deposits to higher-cost money market and time deposits noted above. The static balance sheet assumption does not necessarily reflect the Corporation's expectation for future balance sheet growth, which is a function of the business environment and customer behavior. Another significant simulation assumption is the sensitivity of core savings deposits to fluctuations in interest rates. Income simulation results assume that changes in both core savings deposit rates and balances are related to changes in short-term interest rates. The assumed relationship between short-term interest rate changes and core deposit rate and balance changes used in income simulation may differ from the ALCO's

estimates. Lastly, mortgage-backed securities and mortgage loans involve a level of risk that unforeseen changes in prepayment speeds may cause related cash flows to vary significantly in differing rate environments. Such changes could affect the level of reinvestment risk associated with cash flow from these instruments, as well as their market value. Changes in prepayment speeds could also increase or decrease the amortization of premium or accretion of discounts related to such instruments, thereby affecting interest income.

-37-

---



The Corporation also monitors the potential change in market value of its available for sale debt securities in changing interest rate environments. The purpose is to determine market value exposure that may not be captured by income simulation, but which might result in changes to the Corporation's capital position. Results are calculated using industry-standard analytical techniques and securities data. Available for sale equity securities are excluded from this analysis because the market value of such securities cannot be directly correlated with changes in interest rates. The following table summarizes the potential change in market value of the Corporation's available for sale debt securities as of September 30, 2007 and December 31, 2006 resulting from immediate parallel rate shifts:

| (Dollars in thousands)   | Down 100<br>Basis<br>Points | Up 200<br>Basis<br>Points |
|--|-----------------------------|---------------------------|
| Security Type  |                             |                           |
| U.S. Treasury and government-sponsored agency securities (noncallable) (as restated) | \$ 2,467                    | \$ (4,543)                |
| U.S. government-sponsored agency securities (callable) (as restated)                 | 466                         | (4,689)                   |
| States and political subdivision (as restated)                                       | 5,287                       | (12,615)                  |
| Mortgage-backed securities (as restated)   | 8,318                       | (23,300)                  |
| Corporate securities   | 252                         | (514)                     |
| Total change in market value as of September 30, 2007 (as restated)                  | \$ 16,790                   | \$ (45,661)               |
| Total change in market value as of December 31, 2006                                 | \$ 11,567                   | \$ (29,447)               |

See additional discussion in Note 10 to the Corporation's Consolidated Financial Statements for more information regarding the nature and business purpose of financial instruments with off-balance sheet risk and derivative financial instruments.

### ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Information regarding quantitative and qualitative disclosures about market risk appears under Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations," under the caption "Asset/Liability Management and Interest Rate Risk."

### ITEM 4. Controls and Procedures

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), the Corporation carried out an evaluation under the supervision and with the participation of the Corporation's management, including the Corporation's principal executive officer and principal financial and accounting officer, of the effectiveness of the design and operation of the Corporation's disclosure controls and procedures as of the end of the quarter ended September 30, 2007. Based upon that evaluation, the Corporation's principal executive officer and principal financial and accounting officer concluded that the Corporation's disclosure controls and procedures are effective and designed to ensure that information required to be disclosed by the Corporation in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. The Corporation will continue to review and document its disclosure controls and procedures and consider such changes in future evaluations of the effectiveness of such controls and procedures, as it deems appropriate. There has been no change in our internal control over financial reporting during the period ended September 30, 2007 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II

### Other Information

#### Item 1. Legal Proceedings

The Corporation is involved in various claims and legal proceedings arising out of the ordinary course of business. Management is of the opinion, based on its review with counsel of the development of such matters to date, that the ultimate disposition of such matters will not materially affect the consolidated financial position or results of

operations of the Corporation.

**Item 1A. Risk Factors**

There have been no material changes in the risk factors described in Item 1A of Washington Trust's Annual Report on Form 10-K for the year ended December 31, 2006.

-38-

---

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following table provides information as of and for the quarter ended September 30, 2007 regarding shares of common stock of the Corporation that were repurchased under the Deferred Compensation Plan, the 2006 Stock Repurchase Plan, the Amended and Restated 1988 Stock Option Plan (the “1988 Plan”), the Bancorp’s 1997 Equity Incentive Plan, as amended (the “1997 Plan”), and the Bancorp’s 2003 Stock Incentive Plan, as amended (the “2003 Plan”).

|   | Total<br>number of<br>shares<br>purchased | Average<br>price paid<br>per share | Total<br>number of<br>shares<br>purchased<br>as part of<br>publicly<br>announced<br>plan(s) | Maximum<br>number of<br>shares that<br>may yet be<br>purchased<br>under the<br>plan(s) |
|---|---|------------------------------------|---|--|
| <b>Deferred Compensation Plan (1)</b>       |   |                                    |   |  |
| Balance at beginning of period              |   |                                    |   | N/A  |
| 7/1/2007 to 7/31/2007                       | 627                                       | \$ 24.27                           | 627   | N/A  |
| 8/1/2007 to 8/31/2007                       | 216                                       | 26.03                              | 216   | N/A  |
| 9/1/2007 to 9/30/2007                       | 225                                       | 26.33                              | 225   | N/A  |
| <b>Total Deferred Compensation Plan</b>     | <b>1,068</b>                              | <b>\$ 25.06</b>                    | <b>1,068</b>  | <b>N/A</b>   |
| <b>2006 Stock Repurchase Plan (2)</b>       |   |                                    |   |  |
| Balance at beginning of period              |   |                                    |   | 250,300  |
| 7/1/2007 to 7/31/2007                       | –   | –                                  | –   | 250,300  |
| 8/1/2007 to 8/31/2007                       | 21,200                                    | \$ 25.93                           | 21,200  | 229,100  |
| 9/1/2007 to 9/30/2007                       | 14,500                                    | 25.61                              | 14,500  | 214,600  |
| <b>Total 2006 Stock Repurchase Plan</b>     | <b>35,700</b>                             | <b>\$ 25.80</b>                    | <b>35,700</b>   | <b>214,600</b>   |
| <b>Other (3)</b>                            |   |                                    |   |  |
| Balance at beginning of period              |   |                                    |   | N/A  |
| 7/1/2007 to 7/31/2007                       | 23  | \$ 18.25                           | 23  | N/A  |
| 8/1/2007 to 8/31/2007                       | 6,204                                     | 18.92                              | 6,204   | N/A  |
| 9/1/2007 to 9/30/2007                       | 5,081                                     | 18.25                              | 5,081   | N/A  |
| <b>Total Other</b>                          | <b>11,308</b>                             | <b>\$ 18.62</b>                    | <b>11,308</b>   | <b>N/A</b>   |
| <b>Total Purchases of Equity Securities</b> | <b>48,076</b>                             | <b>\$ 24.09</b>                    | <b>48,076</b>   |  |

- (1) The Deferred Compensation Plan was established on January 1, 1999. This plan allows directors and officers to defer a portion of their compensation. The deferred compensation is contributed to a rabbi trust that invests the assets of the trust into selected mutual funds as well as shares of the Bancorp’s common stock pursuant to the direction of the plan participants. The plan authorizes Bancorp to acquire shares of Bancorp’s common stock to satisfy its obligation under this plan. All shares are purchased in the open market.
- (2) The 2006 Stock Repurchase Plan was established in December 2006. A maximum of 400,000 shares were authorized under the plan. The Bancorp plans to hold the repurchased shares as treasury stock for general corporate purposes.
- (3) Pursuant to the Corporation’s share-based compensation plans, employees may deliver back shares of stock previously issued in payment of the exercise price of stock options. While required to be reported in this table, such transactions are not reported as share repurchases in the Corporation’s Consolidated Financial Statements. The Corporation’s share-based compensation plans (the 1988 Plan, the 1997 Plan and the 2003 Plan) have expiration dates of December 31, 1997, April 29 2007 and April 29, 2013, respectively.



**Item 6. Exhibits**

(a) Exhibits. The following exhibits are included as part of this Form 10-Q:

Exhibit  
Number

- 3.1 Amended and Restated By-Laws of Washington Trust Bancorp Inc. - Filed as Exhibit 3.1 to the Bancorp's Current Report on Form 8-K (File No. 000-13091), as filed with the Securities and Exchange Commission on September 24, 2007 (1)
  - 15.1 Letter re: Unaudited Interim Financial Information - Filed herewith.
  - 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. – Filed herewith.
  - 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. – Filed herewith.
  - 32.1 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 – Filed herewith. (2)
- (1) Not filed herewith. In accordance with Rule 12b-32 promulgated pursuant to the Exchange Act, reference is made to the documents previously filed with the SEC, which are incorporated by reference herein.
- (2) These certifications are not “filed” for purposes of Section 18 of the Exchange Act or incorporated by reference into any filing under the Securities Act or the Exchange Act.

**SIGNATURES**

Pursuant to the requirements 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.

WASHINGTON TRUST BANCORP, INC.  
(Registrant)

Date: November 9, 2007

By: /s/ John C. Warren  
John C. Warren  
Chairman and Chief Executive Officer  
(principal executive officer)

Date: November 9, 2007

By: /s/ David V. Devault  
David V. Devault  
Executive Vice President, Secretary, Treasurer and  
Chief Financial Officer  
(principal financial and accounting officer)

**Exhibit Index**

Exhibit  
Number

- 3.1 Amended and Restated By-Laws of Washington Trust Bancorp Inc. - Filed as Exhibit 3.1 to the Bancorp's Current Report on Form 8-K (File No. 000-13091), as filed with the Securities and Exchange Commission on September 24, 2007 (1)
  - 15.1 Letter re: Unaudited Interim Financial Information - Filed herewith.
  - 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. – Filed herewith.
  - 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. – Filed herewith.
  - 32.1 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 – Filed herewith. (2)
- (1) Not filed herewith. In accordance with Rule 12b-32 promulgated pursuant to the Exchange Act, reference is made to the documents previously filed with the SEC, which are incorporated by reference herein.
- (2) These certifications are not “filed” for purposes of Section 18 of the Exchange Act or incorporated by reference into any filing under the Securities Act or the Exchange Act.