

WASHINGTON TRUST BANCORP INC  
Form 10-Q  
August 08, 2006

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 **JUNE 30, 2006** 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

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 July 31, 2006 was 13,442,052.

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**WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES**  
For the Quarter Ended June 30, 2006

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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 (as defined below) 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 and trust 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, 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.

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Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****WASHINGTON TRUST BANCORP, INC. AND  
SUBSIDIARIES****(Dollars in thousands)****CONSOLIDATED BALANCE SHEETS**

	(Unaudited)	
	June 30, 2006	December 31, 2005
<b>Assets:</b>		
Cash and due from banks	\$ 44,042	\$ 48,997
Federal funds sold and other short-term investments	8,133	17,166
Mortgage loans held for sale	1,362	439
<b>Securities:</b>		
Available for sale, at fair value; amortized cost \$636,298 in 2006 and \$620,638 in 2005	625,793	619,234
Held to maturity, at cost; fair value \$155,484 in 2006 and \$162,756 in 2005	160,458	164,707
Total securities	786,251	783,941
Federal Home Loan Bank stock, at cost	33,915	34,966
<b>Loans:</b>		
Commercial and other	565,609	554,734
Residential real estate	589,194	582,708
Consumer	276,505	264,466
Total loans	1,431,308	1,401,908
Less allowance for loan losses	18,480	17,918
Net loans	1,412,828	1,383,990
Premises and equipment, net	24,261	23,737
Accrued interest receivable	10,749	10,594
Investment in bank-owned life insurance	38,985	30,360
Goodwill	39,963	39,963
Identifiable intangible assets, net	13,598	14,409
Other assets	18,190	13,441
Total assets	\$ 2,432,277	\$ 2,402,003
<b>Liabilities:</b>		
<b>Deposits:</b>		
Demand deposits	\$ 184,227	\$ 196,102
NOW accounts	178,063	178,677
Money market accounts	239,912	223,255
Savings accounts	191,585	212,499
Time deposits	877,010	828,725
Total deposits	1,670,797	1,639,258
Dividends payable	2,554	2,408
Federal Home Loan Bank advances	543,588	545,323
Junior subordinated debentures	22,681	22,681
Other borrowings	7,173	9,774
Accrued expenses and other liabilities	24,155	24,113
Total liabilities	2,270,948	2,243,557
<b>Shareholders' Equity:</b>		
Common stock of \$.0625 par value; authorized 30,000,000 shares; issued 13,443,046 shares in 2006 and 13,372,295 in 2005	840	836
Paid-in capital	34,516	32,778

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Retained earnings	133,880	126,735
Accumulated other comprehensive loss	(7,566)	(1,653)
Treasury stock, at cost; 13,677 shares in 2006 and 10,519 shares in 2005	(341)	(250)
Total shareholders' equity	161,329	158,446
Total liabilities and shareholders' equity	\$ 2,432,277	\$ 2,402,003

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

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BANCORP, INC. AND  
SUBSIDIARIES  
CONSOLIDATED  
STATEMENTS OF INCOME****(Dollars and shares in thousands,  
except per share amounts)**

Periods ended June 30,	<b>Three Months</b>		<b>Six Months</b>	
	2006	2005	2006	2005
<b>Interest income:</b>				
Interest and fees on loans	\$ 23,130	\$ 19,096	\$ 45,027	\$ 36,921
<b>Interest on securities:</b>				
Taxable	8,648	8,285	17,060	16,719
Nontaxable	371	204	699	389
Dividends on corporate stock and Federal Home Loan Bank stock	249	625	926	1,244
Interest on federal funds sold and other short-term investments	150	79	265	134
<b>Total interest income</b>	<b>32,548</b>	<b>28,289</b>	<b>63,977</b>	<b>55,407</b>
<b>Interest expense:</b>				
Deposits	11,161	7,627	21,399	14,559
Federal Home Loan Bank advances	5,745	5,670	11,104	11,219
Junior subordinated debentures	338	-	676	-
Other	87	20	166	36
<b>Total interest expense</b>	<b>17,331</b>	<b>13,317</b>	<b>33,345</b>	<b>25,814</b>
<b>Net interest income</b>	<b>15,217</b>	<b>14,972</b>	<b>30,632</b>	<b>29,593</b>
Provision for loan losses	300	300	600	600
<b>Net interest income after provision for loan losses</b>	<b>14,917</b>	<b>14,672</b>	<b>30,032</b>	<b>28,993</b>
<b>Noninterest income:</b>				
Wealth management and trust services	6,177	3,486	12,059	6,698
Service charges on deposit accounts	1,236	1,168	2,355	2,179
Merchant processing fees	1,656	1,337	2,703	2,115
Income from bank-owned life insurance	346	279	625	551
Net gains on loan sales	336	418	612	905
Net realized gains on securities	765	3	824	3
Other income	931	303	1,789	622
<b>Total noninterest income</b>	<b>11,447</b>	<b>6,994</b>	<b>20,967</b>	<b>13,073</b>
<b>Noninterest expense:</b>				
Salaries and employee benefits	9,830	7,450	19,449	14,909
Net occupancy	1,018	802	1,972	1,655
Equipment	881	869	1,680	1,751
Merchant processing costs	1,407	1,098	2,294	1,734
Advertising and promotion	681	733	1,118	1,036
Outsourced services	496	444	1,014	857
Legal, audit and professional fees	403	520	779	912
Amortization of intangibles	406	99	811	246

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Other	2,158	1,358	3,867	2,717
Total noninterest expense	17,280	13,373	32,984	25,817
Income before income taxes	9,084	8,293	18,015	16,249
Income tax expense	2,907	2,654	5,765	5,200
Net income	\$ 6,177	\$ 5,639	\$ 12,250	\$ 11,049
Weighted average shares				
outstanding - basic	13,419.9	13,296.0	13,403.4	13,289.4
Weighted average shares				
outstanding - diluted	13,703.2	13,592.3	13,699.6	13,602.3
Per share information:				
Basic earnings per share	\$ 0.46	\$ 0.42	\$ 0.91	\$ 0.83
Diluted earnings per share	\$ 0.45	\$ 0.41	\$ 0.89	\$ 0.81
Cash dividends declared per share	\$ 0.19	\$ 0.18	\$ 0.38	\$ 0.36

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

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Table of Contents**WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS****(Dollars in thousands)**

Six months ended June 30,	2006	2005
<b>Cash flows from operating activities:</b>		
Net income	\$ 12,250	\$ 11,049
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	600	600
Depreciation of premises and equipment	1,513	1,507
Net amortization of premium and discount	791	1,210
Net amortization of intangibles	811	246
Share-based compensation	360	154
Earnings from bank-owned life insurance	(625)	(551)
Net gains on loan sales	(612)	(905)
Net realized gains on securities	(824)	(3)
Proceeds from sales of loans	18,208	28,103
Loans originated for sale	(18,646)	(28,353)
Increase in accrued interest receivable, excluding purchased interest	(51)	(390)
Increase in other assets	(1,562)	(3,046)
Increase in accrued expenses and other liabilities	42	1,121
Other, net	(101)	37
Net cash provided by operating activities	12,154	10,779
<b>Cash flows from investing activities:</b>		
Purchases of: Mortgage-backed securities available for sale	(23,854)	(31,993)
Other investment securities available for sale	(41,868)	(22,223)
Mortgage-backed securities held to maturity	-	(17,505)
Other investment securities held to maturity	(12,526)	(14,113)
Proceeds from sale of: Mortgage-backed securities available for sale	1,026	-
Other investment securities available for sale	193	41,199
Maturities and principal payments of: Mortgage-backed securities available for sale	49,168	59,193
Other investment securities available for sale	-	30,000
Mortgage-backed securities held to maturity	8,965	13,675
Other investment securities held to maturity	7,685	2,110
Remittance (purchase) of Federal Home Loan Bank stock	1,051	(593)
Principal collected on loans under loan originations	(8,016)	(40,454)
Purchases of loans, including purchased interest	(21,592)	(55,207)
Purchases of premises and equipment	(2,037)	(1,425)
Purchases of bank-owned life insurance	(8,000)	-
Net cash used in investing activities	(49,805)	(37,336)
<b>Cash flows from financing activities:</b>		
Net increase in deposits	31,541	72,819
Net decrease in other borrowings	(2,601)	(541)
Proceeds from Federal Home Loan Bank advances	338,104	387,683
Repayment of Federal Home Loan Bank advances	(339,814)	(434,753)
Purchases of treasury stock, net	(91)	20
Proceeds from the issuance of common stock under dividend reinvestment plan	610	-
Proceeds from the exercise of share options	632	226
Tax benefit from share option exercises	241	-

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Cash dividends paid	(4,959)	(4,651)
Net cash provided by financing activities	23,663	20,803
Net decrease in cash and cash equivalents	(13,988)	(5,754)
Cash and cash equivalents at beginning of year	66,163	52,081
Cash and cash equivalents at end of period	\$ 52,175	\$ 46,327
<b>Noncash Investing and Financing Activities:</b> Loans charged off	\$ 151	\$ 238
<b>Supplemental Disclosures:</b> Interest payments	32,588	25,023
Income tax payments (refunds)	6,400	5,241

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

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**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 and trust 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 accounting principles generally accepted in the United States of America (“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 change are the determination of the allowance for loan losses and the review of goodwill and other intangible assets for impairment.

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 June 30, 2006 and December 31, 2005, respectively, and the results of operations and cash flows for the interim periods presented. 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 accounting principles generally accepted in the United States of America. 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, 2005.

**(2) New Accounting Pronouncements**

In May 2005, the Financial Accounting Standards Board (“FASB”) issued SFAS No. 154, “Accounting Changes and Error Corrections”. SFAS No 154 replaces Accounting Principles Board (“APB”) Opinion No. 20, “Accounting Changes”, and FASB Statement No. 3, “Reporting Accounting Changes in Interim Financial Statements”, and changes the requirements for the accounting for and reporting of a change in accounting principle. This Statement applies to all voluntary changes in accounting principles. It also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. APB Opinion 20 previously required that most voluntary changes in accounting principle be recognized by including in net income of the period of the change the cumulative effect of changing to the new accounting principle. SFAS No. 154 requires retrospective application to prior periods’ financial statements of changes in accounting principle, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. SFAS No. 154 defines retrospective application as the application of a different accounting principle to prior accounting periods as if that principle had always been used or as the adjustment of previously issued financial statements to reflect a change in the reporting

entity. This Statement also redefines restatement as the revising of previously issued financial statements to reflect the correction of an error. This Statement requires that retrospective application of a change in accounting principle be limited to the direct effects of the change. This Statement carries forward without change the guidance contained in APB Opinion 20 for reporting the correction of an error in previously issued financial statements and a change in accounting estimate. This Statement also carries forward the guidance in APB Opinion 20 requiring justification of a change in accounting principle on the basis of preferability. This Statement was effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The adoption of SFAS No. 154 did not have a material impact on the Corporation's financial position or results of operations.

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

In November 2005, the FASB issued FASB Staff Position (“FSP”) 115-1, “The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments.” This FSP provides additional guidance on when an investment in a debt or equity security should be considered impaired, and when that impairment should be considered other-than-temporary and recognized as a loss in earnings. Specifically, the guidance clarifies that an investor should recognize an impairment loss no later than when the impairment is deemed other-than-temporary, even if a decision to sell has not been made. The FSP also requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. This FSP was effective for reporting periods beginning after December 15, 2005. The adoption of FSP 115-1 did not have a material impact on the Corporation’s financial position or results of operations.

In February 2006, the FASB issued SFAS No. 155, “Accounting for Certain Hybrid Financial Instruments - an amendment of FASB Statements No. 133 and 140.” This Statement 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. This Statement 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 this Statement 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 Corporation believes the adoption of SFAS No. 155 will 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.” This Statement 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 after September 15, 2006. The Corporation believes the adoption of SFAS No. 156 will not have a material impact on the Corporation’s financial position or results of operations.

In June 2006, the FASB issued 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 provisions of FIN 48 are effective for fiscal years beginning after December 15, 2006. The provisions of FIN 48 are to be applied to all tax positions upon initial adoption of this standard. Only tax positions that meet the more-likely-than-not recognition threshold at the effective date may be recognized or continue to be recognized upon adoption of FIN 48. The Corporation has not yet determined the potential financial impact of adopting FIN 48.

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

**(3) Share-Based Compensation Arrangements**

Washington Trust has three share-based compensation plans, which are described below. Effective January 1, 2006, the fair value recognition provisions of SFAS 123R, "Share-Based Payment", were adopted on a modified prospective basis. Prior to this date, the provisions of APB No. 25 and related interpretations were applied for option grant accounting.

In the Corporation's consolidated financial statements for the three and six months ended June 30, 2005, the following pro forma net income and earnings per share information was disclosed in accordance with SFAS No. 123 and SFAS No. 148:

(Dollars in thousands, except per share amounts)

		Three Months Ended June 30, 2005	Six Months Ended June 30, 2005
Net income	As reported	\$ 5,639	\$ 11,049
Less total share-based compensation determined under the fair value method for all awards, net of tax		(590)	(728)
Pro forma		\$ 5,049	\$ 10,321
Basic earnings per share	As reported	\$ 0.42	\$ 0.83
Pro forma		\$ 0.38	\$ 0.78
Diluted earnings per share	As reported	\$ 0.41	\$ 0.81
Pro forma		\$ 0.37	\$ 0.76

The Bancorp's 2003 Stock Incentive Plan, as amended (the "2003 Plan"), which is shareholder approved, permits the granting of share options and other equity incentives to officers, employees, directors, and other key persons. Up to 600,000 shares of the Bancorp's common stock may be used from authorized but unissued shares, treasury stock, shares reacquired by the Corporation, or shares available from expired or terminated awards. No more than 200,000 shares may be issued in the form of awards other than share options or stock appreciation rights. Share options are designated as either non-qualified or incentive share options. Incentive share option awards may be granted at any time until February 20, 2013.

The Bancorp's 1997 Equity Incentive Plan, as amended (the "1997 Plan"), which is shareholder approved, permits the granting of share options and other equity incentives to key employees, directors, advisors, and consultants. Up to 1,012,500 shares of the Bancorp's common stock may be used from authorized but unissued shares, treasury stock, shares reacquired by the Corporation, or shares available from expired or terminated awards. Share options are designated as either non-qualified or incentive share options. Incentive share option awards may be granted at any time until April 29, 2007.

The Amended and Restated 1988 Stock Option Plan (the "1988 Plan"), which was shareholder approved, provided for the granting of share options to directors, officers and key employees. The 1988 Plan permitted share options to be granted at any time until December 31, 1997. The 1988 Plan provided for shares of the Bancorp's common stock to be used from authorized but unissued shares, treasury stock, or shares available from expired awards. Share options were

designated as either non-qualified or incentive share options.

The 1988 Plan, the 1997 Plan and the 2003 Plan (collectively, "the Plans") permit options to be granted with stock appreciation rights ("SARs"), however, no share options have been granted with SARs. Pursuant to the Plans, the exercise price of each share option may not be less than fair market value of the common stock on the date of the grant. In general, the share option price is payable in cash, by the delivery of shares of common stock already owned by the grantee, or a combination thereof. Nonvested share units and shares are valued at the fair market value of the common stock as of the award date. No option, share unit or share awards made prior to January 1, 2003 had requisite vesting periods remaining as of January 1, 2006. Share options awarded during 2003, 2004 and 2005 were granted with a variety of vesting terms including immediate vesting, graded vesting over three-year periods and cliff vesting over three-year periods. Nonvested share units or shares awarded during 2004, 2005 and 2006 were granted with vesting terms ranging from one to five years. Share option and share awards provide for accelerated vesting if there is a change in control (as defined in the Plans).

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

Amounts recognized in the consolidated financial statements for share option, nonvested share unit and nonvested share awards are as follows:

(Dollars in thousands)

Periods ended June 30,	Three Months		Six Months	
	2006	2005	2006	2005
Share-based compensation expense	\$ 179	\$ 84	\$ 360	\$ 154
Related income tax benefit	56	30	107	54

A summary of share option activity under the Plans as of June 30, 2006, and changes during the six months ended June 30, 2006, is presented below:

(Dollars in thousands)

	Number of Share Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding at January 1, 2006	1,198,111	\$ 20.31	-	-
Granted	-	-	-	-
Exercised	67,146	15.24	-	-
Forfeited or expired	5,583	27.13	-	-
Outstanding at June 30, 2006	1,125,382	\$ 20.58	5.8 years	\$ 8,089
Exercisable at June 30, 2006	1,096,047	\$ 20.40	5.8 years	\$ 8,083

The total intrinsic value of share options exercised during the six months ended June 30, 2006 was \$774 thousand.

A summary of the status of Washington Trust's nonvested shares as of June 30, 2006, and changes during the six months ended June 30, 2006, is presented below:

	Number of Shares	Weighted Average Grant Date Fair Value
Nonvested at January 1, 2006	55,850	\$ 24.77
Granted	17,400	26.59
Vested	-	-
Forfeited	(450)	23.61
Nonvested at June 30, 2006	72,800	\$ 25.21

As of June 30, 2006, there was \$1.2 million of total unrecognized compensation cost related to nonvested share-based compensation arrangements (including share option and nonvested share awards) granted under the Plans. That cost is expected to be recognized over a weighted average period of 2.2 years.





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

**(4) Securities**

Securities available for sale are summarized as follows:

(Dollars in thousands)	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
<b>June 30, 2006</b>				
U.S. Treasury obligations and obligations of U.S. government-sponsored agencies	\$ 145,126	\$ 63	\$ (2,503)	\$ 142,686
Mortgage-backed securities	411,237	579	(14,615)	397,201
Corporate bonds	63,560	322	(652)	63,230
Corporate stocks	16,375	6,747	(446)	22,676
Total	636,298	7,711	(18,216)	625,793

**December 31, 2005**

U.S. Treasury obligations and obligations of U.S. government-sponsored agencies	107,135	1,332	(816)	107,651
Mortgage-backed securities	436,142	1,019	(8,987)	428,174
Corporate bonds	63,565	346	(716)	63,195
Corporate stocks	13,796	6,573	(155)	20,214
Total	\$ 620,638	\$ 9,270	\$ (10,674)	\$ 619,234

Securities held to maturity are summarized as follows:

(Dollars in thousands)	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
<b>June 30, 2006</b>				
U.S. Treasury obligations and obligations of U.S. government-sponsored agencies	\$ 42,000	\$ -	\$ (936)	\$ 41,064
Mortgage-backed securities	76,487	243	(2,814)	73,916
States and political subdivisions	41,971	15	(1,482)	40,504
Total	160,458	258	(5,232)	155,484

**December 31, 2005**

U.S. Treasury obligations and obligations of U.S. government-sponsored agencies	47,250	-	(797)	46,453
Mortgage-backed securities	84,960	768	(1,527)	84,201
States and political subdivisions	32,497	72	(467)	32,102
Total	\$ 164,707	\$ 840	\$ (2,791)	\$ 162,756

Securities available for sale and held to maturity with a fair value of \$580.5 million and \$564.3 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 June 30, 2006 and December 31, 2005, respectively. In addition, securities available for sale and held to maturity with a fair value of \$11.1 million and \$13.8 million were collateralized for the

discount window at the Federal Reserve Bank at June 30, 2006 and December 31, 2005, respectively. There were no borrowings with the Federal Reserve Bank at either date. Securities available for sale with a fair value of \$2.0 million and \$2.2 million were designated in a rabbi trust for a nonqualified retirement plan at June 30, 2006 and December 31, 2005, respectively.

At June 30, 2006 and December 31, 2005, the available for sale and held to maturity securities portfolio included \$15.5 million and \$3.4 million of net pretax unrealized losses, respectively. Included in these net amounts were gross unrealized losses amounting to \$23.4 million and \$13.5 million at June 30, 2006 and December 31, 2005, respectively.

The following tables summarize, for all securities in an unrealized loss position at June 30, 2006 and December 31, 2005, respectively, the aggregate fair value and gross unrealized loss by length of time those securities have been continuously in an unrealized loss position.

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

(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 June 30, 2006</b>									
U.S. Treasury obligations and obligations of U.S. government-sponsored agencies	13	\$ 110,346	\$ 1,546	11	\$ 67,357	\$ 1,893	24	\$ 177,703	\$ 3,439
Mortgage-backed securities	47	118,588	3,039	74	285,004	14,389	121	403,592	17,428
States and political subdivisions	46	29,603	1,122	14	7,380	360	60	36,983	1,482
Corporate bonds	5	13,033	277	10	28,389	375	15	41,422	652
Subtotal, debt securities	111	271,570	5,984	109	388,130	17,017	220	659,700	23,001
Corporate stocks	10	8,195	370	1	435	76	11	8,630	446
Total temporarily impaired securities	121	\$ 279,765	\$ 6,354	110	\$ 388,565	\$ 17,093	231	\$ 668,330	\$ 23,447

(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, 2005</b>									
U.S. Treasury obligations and obligations of U.S. government-sponsored agencies	12	\$ 70,586	\$ 827	6	\$ 43,464	\$ 786	18	\$ 114,050	\$ 1,613
Mortgage-backed securities	56	178,688	2,565	47	238,844	7,949	103	417,532	10,514
States and political subdivisions	33	19,129	349	5	3,557	118	38	22,686	467
Corporate bonds	5	10,929	75	9	25,019	641	14	35,948	716
Subtotal, debt securities	106	279,332	3,816	67	310,884	9,494	173	590,216	13,310
Corporate stocks	6	2,617	126	1	483	28	7	3,100	155
Total temporarily impaired securities	112	\$ 281,949	\$ 3,942	68	\$ 311,367	\$ 9,522	180	\$ 593,316	\$ 13,465

For those debt securities whose amortized cost exceeds fair value, the primary cause is related to interest rates. The majority of debt securities reported in an unrealized loss position at June 30, 2006 were purchased during 2005, 2004 and 2003, during which time interest rates were at or near historical lows. The relative increase in short and medium term interest rates resulted in a decline in market value for these debt securities. The Corporation believes that the nature and duration of impairment on its debt security holdings are primarily a function of future 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 debt securities in an unrealized loss position at June 30, 2006 consisted of 220 debt security holdings. The largest loss percentage of any single holding was 7.21% 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 June 30, 2006 consisted of 11 holdings of financial and commercial entities. The largest loss percentage position of any single holding was 14.84% of its cost.

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

**(5) Loan Portfolio**

The following is a summary of loans:

(Dollars in thousands)	June 30, 2006		December 31, 2005	
	Amount	%	Amount	%
<b>Commercial:</b>				
Mortgages (1)	\$ 273,186	19%	\$ 291,292	21%
Construction and development (2)	33,768	2%	37,190	3%
Other (3)	258,655	19%	226,252	16%
Total commercial	565,609	40%	554,734	40%
<b>Residential real estate:</b>				
Mortgages (4)	568,914	40%	565,680	40%
Homeowner construction	20,280	1%	17,028	2%
Total residential real estate	589,194	41%	582,708	42%
<b>Consumer</b>				
Home equity lines	153,037	11%	161,100	11%
Home equity loans	84,030	6%	72,288	5%
Other	39,438	2%	31,078	2%
Total consumer	276,505	19%	264,466	18%
Total loans (5)	\$ 1,431,308	100%	\$ 1,401,908	100%

(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 9 for additional discussion of FHLB borrowings).

(5) Net of unamortized loan origination fees, net of costs, totaling \$302 thousand and \$373 thousand at June 30, 2006 and December 31, 2005, respectively. Also includes \$484 thousand and \$753 thousand of premium, net of discount, on purchased loans at June 30, 2006 and December 31, 2005, respectively.

**(6) Allowance For Loan Losses**

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

(Dollars in thousands)	Three Months			Six Months		
	2006		2005	2006		2005
Periods ended June 30,						
Balance at beginning of period	\$	18,247	\$	17,058	\$	16,771
Provision charged to expense		300		300		600
Subtotal		18,547		17,358		17,371
Charge-offs		(113)		(134)		(238)
Recoveries		46		218		309

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Net recoveries (charge-offs)		(67)		84		(38)		71
Balance at end of period	\$	18,480	\$	17,442	\$	18,480	\$	17,442

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

**(7) Goodwill and Other Intangibles**

The changes in the carrying value of goodwill and other intangible assets for the six months ended June 30, 2006 are as follows:

**Goodwill**

(Dollars in thousands)	Commercial Banking Segment	Wealth Management Service Segment	Total
Balance at December 31, 2005	\$ 22,591	\$ 17,372	\$ 39,963
Goodwill acquired during the period	-	-	-
Impairment recognized	-	-	-
Balance at June 30, 2006	\$ 22,591	\$ 17,372	\$ 39,963

**Other Intangible Assets**

	Core Deposit Intangible	Advisory Contracts	Non-compete Agreements	Total
Balance at December 31, 2005	\$ 911	\$ 13,220	\$ 278	\$ 14,409
Amortization	131	656	24	811
Balance at June 30, 2006	\$ 780	\$ 12,564	\$ 254	\$ 13,598

Amortization of intangible assets for the six months ended June 30, 2006, totaled \$811 thousand. 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 Deposits	Advisory Contracts	Non-compete Agreements	Total
Estimated amortization expense:				
2006 (full year)	\$ 261	\$ 1,283	\$ 49	\$ 1,593
2007	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

The components of intangible assets at June 30, 2006 are as follows:

(Dollars in thousands)

	Core Deposits	Advisory Contracts	Non-compete Agreements	Total
Gross carrying amount	\$ 2,997	\$ 13,657	\$ 1,147	\$ 17,801
Accumulated amortization	2,217	1,093	893	4,203
Net amount	\$ 780	\$ 12,564	\$ 254	\$ 13,598

**(8) 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:

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

(Dollars in thousands)	June 30, 2006	December 31, 2005
Financial instruments whose contract amounts represent credit risk:		
Commitments to extend credit:		
Commercial loans	\$ 108,573	\$ 105,971
Home equity lines	180,301	174,073
Other loans	11,844	17,271
Standby letters of credit	11,056	10,986
Financial instruments whose notional amounts exceed the amount of credit risk:		
Forward loan commitments:		
Commitments to originate fixed rate mortgage loans to be sold	2,668	2,188
Commitments to sell fixed rate mortgage loans	4,034	2,626

**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 June 30, 2006 and December 31, 2005, the maximum potential amount of undiscounted future payments, not reduced by amounts that may be recovered, totaled \$11.1 million and \$11.0 million, respectively. At June 30, 2006 and December 31, 2005, there was no liability to beneficiaries resulting from standby letters of credit.

At June 30, 2006, 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 June 30, 2006 and December 31, 2005 and the respective changes in fair values for the six months ended June 30, 2006 and 2005 were insignificant.

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

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

(Dollars in thousands)	June 30, 2006	December 31, 2005
FHLB advances	\$ 543,588	\$ 545,323

In addition to outstanding advances, the Corporation also has access to an unused line of credit amounting to \$8.0 million at June 30, 2006 and December 31, 2005. Under 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

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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 June 30, 2006 and December 31, 2005. Included in the collateral were securities available for sale and held to maturity with a fair value of \$497.2 million and \$498.0 million that were specifically pledged to secure FHLB borrowings at June 30, 2006 and December 31, 2005, respectively. Unless there is an event of default under the agreement 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.

**Junior Subordinated Debentures**

In connection with the Weston Financial Group, Inc. (“Weston Financial”) acquisition, trust preferred securities totaling \$22 million were issued in the third quarter of 2005 by WT Capital Trust I (“Trust I”) and WT Capital Trust II (“Trust II”), capital trusts created by the Bancorp. In accordance with FASB Interpretation 46-R, “Consolidation of Variable Interest Entities - Revised”, Trust I and Trust II are not consolidated into the Corporation’s financial statements; however, the Corporation reflects the amounts of junior subordinated debentures payable to Trust I and Trust II as debt in its financial statements. At June 30, 2006 and December 31, 2005, junior subordinated debentures payable amounted to \$22.7 million.

**Other Borrowings**

The following is a summary of other borrowings:

(Dollars in thousands)	June 30, 2006	December 31, 2005
Treasury, Tax and Loan demand note balance	\$ 1,122	\$ 3,794
Deferred acquisition obligations	5,592	5,469