WASHINGTON TRUST BANCORP INC
Form 10-Q
November 06, 2008

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

FORM 10-Q

(Mark One)
x Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended SEPTEMBER 30, 2008 or

o 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.
x Yes o No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, or a smaller reporting company. See definitions of “large accelerated filer,” “accelerated filer,” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Mark one)

Large accelerated filer o	Accelerated filer x
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
o Yes o No

The number of shares of common stock of the registrant outstanding as of October 31, 2008 was 15,934,475.

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FORM 10-Q
WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES
For the Quarter Ended September 30, 2008

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES

(Dollars in thousands)

CONSOLIDATED BALANCE SHEETS

	Unaudited September 30, 2008	December 31, 2007
Assets:		
Cash and noninterest-bearing balances due from banks	$ 27,099	$ 30,817
Interest-bearing balances due from banks	588	1,973
Federal funds sold and securities purchased under resale agreements	21,857	7,600
Other short-term investments	864	722
Mortgage loans held for sale	1,073	1,981
Securities available for sale, at fair value;		
amortized cost $771,537 in 2008 and $750,583 in 2007	753,456	751,778
Federal Home Loan Bank stock, at cost	42,008	31,725
Loans:		
Commercial and other	841,838	680,266
Residential real estate	618,329	599,671
Consumer	308,874	293,715
Total loans	1,769,041	1,573,652
Less allowance for loan losses	22,631	20,277
Net loans	1,746,410	1,553,375
Premises and equipment, net	24,314	25,420
Accrued interest receivable	10,980	11,427
Investment in bank-owned life insurance	42,714	41,363
Goodwill	56,117	50,479
Identifiable intangible assets, net	10,461	11,433
Other assets	29,941	19,847
Total assets	$ 2,767,882	$ 2,539,940
Liabilities:		
Deposits:		
Demand deposits	$ 187,839	$ 175,542
NOW accounts	164,829	164,944
Money market accounts	298,106	321,600
Savings accounts	171,856	176,278
Time deposits	914,621	807,841
Total deposits	1,737,251	1,646,205
Dividends payable	2,824	2,677
Federal Home Loan Bank advances	747,430	616,417
Junior subordinated debentures	32,991	22,681
Other borrowings	30,439	32,560
Accrued expenses and other liabilities	32,185	32,887
Total liabilities	2,583,120	2,353,427
Shareholders’ Equity:		
Common stock of $.0625 par value; authorized 30,000,000 shares;		
issued 13,518,868 shares in 2008 and 13,492,110 shares in 2007	845	843
Paid-in capital	35,184	34,874
Retained earnings	163,809	154,647

Accumulated other comprehensive loss	(12,570)	(239)
Treasury stock, at cost; 95,635 shares in 2008 and 137,652 shares in 2007	(2,506)	(3,612)
Total shareholders’ equity	184,762	186,513
Total liabilities and shareholders’ equity	$ 2,767,882	$ 2,539,940

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

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WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

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

Unaudited

	Three Months		Nine Months	
Periods ended September 30,	2008	2007	2008	2007
Interest income:				
Interest and fees on loans	$ 25,520	$ 25,032	$ 74,896	$ 73,380
Interest on securities:				
Taxable	8,504	7,565	25,222	23,196
Nontaxable	778	781	2,344	2,208
Dividends on corporate stock and Federal Home Loan Bank stock	407	669	1,516	2,072
Other interest income	128	275	318	650
Total interest income	35,337	34,322	104,296	101,506
Interest expense:				
Deposits	9,884	13,140	31,031	39,332
Federal Home Loan Bank advances	8,011	5,243	23,104	15,323
Junior subordinated debentures	524	338	1,371	1,014
Other interest expense	274	291	863	730
Total interest expense	18,693	19,012	56,369	56,399
Net interest income	16,644	15,310	47,927	45,107
Provision for loan losses	1,100	300	2,950	900
Net interest income after provision for loan losses	15,544	15,010	44,977	44,207
Noninterest income:				
Wealth management services:				
Trust and investment advisory fees	5,238	5,336	15,901	15,626
Mutual fund fees	1,383	1,386	4,169	4,000
Financial planning, commissions and other service fees	570	456	2,029	1,915
Wealth management services	7,191	7,178	22,099	21,541
Service charges on deposit accounts	1,215	1,214	3,583	3,559
Merchant processing fees	2,221	2,252	5,407	5,285
Income from bank-owned life insurance	452	376	1,352	1,166
Net gains on loan sales and commissions on loans originated for others	239	431	1,163	1,205
Net gains on securities	–	–	1,909	336
Losses on write-downs of investments to fair value	(982)	–	(2,989)	–
Other income	254	399	1,269	1,129
Total noninterest income	10,590	11,850	33,793	34,221
Noninterest expense:				
Salaries and employee benefits	10,580	10,098	31,334	30,195
Net occupancy	1,123	1,021	3,325	3,076
Equipment	956	871	2,877	2,564
Merchant processing costs	1,857	1,916	4,523	4,493
Outsourced services	700	556	2,078	1,610
Advertising and promotion	376	466	1,229	1,467

Legal, audit and professional fees	626	444	1,599	1,298
Amortization of intangibles	320	341	972	1,057
Debt prepayment penalties	–	–	–	1,067
Other expenses	1,933	1,599	5,730	5,354
Total noninterest expense	18,471	17,312	53,667	52,181
Income before income taxes	7,663	9,548	25,103	26,247
Income tax expense	1,623	2,992	7,152	8,234
Net income	$ 6,040	$ 6,556	$ 17,951	$ 18,013
Weighted average shares outstanding – basic	13,409.5	13,323.6	13,383.0	13,358.1
Weighted average shares outstanding – diluted	13,588.3	13,564.1	13,564.5	13,612.7
Per share information:				
Basic earnings per share	$ 0.45	$ 0.49	$ 1.34	$ 1.35
Diluted earnings per share	$ 0.44	$ 0.48	$ 1.32	$ 1.32
Cash dividends declared per share	$ 0.21	$ 0.20	$ 0.62	$ 0.60

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

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WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES (Dollars in thousands)

CONSOLIDATED STATEMENTS OF CASH FLOWS

		Unaudited	
Nine months ended September 30,		2008	2007
Cash flows from operating activities:			
Net income		$ 17,951	$ 18,013
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses		2,950	900
Depreciation of premises and equipment		2,275	2,209
(Gain) loss on disposal/sale of premises and equipment		(41)	23
Net amortization of premium and discount		692	466
Amortization of intangibles		972	1,057
Share-based compensation		407	427
Non-cash charitable contribution		–	520
Earnings from bank-owned life insurance		(1,352)	(1,166)
Net gains on loan sales		(1,163)	(1,205)
Net gains on securities		(1,909)	(336)
Losses on write-downs of investments to fair value		2,989	
Proceeds from sales of loans		47,396	47,313
Loans originated for sale		(45,747)	(46,496)
Decrease (increase) in accrued interest receivable, excluding purchased interest		644	(731)
Increase in other assets		(2,469)	(1,211)
(Decrease) increase in accrued expenses and other liabilities		(1,243)	533
Other, net		(6)	(3)
Net cash provided by operating activities		22,346	20,313
Cash flows from investing activities:			
Purchases of:	Mortgage-backed securities available for sale	(170,332)	(143,774)
	Other investment securities available for sale	(1,025)	(39,290)
	Other investment securities held to maturity	–	(12,882)
Proceeds from sale of:	Mortgage-backed securities available for sale	–	47,938
	Other investment securities available for sale	64,321	10,160
	Mortgage-backed securities held for sale	–	38,501
	Other investment securities held to maturity	–	21,698
Maturities and principal payments of:	Mortgage-backed securities available for sale	70,434	50,042
	Other investment securities available for sale	13,976	14,957
	Mortgage-backed securities held to maturity	–	3,191
	Other investment securities held to maturity	–	20,490
Purchase of Federal Home Loan Bank stock		(10,283)	–
Net increase in loans		(167,605)	(48,704)
Proceeds from sale of loans		18,047	–
Purchases of loans, including purchased interest		(46,324)	(5,841)
Proceeds from sale of premises and equipment, net of selling costs		1,433	–
Purchases of premises and equipment		(2,561)	(3,715)
Equity investment in capital trusts		(310)	–
Payment of deferred acquisition obligation		(8,065)	(6,720)
Net cash used in investing activities		(238,294)	(53,949)

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

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WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES (Dollars in thousands)
CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)

	Unaudited	
Nine months ended September 30,	2008	2007
Cash flows from financing activities:		
Net increase (decrease) in deposits	91,046	(22,110)
Net increase in other borrowings	305	22,518
Proceeds from Federal Home Loan Bank advances	795,421	532,463
Repayment of Federal Home Loan Bank advances	(664,387)	(504,729)
Purchases of treasury stock, including deferred compensation plan activity	43	(5,211)
Net proceeds from the issuance of common stock under dividend reinvestment plan	596	–
Net proceeds from the exercise of stock options and issuance of other equity instruments	179	989
Tax benefit from stock option exercises and issuance of other equity instruments	199	723
Proceeds from the issuance of junior subordinated debentures, net of debt issuance costs	10,016	–
Cash dividends paid	(8,174)	(7,904)
Net cash provided by financing activities	225,244	16,739
Net increase (decrease) in cash and cash equivalents	9,296	(16,897)
Cash and cash equivalents at beginning of period	41,112	71,909
Cash and cash equivalents at end of period	$ 50,408	$ 55,012
Noncash Investing and Financing Activities:		
Loans charged off	$ 818	$ 553
Increase to deferred acquisition obligation	5,638	5,921
Net transfers from loans to property acquired through foreclosure or repossession	113	–
Held to maturity securities transferred to available for sale	–	162,977
Supplemental Disclosures:		
Interest payments	56,034	56,792
Income tax payments	10,427	8,965

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

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WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES
CONDENSED NOTES TO UNAUDITED 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 offices in Rhode Island, Massachusetts and southeastern Connecticut, ATMs, and its Internet web site (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 period amounts have been reclassified to conform to the current period's 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 the review of goodwill, other intangible assets and investments 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 September 30, 2008 and December 31, 2007, 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 Bancorp, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2007.

(2) New Accounting Pronouncements
In September 2006, the Financial Accounting Standards Board ("FASB") issued SFAS No. 157, "Fair Value Measurements" ("SFAS No. 157"), which 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 adoption of SFAS No. 157 for financial assets and liabilities did not have a material impact on the Corporation's financial position or results of operations. The required disclosures about fair value measurements for financial assets and liabilities have been included in Note 10. In accordance with FASB Staff Position No. 157-2, "Effective Date of FASB Statement No. 157," the effective date of SFAS No. 157 as it applies to nonfinancial assets, such as goodwill, and nonfinancial liabilities has been delayed to January 1, 2009. The Corporation is currently evaluating the impact that the adoption of SFAS No. 157 for nonfinancial assets and liabilities will have on the Corporation's financial position and results of operations. On October 10, 2008, the FASB issued FASB Staff Position

No. 157-3, “Determining the Fair Value of a Financial Asset When the Market of That Asset Is Not Active,” to clarify the application of SFAS No. 157 in a market that is not active. FASB Staff Position No. 157-3 was effective upon issuance, including prior periods for which financial statements have not been issued. The Corporation complied with the guidance in FASB Staff Position No. 157-3 in determining the fair value of its securities at September 30, 2008.

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 requirement to measure the plan's assets and obligations as of the employer's fiscal year end was adopted effective January 1, 2008. The adoption of the measurement date provision of SFAS No. 158 did not have a material impact on the Corporation's financial position or results of operations. See further discussion in Note 11.

The SEC released Staff Accounting Bulletin ("SAB") No. 109 in November 2007. SAB No. 109 provides guidance on written loan commitments that are accounted for at fair value through earnings. SAB No. 109 supersedes SAB No. 105, which provided guidance on derivative loan commitments pursuant to SFAS No. 133, "Accounting for Derivative Instruments and Hedging Transactions" ("SFAS No 133"). SAB No. 105 stated that in measuring the fair value of a derivative loan commitment it would be inappropriate to incorporate the expected net future cash flows related to the associated loan. SAB No. 109, consistent with the guidance in SFAS No. 156 and SFAS No. 159, requires that expected net future cash flows related to the associated servicing of the loan be included in the measurement of all written loan commitments that are accounted for at fair value through earnings. The guidance in SAB No. 109 is applied on a prospective basis to derivative loan commitments issued or modified in fiscal quarters beginning after December 15, 2007. The adoption of SAB No. 109 did not have a material impact on the Corporation's financial position or results of operations.

The SEC released SAB No. 110 in December 2007. SAB No. 110 provides guidance on the use of a "simplified" method, as discussed in SAB No. 107, in developing an estimate of expected term of "plain vanilla" share options in accordance with SFAS No. 123 (revised 2004), "Share-Based Payment". SAB No. 107 did not expect a company to use the simplified method for share option grants after December 31, 2007. At the time SAB No. 107 was issued, the SEC believed that more detailed external information about employee exercise behavior (e.g., employee exercise patterns by industry and/or other categories of companies) would, over time, become readily available to companies. The SEC understands that such detailed information about employee exercise behavior may not be widely available by December 31, 2007. Accordingly, the SEC will continue to accept, under certain circumstances, the use of the simplified method beyond December 31, 2007. The adoption of SAB No. 110 did not have a material impact on the Corporation's financial position or results of operations.

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities" ("SFAS No. 161"). SFAS No. 161 changes the disclosure requirements for derivative instruments and hedging activities. Entities are required to provide enhanced disclosures about (1) how and why an entity uses derivative instruments, (2) how derivative instruments and related hedge items are accounted for under SFAS No. 133 and its related interpretations, and (3) how derivative instruments and related hedged items affect an entity's financial position, financial performance and cash flows. SFAS No. 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early adoption encouraged. SFAS No. 161 encourages but does not require comparative disclosures for earlier periods at initial adoption. The Corporation will provide the additional disclosures necessary upon the adoption of SFAS No. 161.

In May 2008, the FASB issued SFAS No. 162, "The Hierarchy of Generally Accepted Accounting Principles" ("SFAS No. 162"). SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with GAAP. The current GAAP hierarchy is set forth in the American Institute of Certified Public Accountants Statement on Auditing Standards No. 69, "The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles." The FASB has concluded that the GAAP hierarchy should reside in the accounting literature established by the FASB and issued SFAS No. 162 to achieve that result. SFAS No. 162 is effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to Interim Auditing Standards AU

Section 411, "The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles". The FASB does not expect that SFAS No. 162 will result in a change in current practice.

(3) Securities
Securities are summarized as follows:

(Dollars in thousands)

September 30, 2008	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities Available for Sale:				
U.S. Treasury obligations and obligations of U.S. government-sponsored agencies	$ 76,013	$ 1,949	$ –	$ 77,962
Mortgage-backed securities issued by U.S. government and government-sponsored agencies	568,495	2,385	(4,904)	565,976
States and political subdivisions	80,685	34	(4,091)	76,628
Trust preferred securities	37,985	–	(12,201)	25,784
Corporate bonds	1,748	–	(14)	1,734
Common stock	1,458	350	(36)	1,772
Perpetual preferred stocks	5,153	–	(1,553)	3,600
Total securities available for sale	$ 771,537	$ 4,718	$ (22,799)	$ 753,456

(Dollars in thousands)

December 31, 2007	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities Available for Sale:				
U.S. Treasury obligations and obligations of U.S. government-sponsored agencies	$ 136,721	$ 2,888	$ (10)	$ 139,599
Mortgage-backed securities issued by U.S. government and government-sponsored agencies	469,197	2,899	(2,708)	469,388
States and political subdivisions	80,634	499	(239)	80,894
Trust preferred securities	37,995	–	(3,541)	34,454
Corporate bonds	13,940	161	–	14,101
Common stocks	3,931	2,850	–	6,781
Perpetual preferred stocks	8,165	–	(1,604)	6,561
Total securities available for sale	$ 750,583	$ 9,297	$ (8,102)	$ 751,778

Securities available for sale with a fair value of $667.8 million and $592.7 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, 2008 and December 31, 2007, respectively. In addition, securities available for sale with a fair value of $7.4 million and $8.4 million were collateralized for the discount window at the Federal Reserve Bank at September 30, 2008 and December 31, 2007, respectively. There were no borrowings with the Federal Reserve Bank at either date. Securities available for sale with a fair value of $8.8 million and $1.9 million were designated in rabbi trusts for nonqualified retirement plans at September 30, 2008 and December 31, 2007, respectively. As of September 30, 2008 and December 31, 2007, securities available for sale with a fair value of $521 thousand and $532 thousand, respectively, were pledged as collateral to secure certain interest rate swap agreements.

During the nine months ended September 30, 2008, impairment charges of $3.0 million were recognized on equity security perpetual preferred stock holdings issued by FHLMC, FNMA and two other corporate issuers that were deemed to be other-than-temporarily impaired based on an analysis of the financial condition and operating outlook of the issuers. These charges were reported in losses on write-downs of investments to fair value in the Consolidated Statements of Income for the nine months ended September 30, 2008.

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

The following table summarizes temporarily impaired securities as of September 30, 2008, segregated by length of time the securities have been in a continuous unrealized loss position.

(Dollars in thousands)	Less than 12 Months			12 Months or Longer			Total		
At September 30, 2008	#	Fair Value	Unrealized Losses	#	Fair Value	Unrealized Losses	#	Fair Value	Unrealized Losses
Mortgage-backed securities issued by U.S. government and government-sponsored agencies	60	$ 254,991	$ 2,453	25	$ 62,950	$ 2,451	85	$ 317,941	$ 4,904
States and political subdivisions	90	64,702	3,273	8	8,836	818	98	73,538	4,091
Trust preferred securities	–	–	–	13	25,784	12,201	13	25,784	12,201
Corporate bonds	1	1,734	14	–	–	–	1	1,734	14
Subtotal, debt securities	151	321,427	5,740	46	97,570	15,470	197	418,997	21,210
Common stock	2	1,341	36	–	–	–	2	1,341	36
Perpetual preferred stock	1	1,000	710	6	2,511	843	7	3,511	1,553
Subtotal, equity securities	3	2,341	746	6	2,511	843	9	4,852	1,589
Total temporarily impaired securities	154	$ 323,768	$ 6,486	52	$ 100,081	$ 16,313	206	$ 423,849	$ 22,799

The following table summarizes temporarily impaired securities as of December 31, 2007, segregated by length of time the securities have been in a continuous unrealized loss position.

(Dollars in thousands)	Less than 12 Months			12 Months or Longer			Total		
At December 31, 2007	#	Fair Value	Unrealized Losses	#	Fair Value	Unrealized Losses	#	Fair Value	Unrealized Losses
U.S. Treasury obligations and obligations of U.S. government-sponsored agencies	1	$ 6,996	$ 1	1	$ 3,990	$ 9	2	$ 10,986	$ 10
Mortgage-backed securities issued by U.S. government and government-sponsored agencies	22	108,630	1,028	46	110,348	1,680	68	218,978	2,708
States and political subdivisions	13	12,402	128	10	7,681	111	23	20,083	239
Trust preferred securities	8	23,167	2,769	5	11,287	772	13	34,454	3,541
Subtotal, debt securities	44	151,195	3,926	62	133,306	2,572	106	284,501	6,498
Perpetual preferred stock	5	5,258	1,495	4	1,304	233	9	6,562	1,728
Total temporarily impaired securities	49	$ 156,453	$ 5,421	66	$ 134,610	$ 2,805	115	$ 291,063	$ 8,226

Unrealized losses on debt securities generally occur as a result of increases in interest rates since the time of purchase, a structural change in an investment or from deterioration in credit quality of the issuer. Management evaluates impairments in value whether caused by adverse interest rates or credit movements to determine if they are other-than-temporary.

In accordance with applicable accounting literature, Washington Trust must, in addition to other criteria, demonstrate an ability and intent to hold temporarily impaired securities until full recovery of their cost basis to classify such losses as temporary. Management uses both internal and external information sources to arrive at the most informed decision. This quantitative and qualitative assessment begins with a review of general market conditions and changes to market conditions, credit, investment performance and structure since the prior review period. The ability to hold temporarily impaired securities will involve a number of factors, including: forecasted recovery period based on average life and Washington Trust's capital, earnings and cash flow positions, among other things. Washington Trust currently intends to hold all temporarily impaired securities to full recovery of the cost basis, which may be until maturity.

Management assesses a variety of factors in determining if an impairment is other than temporary, including but not limited to, the likelihood of and probable time horizon for recovery of the cost basis, including analyst forecasts, earnings assumptions and other company specific or sector financial performance metrics.

Debt securities in an unrealized loss position at September 30, 2008 consisted of 197 debt security holdings. The majority of the loss for debt securities reported in an unrealized loss position at September 30, 2008 was concentrated in variable rate trust preferred securities issued by financial services companies and in U.S. agency or government-sponsored agency mortgage-backed securities.

Included in debt securities in an unrealized loss position at September 30, 2008 were 13 trust preferred security holdings. These holdings represent seven individual name issuers in the financial industry, including, where applicable, the impact of mergers and acquisitions of issuers subsequent to original purchase, and two pooled trust preferred securities in the form of collateralized debt obligations. The aggregate unrealized losses on the 13 trust preferred holdings amounted to $12.2 million, or 32% of amortized cost, as of September 30, 2008. Management believes the September 30, 2008 temporary impairment on trust preferred securities, including the pooled trust preferred holdings, was not a function of underlying credit issues associated with the issuers of the debt obligations and primarily reflected increased investor concerns beginning in the latter part of 2007 and continuing into 2008 about recent losses in the financial services industry related to sub-prime lending and sub-prime exposure. These concerns resulted in a substantial decrease in market liquidity and increased risk premiums for securities in this sector. Credit spreads for issuers in this sector widened substantially during recent months, causing prices for these securities holdings to decline. As recently as September 30, 2007, the aggregate unrealized loss position of the 13 trust preferred holdings was 6.3% of amortized cost and the aggregate unrealized loss position at December 31, 2007 was 9.3% of amortized cost for these holdings. The largest unrealized loss dollar amount of any single individual name issuer was $2.0 million, or 21% of its amortized cost, at September 30, 2008. As of September 30, 2008, the amortized cost and fair value of the two pooled trust preferred holdings was $7.5 million and $3.0 million, respectively. The pooled trust preferred holdings consist of trust preferred obligations of banking industry companies and, to a lesser extent, insurance industry companies. Valuations of the pooled trust preferred holdings are also dependent in part on cash flows from underlying issuers. Unexpected cash flow disruptions could have an adverse impact on the fair value and performance of these pooled trust preferred securities. For both of its pooled trust preferred holdings, Washington Trust's investment is senior to one or more subordinated tranches which have first loss exposure. As part of management's evaluation to determine if impairment is other-than-temporary, management prepared an analysis consistent with EITF 99-20, "Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests that Continue to Be Held by a Transferor in Securitized Assets", and concluded that there was no adverse change in cash flows on these two pooled trust preferred securities. All individual name trust preferred debt securities and the respective tranche of the pooled trust preferred securities held in our portfolio continue to accrue and make payments as expected, and all have credit ratings at or above investment grade minimums. Washington Trust has the ability and intent to hold these securities to full recovery of the cost basis and management does not consider these investments to be other-than-temporarily impaired at this time.

The unrealized losses on U.S. agency or government-sponsored agency mortgage-backed securities was concentrated in securities purchased during 2003 and 2004, during which time interest rates were at or near historical lows. The fair value for these and the state and municipal holdings included in this analysis have declined due to a combination of factors, including the relative increase in short and medium term interest rates since the time of purchase, decreased liquidity and rising risk premiums for credit-sensitive securities, and downgrades in credit ratings for municipal bond insurers. The largest unrealized loss percentage amount on any holding in these categories was 8.75% of its amortized cost at September 30, 2008. Management believes that the nature and duration of impairment on these debt security holdings are a function of changes in investment spreads and interest rate movements. Washington Trust has the ability and intent to hold these securities to full recovery of the cost basis and management does not consider these investments to be other-than-temporarily impaired.

The equity securities in an unrealized loss position at September 30, 2008 consisted of 9 holdings of financial and commercial entities with unrealized losses of $1.6 million, or 25% of their aggregate cost. During the nine months ended September 30, 2008, Washington Trust recorded $3.0 million in impairment charges on perpetual preferred stock holdings issued by FHLMC, FNMA and two other corporate issuers, based on an analysis of the financial condition and operating outlook of the issuers. As of September 30, 2008, the Corporation had 2 perpetual preferred stock holdings of FHLMC and FNMA with a total fair value and carrying value of $89 thousand and 7 perpetual preferred stock holdings of financial and utility companies with a total fair value of $3.5 million and unrealized losses of $1.6 million. In October 2008, the SEC's Office of the Chief Accountant, after consultation and concurrence with the FASB, concluded that the assessment of other-than-temporary impairment of perpetual preferred securities for third quarter filings made after October 14, 2008 can be made using an impairment model (including an anticipated recovery period) similar to a debt security provided there has been no evidence of a deterioration in credit of the issuer. Washington Trust complied with this guidance in it's evaluation of other-than-temporary impairment of perpetual preferred stocks. Causes of conditions whereby the fair value of 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. Management believes that a portion of the September 30, 2008 temporary impairment on its equity securities holdings was not a function of the financial condition and operating outlook of the issuers and reflected increased investor concerns beginning in the latter part of 2007 and continuing into 2008 about recent losses in the financial services industry related to sub-prime lending and sub-prime exposure. These concerns resulted in greater volatility in market prices for both common and preferred stocks in this market sector. Washington Trust has the ability and intent to hold these investments to full recovery of the cost basis and considers the unrealized losses on these equity securities to be temporary.

Further deterioration in credit quality of the companies backing the securities and/or a continuation of the current imbalances in liquidity that exist in the marketplace may further effect the fair value of these securities and increase the potential that certain unrealized losses be designated as other than temporary in future periods and the Corporation may incur additional write-downs.

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(4) Loan Portfolio
The following is a summary of loans:

(Dollars in thousands)	September 30, 2008		December 31, 2007	
	Amount	%	Amount	%
Commercial:				
Mortgages (1)	$ 394,085	22%	$ 278,821	18%
Construction and development (2)	51,592	3%	60,361	4%
Other (3)	396,161	23%	341,084	21%
Total commercial	841,838	48%	680,266	43%
Residential real estate:				
Mortgages (4)	604,205	34%	588,628	37%
Homeowner construction	14,124	1%	11,043	1%
Total residential real estate	618,329	35%	599,671	38%
Consumer:				
Home equity lines	158,837	9%	144,429	9%
Home equity loans	93,690	5%	99,827	6%
Other	56,347	3%	49,459	4%
Total consumer	308,874	17%	293,715	19%
Total loans (5)	$ 1,769,041	100%	$ 1,573,652	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 Federal Home Loan Bank borrowings (See Note 7 for additional discussion of Federal Home Loan Bank borrowings).
(5) Includes net deferred loan origination costs of $10 thousand and net discounts on purchased loans of $296 thousand at September 30, 2008, compared to net deferred fees of $100 thousand and net premiums on purchased loans of $297 thousand at December 31, 2007.

Nonaccrual Loans
The balance of loans on nonaccrual status as of September 30, 2008 was $6.7 million, compared to $4.3 million at December 31, 2007. The $2.4 million increase in nonaccrual loans was largely due to certain commercial loan relationships moving into the non-accruing loan classification.

(5) Allowance for Loan Losses
The following is an analysis of the allowance for loan losses:

(Dollars in thousands)

	Three months		Nine months	
Periods ended September 30,	2008	2007	2008	2007
Balance at beginning of period	$ 21,963	19,327	$ 20,277	$ 18,894
Provision charged to expense	1,100	300	2,950	900
Recoveries of loans previously charged off	60	27	222	231

Loans charged off	(492)	(182)	(818)	(553)
Balance at end of period	$ 22,631	$ 19,472	$ 22,631	$ 19,472

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WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES (Continued)
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(6) Goodwill and Other Intangibles
The changes in the carrying value of goodwill and other intangible assets for the nine months ended September 30, 2008 are as follows:

Goodwill

(Dollars in thousands)	Commercial Banking Segment	Wealth Management Service Segment	Total
Balance at December 31, 2007	$ 22,591	$ 27,888	$ 50,479
Additions to goodwill during the period	–	5,638	5,638
Impairment recognized	–	–	–
Balance at September 30, 2008	$ 22,591	$ 33,526	$ 56,117

The Stock Purchase Agreement for the August 2005 acquisition of Weston Financial Group, Inc. ("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. During the third quarter of 2008, the Corporation recognized a liability of $5.6 million, with a corresponding increase to goodwill, representing the amounts earned under the terms of the Stock Purchase Agreement.

Other Intangible Assets

(Dollars in thousands)	Core Deposit Intangible	Advisory Contracts	Non-compete Agreements	Total
Balance at December 31, 2007	$ 510	$ 10,743	$ 180	$ 11,433
Amortization	90	845	37	972
Balance at September 30, 2008	$ 420	$ 9,898	$ 143	$ 10,461

Amortization of intangible assets for the nine months ended September 30, 2008 totaled $972 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)

Estimated amortization expense:	Core Deposits	Advisory Contracts	Non-compete Agreements	Total
2008 (full year)	$ 120	$ 1,111	$ 49	$ 1,280
2009	120	1,040	49	1,209
2010	120	922	49	1,091
2011	120	768	33	921
2012	30	727	–	757

The components of intangible assets at September 30, 2008 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		2,577		3,759		1,004		7,340
Net amount	$	420	$	9,898	$	143	$	10,461

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(7) Borrowings

Federal Home Loan Bank Advances

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

(Dollars in thousands)	September 30, 2008	December 31, 2007
FHLB advances	$ 747,430	$ 616,417

In addition to outstanding advances, the Corporation also has access to an unused line of credit amounting to $8.0 million at September 30, 2008. 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, 2008. Included in the collateral were securities available for sale with a fair value of $524.7 million and $476.8 million that were specifically pledged to secure FHLB borrowings at September 30, 2008 and December 31, 2007, 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

Junior subordinated debentures are summarized as follows:

(Dollars in thousands)	September 30, 2008	December 31, 2007
Junior subordinated debentures	$ 32,991	$ 22,681

In April 2008, the Bancorp sponsored the creation of Washington Preferred Capital Trust ("Washington Preferred"). Washington Preferred is a Delaware statutory trust created for the sole purpose of issuing trust preferred securities and investing the proceeds in junior subordinated debentures of the Bancorp. The Bancorp is the owner of all of the common securities of Washington Preferred. In accordance with FASB Interpretation 46-R, "Consolidation of Variable Interest Entities—Revised", Washington Preferred will be treated as an unconsolidated subsidiary. The common stock investment in the statutory trust will be included in "Other Assets" in the Consolidated Balance Sheet.

On April 7, 2008, Washington Preferred issued $10 million of trust preferred securities ("Capital Securities") in a private placement to two institutional investors pursuant to an applicable exemption from registration. The Capital Securities mature in June 2038, are redeemable at the Bancorp's option beginning after five years, and require quarterly distributions by Washington Preferred to the holder of the Capital Securities, at a rate of 6.2275% until June 15, 2008, and resets quarterly thereafter at a rate equal to the three-month LIBOR rate plus 3.50%. The Bancorp has guaranteed the Capital Securities and, to the extent not paid by Washington Preferred, accrued and unpaid distributions on the Capital Securities, as well as the redemption price payable to the Capital Securities holders. The proceeds of the Capital Securities, along with the proceeds of $310 thousand from the issuance of common securities by Washington Preferred to the Bancorp, were used to purchase $10,310,000 of the Bancorp's junior subordinated deferrable interest notes (the "Washington Preferred Debentures") and constitute the primary asset of Washington Preferred. The Bancorp will use the proceeds from the sale of the Washington Preferred Debentures for general corporate purposes. Like the Capital Securities, the Washington Preferred Debentures bear interest at a rate of 6.2275% until June 15, 2008, and resets quarterly thereafter at a rate equal to the three-month LIBOR rate plus 3.50%. The Washington Preferred Debentures mature on June 15, 2038, but may be redeemed at par at the Bancorp's option, subject to the approval of the applicable banking regulator to the extent required under applicable guidelines or policies, at any time on or after June 15, 2013, or upon the occurrence of certain special qualifying events.

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WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES (Continued)
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Other Borrowings
The following is a summary of other borrowings:

(Dollars in thousands)	September 30, 2008	December 31, 2007
Treasury, Tax and Loan demand note balance	$ 2,972	$ 2,793
Deferred acquisition obligations	7,605	9,884
Securities sold under repurchase agreements	19,500	19,500
Other	362	383
Other borrowings	$ 30,439	$ 32,560

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 $7.6 million and $9.9 million at September 30, 2008 and December 31, 2007, respectively. During the third quarter of 2008, the Corporation recognized a liability of $5.6 million, representing the amounts earned under the terms of the Stock Purchase Agreement. In the first quarter of 2008 the Corporation paid approximately $8.1 million, which represented the 2007 earn-out payment.

(8) Shareholders' Equity
Stock Repurchase Plan:
The Corporation's 2006 Stock Repurchase Plan authorizes the repurchase of up to 400,000 shares of the Corporation's common stock in open market transactions. There were no shares repurchased under the Corporation's 2006 Stock Repurchase Plan during the nine months ended September 30, 2008. As of September 30, 2008, a cumulative total of 185,400 shares have been repurchased at a total cost of $4.8 million.

Pursuant to the Amended and Restated Nonqualified Deferred Compensation Plan ("Deferred Compensation Plan"), 3,423 shares were acquired during the nine months ended September 30, 2008.

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WASHINGTON TRUST BANCORP, INC. AND SUBSIDIARIES (Continued)
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Regulatory Capital Requirements:

The following table presents the Corporation's and the Bank's actual capital amounts and ratios at September 30, 2008 and December 31, 2007, as well as the corresponding minimum and well capitalized regulatory amounts and ratios:

(Dollars in thousands)	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of September 30, 2008:						
Total Capital (to Risk-Weighted Assets):						
Corporation	$ 187,468	10.45%	$ 143,477	8.00%	$ 179,346	10.00%
Bank	$ 193,878	10.82%	$ 143,350	8.00%	$ 179,188	10.00%
Tier 1 Capital (to Risk-Weighted Assets):						
Corporation	$ 165,043	9.20%	$ 71,738	4.00%	$ 107,608	6.00%
Bank	$ 171,473	9.57%	$ 71,675	4.00%	$ 107,513	6.00%
Tier 1 Capital (to Average Assets): (1)						
Corporation	$ 165,043	6.10%	$ 108,185	4.00%	$ 135,232	5.00%
Bank	$ 171,473	6.34%	$ 108,103	4.00%	$ 135,129	5.00%
As of December 31, 2007:						
Total Capital (to Risk-Weighted Assets):	$ 167,061	10.39%	$ 128,648	8.00%	$ 160,810	10.00%
Corporation	$ 174,750	10.87%	$ 128,574	8.00%	$ 160,717	10.00%
Bank						
Tier 1 Capital (to Risk-Weighted Assets):	$ 146,393	9.10%	$ 64,324	4.00%	$ 96,486	6.00%
Corporation	$ 154,093	9.59%	$ 64,287	4.00%	$ 96,430	6.00%
Bank						
Tier 1 Capital (to Average Assets): (1)	$ 146,393	6.09%	$ 96,088	4.00%	$ 120,110	5.00%
Corporation	$ 154,093	6.42%	$ 96,042	4.00%	$ 120,053	5.00%
Bank						

(1) Leverage ratio

As of September 30, 2008, Bancorp has sponsored the creation of three statutory trusts for the sole purpose of issuing trust preferred securities and investing the proceeds in junior subordinated debentures of the Bancorp. In accordance with FASB Interpretation 46-R, "Consolidation of Variable Interest Entities – Revised" ("FIN 46-R"), these statutory trusts created by Bancorp are not consolidated into the Corporation's financial statements; however, the Corporation reflects the amounts of junior subordinated debentures payable to the preferred shareholders of statutory trusts as debt in its financial statements. The trust preferred securities qualify as Tier 1 capital.

The Corporation's capital ratios at September 30, 2008 place the Corporation in the "well-capitalized" category according to regulatory standards. On March 1, 2005, the Federal Reserve Board issued a final rule that would retain trust preferred securities in Tier 1 capital of bank holding companies, but with stricter quantitative limits and clearer standards. Under the proposal, after a five-year transition period that would end on March 31, 2009, the aggregate amount of trust preferred securities would be limited to 25% of Tier 1 capital elements, net of goodwill. The Corporation has evaluated the potential impact of such a change on its Tier 1 capital ratio and has concluded that the regulatory capital treatment of the trust preferred securities in the Corporation's total capital ratio would be unchanged.

On October 2, 2008, Washington Trust announced that it had issued 2.5 million shares in a private placement of its common stock with net proceeds of approximately $47 million. See Note 17 for additional disclosure on the capital issuance.

(9) 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, interest rate swap agreements 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:

(Dollars in thousands)	September 30, 2008	December 31, 2007
Financial instruments whose contract amounts represent credit risk:		
Commitments to extend credit:		
Commercial loans	$ 166,531	$ 149,465
Home equity lines	178,652	176,284
Other loans	27,580	20,770
Standby letters of credit	7,656	8,048
Financial instruments whose notional amounts exceed the amount of credit risk:		
Forward loan commitments:		
Commitments to originate fixed rate mortgage loans to be sold	3,299	3,495
Commitments to sell fixed rate mortgage loans	4,372	5,472
Customer related derivative contracts:		
Interest rate swaps with customers	14,048	3,850
Mirror swaps with counterparties	14,048	3,850
Interest rate risk management contract:		
Interest rate swap	10,000	–

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, 2008 and December 31, 2007, the maximum potential amount of undiscounted future payments, not reduced by amounts that may be recovered, totaled $7.7 million and $8.0 million, respectively. At September 30, 2008 and December 31, 2007, 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, 2008 and 2007 was insignificant.

At September 30, 2008, 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.

Interest Rate Risk Management Agreements

Interest rate swaps are used from time to time as part of the Corporation's interest rate risk management strategy. Swaps are agreements in which the Corporation and another party agree to exchange interest payments (e.g., fixed-rate for variable-rate payments) computed on a notional principal amount. The credit risk associated with swap transactions is the risk of default by the counterparty. To minimize this risk, the Corporation enters into interest rate agreements only with highly rated counterparties that management believes to be creditworthy. The notional amounts of these agreements do not represent amounts exchanged by the parties and, thus, are not a measure of the potential loss exposure.

In April 2008, the Bancorp entered into an interest rate swap contract with a notional amount of $10 million to hedge the interest rate risk associated with $10 million of the variable rate junior subordinated debentures. See additional disclosure in Note 7. The interest rate swap contract matures in 2013. At inception, the swap was intended to convert the debt from variable rate to fixed rate and qualify for cash flow hedge accounting under SFAS No. 133. In September 2008, the hedging relationship was no longer highly effective due to changes in the creditworthiness of the counterparty to the derivative. As a result, cash flow hedge accounting has been discontinued prospectively. The fair value of this interest rate swap contract amounted to $43 thousand at September 30, 2008 and was reported in other assets on the consolidated balance sheet. The net gain on the swap recorded in accumulated other comprehensive income/loss, net of taxes as of the date of discontinuance amounted to $30 thousand. This amount will be subsequently reclassified into interest expense as a yield adjustment in the same period in which the related interest on the variable rate debentures affect earnings. All subsequent changes in fair value of the interest rate swap will be recognized directly in earnings as interest expense.

The Corporation has entered into interest rate swap contracts to help commercial loan borrowers manage their interest rate risk. The interest rate swap contracts with commercial loan borrowers allow them to convert floating rate loan payments to fixed rate loan payments. When we enter into an interest rate swap contract with a commercial loan borrower, we simultaneously enter into a “mirror” swap contract with a third party. The third party exchanges the client’s fixed rate loan payments for floating rate loan payments. We retain the risk that is associated with the potential failure of counterparties and inherent in making loans.

At September 30, 2008 and December 31, 2007, Washington Trust had interest rate swap contracts with commercial loan borrowers with notional amounts of $14.0 million and $3.850 million, respectively, and equal amounts of “mirror” swap contracts with third-party financial institutions. These interest rate swap contracts are carried at fair value with changes recorded as a component of other noninterest income. The fair values of the interest rate swap contracts with commercial loan borrowers amounted to $147 thousand as of September 30, 2008 and $60 thousand as of December 31, 2007. The fair values of the “mirror” swap contracts with third-party financial institutions totaled $153 thousand as of September 30, 2008 and $60 thousand as of December 31, 2007. For the nine months ended September 30, 2008, other noninterest income included net gains on customer related interest rate swap contracts of $121 thousand. Washington Trust did not engage in such interest rate swap contracts during the nine months ended September 30, 2007.

Forward Loan Commitments

Interest rate lock commitments are extended to borrowers that relate to the origination of readily marketable mortgage loans held for sale. To mitigate the interest rate risk inherent in these rate locks, as well as closed mortgage loans held for sale, best efforts forward commitments are established to sell individual mortgage loans. 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 and other liabilities on the consolidated balance sheet and the changes in fair value of such commitments are recorded in current earnings in the consolidated income statement. The carrying value of such commitments as of September 30, 2008 and December 31, 2007 and the respective changes in fair values for the nine months ended September 30, 2008 and 2007 were insignificant.

(10) Fair Value Measurements

Effective January 1, 2008, the Corporation adopted SFAS No. 157 for financial assets and liabilities. The effective date of SFAS No. 157, as it applies to nonfinancial assets and liabilities, has been delayed to January 1, 2009. SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosure requirements about fair value measurements. SFAS No. 157, among other things, emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and states that a fair value measurement should be determined based on the assumptions the market participants would use in pricing the asset or liability. In addition, SFAS No. 157 specifies a hierarchy of valuation techniques based on whether the types of valuation information (“inputs”) are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Corporation's market assumptions. These two types of inputs have created the following fair value hierarchy:

- Level 1 – Quoted prices for identical assets or liabilities in active markets.
- Level 2 – Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets.

- Level 3 – Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable in the markets and which reflect the Corporation's market assumptions.

The Corporation uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Securities available for sale and derivatives are recorded at fair value on a recurring basis. Additionally, from time to time, we may be required to record at fair value other assets on a nonrecurring basis, such as loans held for sale, collateral dependent impaired loans and mortgage servicing rights. These nonrecurring fair value adjustments typically involve the application of lower-of-cost-or-market accounting or write-downs of individual assets.

FASB Staff Position No. 157-3 "Determining the Fair Value of a Financial Asset When the Market for That Assets is Not Active" was issued on October 10, 2008 to clarify the application of SFAS No. 157 in a market that is not active. FASB Staff Position No. 157-3 was effective upon issuance, including prior periods for which financial statements have not been issued. The Corporation complied with the guidance in FASB Staff Position No. 157-3 in determining the fair value of its securities at September 30, 2008.

Determination of Fair Value
Under SFAS No. 157, fair values are based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When available, the Corporation uses quoted market prices to determine fair value. If quoted prices are not available, fair value is based upon valuation techniques such as matrix pricing or other models that use, where possible, current market-based or independently sourced market parameters, such as interest rates. If observable market-based inputs are not available, the Corporation uses unobservable inputs to determine appropriate valuation adjustments using methodologies applied consistently over time.

The following is a description of valuation methodologies for assets and liabilities recorded at fair value, including the general classification of such assets and liabilities pursuant to the valuation hierarchy.

Securities Available for Sale
Securities available for sale are recorded at fair value on a recurring basis. When available, the Corporation uses quoted market prices to determine the fair value of securities; such items are classified as Level 1. This category includes exchange-traded equity securities and U.S. Treasury obligations.

Level 2 securities include debt securities with quoted prices, which are traded less frequently than exchange-traded instruments, whose value is determined using matrix pricing with inputs that are observable in the market or can be derived principally from or corroborated by observable market data. This category generally includes obligations of U.S. government-sponsored agencies, mortgage-backed securities issued by U.S. government and government-sponsored agencies, municipal bonds, trust preferred securities, corporate bonds and certain preferred equity securities.

In certain cases where there is limited activity or less transparency around inputs to the valuation, securities may be classified as Level 3. As of September 30, 2008, Level 3 securities were comprised of two trust preferred CDO holdings, which were not actively traded. To determine their fair value, Washington Trust utilized third party pricing models and discounted cash flow methodologies. Their fair values were reviewed against similar securities that were more actively traded in order to assess the reasonableness of the fair values. Our fair values assumed liquidation in an orderly market and not under distressed circumstances. Due to the continued market illiquidity and credit risk for securities in the financial sector, the fair value of these securities is highly sensitive to assumption changes and market volatility.

Mortgage Loans Held for Sale

Mortgage loans held for sale are carried on an aggregate basis at the lower of cost or market value. The fair value of loans held for sale is based on what secondary markets are currently offering for loans with similar characteristics. As such, we classify loans subjected to nonrecurring fair value adjustments as Level 2.

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

Derivatives

Substantially all of our derivatives are traded in over-the-counter markets where quoted market prices are not readily available. Fair value measurements are determined using independent pricing models that utilize primarily market observable inputs, such as swap rates of different maturities and LIBOR rates, and, accordingly, are classified as Level 2. Examples include interest rate swap contracts. Any derivative for which we measure fair value using significant assumptions that are unobservable are classified as Level 3. Level 3 derivatives include interest rate lock commitments written for our residential mortgage loans that we intend to sell.

Collateral Dependent Impaired Loans

Collateral dependent loans that are deemed to be impaired in accordance with SFAS No. 114, “Accounting by Creditors for Impairment of a Loan,” are valued based upon the fair value of the underlying collateral. The inputs used in the appraisals of the collateral are observable, and, therefore, the loans are categorized as Level 2.

Mortgage Servicing Rights

Mortgage servicing rights do not trade in an active market with readily observable prices. Accordingly, we determine the fair value of mortgage servicing rights using a valuation model that calculates the present value of the estimated future net servicing income. The model incorporates assumptions used in estimating future net servicing income, including estimates of prepayment speeds, discount rate, cost to service and contractual servicing fee income. Mortgage servicing rights are subject to fair value measurements on a nonrecurring basis. Fair value measurements of our mortgage servicing rights use significant unobservable inputs and, accordingly, are classified as Level 3.

Items Recorded at Fair Value on a Recurring Basis

The table below presents the balances of assets and liabilities reported at fair value on a recurring basis.

(Dollars in thousands)	Fair Value Measurements Using			Assets/ Liabilities at Fair Value
September 30, 2008	Level 1	Level 2	Level 3	
Assets:				
Securities available for sale	$ 4,879	$ 745,585	$ 2,992	$ 753,456
Derivative assets (1)	–	246	21	267
Total assets at fair value on a recurring basis	$ 4,879	$ 745,831	$ 3,013	$ 753,723
Liabilities:				
Derivative liabilities (1)	$ –	$ 209	$ 24	$ 233
Total liabilities at fair value on a recurring basis	$ –	$ 209	$ 24	$ 233

(1) Derivatives assets are included in other assets and derivative liabilities are reported in accrued expenses and other liabilities in the Consolidated Balance Sheets.

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

The following table presents the changes in Level 3 assets and liabilities measured at fair value on a recurring basis in the nine month period ended September 30, 2008.

(Dollars in thousands)	Securities Available for Sale	Derivative Assets / (Liabilities)	Total
Balance at January 1, 2008	$ –	$ (4)	$ (4)
Gains and losses (realized and unrealized):			
Included in earnings	–	(2)	(2)
Included in other comprehensive income	(2,734)	–	(2,734)
Purchases, issuances and settlements (net)	(9)	3	(6)
Transfers in and/or out of Level 3	5,735	–	5,735
Balance at September 30, 2008	$ 2,992	$ (3)	$ 2,989

The losses included in earnings for Level 3 derivative assets and liabilities, which were comprised of interest rate lock commitments written for our residential mortgage loans that we intend to sell, were included in net gains on loan sales and commissions on loans originated for others in the Consolidated Statements of Income.

Items Recorded at Fair Value on a Nonrecurring Basis
Certain assets are measured at fair value on a nonrecurring basis in accordance with GAAP. These adjustments to fair value usually result from the application of lower of cost or market accounting or write-downs of individual assets. The valuation methodologies used to measure these fair value adjustments are described above. The following table presents the carrying value of certain assets measured at fair value on a nonrecurring basis during the nine months ended September 30, 2008.

(Dollars in thousands)	Carrying Value at September 30, 2008			
	Level 1	Level 2	Level 3	Total
Assets:				
Collateral dependent impaired loans	$ –	$ 1,519	$ –	$ 1,519
Total assets at fair value on a nonrecurring basis	$ –	$ 1,519	$ –	$ 1,519

The total nonrecurring fair value adjustments included in the Consolidated Statement of Income for the nine months ended September 30, 2008 were immaterial.

(11) Defined Benefit Pension Plans
Effective January 1, 2008, the Corporation adopted the measurement date provisions of SFAS No. 158 "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R)" ("SFAS No. 158"). As a result, the Corporation recognized the following adjustments in individual line items of its Consolidated Balance Sheet as of January 1, 2008:

(Dollars in thousands)	Prior to Adoption of Measurement Date Provisions of SFAS No. 158	Effect of Adopting Measurement Date Provisions of SFAS No. 158	As of January 1, 2008
Net deferred tax asset	$ 7,705	$ 229	$ 7,934
Defined benefit pension liabilities	11,801	655	12,456
Retained earnings	154,647	(468)	154,179

Accumulated other comprehensive loss	(239)	42	(197)

The adoption of the measurement date provisions of SFAS No. 158 had no effect on the Corporation's Consolidated Statements of Income or Cash Flows for the nine months ended September 30, 2008.

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

The following table sets forth the plans' benefit obligations, fair value of plan assets and funded status as of September 30, 2008 and 2007.

Components of Net Periodic Benefit Costs:

(Dollars in thousands)	Qualified Pension Plan		Non-Qualified Retirement Plans	
Three months ended September 30,	2008	2007	2008	2007
Service cost	$ 512	$ 503	$ 63	$ 87
Interest cost	506	462	142	129
Expected return on plan assets	(569)	(496)	-	-
Amortization of transition asset	–	(1)	-	-
Amortization of prior service cost	(8)	(8)	16	16
Recognized net actuarial loss	3	46	54	54
Net periodic benefit cost	$ 444	$ 506	$ 275	$ 286

(Dollars in thousands)	Qualified Pension Plan		Non-Qualified Retirement Plans	
Nine months ended September 30,	2008	2007	2008	2007
Service cost	$ 1,535	$ 1,508	$ 188	$ 259
Interest cost	1,520	1,386	428	389
Expected return on plan assets	(1,707)	(1,488)	-	-
Amortization of transition asset	–	(4)	-	-
Amortization of prior service cost	(25)	(25)	47	47
Recognized net actuarial loss	10	140	163	163
Net periodic benefit cost	$ 1,333	$ 1,517	$ 826	$ 858

Employer Contributions:
The Corporation previously disclosed in its financial statements for the year ended December 31, 2007 that it expected to contribute $2.0 million to its qualified pension plan and $421 thousand in benefit payments to its non-qualified retirement plans in 2008. During the nine months ended September 30, 2008, $2.0 million of contributions have been made to the qualified pension plan and $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 2008.

(12) Share-Based Compensation Arrangement
Washington Trust has three share-based compensation plans, Bancorp's 2003 Stock Incentive Plan, as amended (the "2003 Plan"), Bancorp's 1997 Equity Incentive Plan, as amended (the "1997 Plan") and the Amended and Restated 1988 Stock Option Plan (the "1988 Plan"), collectively the plans.

Amounts recognized in the consolidated financial statements with respect to the plans are as follows:

(Dollars in thousands)	Three months		Nine months	
Periods ended September 30,	2008	2007	2008	2007
Share-based compensation expense	$ 221	$ 104	$ 407	$ 427

Related tax benefit	$ 77	$ 36	$ 142	$ 149

During the three and nine months ended September 30, 2008, the Corporation granted 3,300 and 90,800 non-qualified share options, respectively, to certain key employees. The share options awarded were granted with three-year cliff vesting and also provide for accelerated vesting if there is a change in control, death or retirement (as defined in the plans).

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

The fair value of the share option awards granted were estimated on the date of grant using the Black-Scholes Option-Pricing Model based on assumptions noted in the following table. Washington Trust uses historical data to estimate share option exercise and employee departure behavior used in the option-pricing model; groups of employees that have similar historical behavior are considered separately for valuation purposes. The expected term of options granted was derived from the output of the option valuation model and represents the period of time that options granted are expected to be outstanding. Expected volatility was based on historical volatility of Washington Trust shares. The risk-free rate for periods within the contractual life of the share option was based on the U.S. Treasury yield curve in effect at the date of grant.

Nine months ended September 30,	2008
Expected term (years)	9.0
Expected dividend yield	2.86%
Weighted average expected volatility	33.62
Expected forfeiture rate	–
Weighted average risk-free interest rate	4.55%

The weighted average grant-date fair value of the share options awarded during the nine months ended September 30, 2008 was $8.05. There were no share options awarded during the nine months ended September 30, 2007.

A summary of share option activity under the plans as of September 30, 2008, and changes during the nine months ended September 30, 2008, 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, 2008	955,485	$	21.21			
Granted	90,800		24.05			
Exercised	56,700		17.95			
Forfeited or expired	5,550		27.87			
Outstanding at September 30, 2008	984,035	$	21.62	4.7 years	$	5,155
Exercisable at September 30, 2008	893,235	$	21.37	4.2 years	$	4,924
Options expected to vest as of September 30, 2008	90,800	$	24.05	9.7 years	$	231

The total intrinsic value (which is the amount by which the fair value of the underlying stock exceeds the exercise price of an option on the exercise date) of share options exercised during the nine months ended September 30, 2008 and 2007 was $430 thousand and $1.3 million, respectively.

During the nine months ended September 30, 2008, the Corporation granted 33,200 nonvested share units to directors and certain key employees. The nonvested share units awarded were granted with three-year cliff vesting and also provide for accelerated vesting if there is a change in control, death or retirement (as defined in the plans).

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A summary of the status of Washington Trust's nonvested shares as of September 30, 2008, and changes during the nine months ended September 30, 2008, is presented below:

	Number of Shares		Weighted Average Grant Date Fair Value
Nonvested at January 1, 2008	39,350	$	26.52
Granted	33,200		24.14
Vested	(16,200)		26.40
Forfeited	–		–
Nonvested at September 30, 2008	56,350	$	25.15

During the second quarter of 2008, performance share awards were granted providing certain executives the opportunity to earn shares of common stock of the Corporation, the number of which will be determined pursuant to, and subject to the attainment of, performance goals during a specified measurement period. The number of shares to be earned ranges from zero to 24,186 shares, subject to the attainment of specified performance goals discussed below.

The performance share awards were granted at $24.12, which was the fair market value at the date of grant with vesting ranging from two to three years. The number of shares awarded will range from zero to 200% of the target number of shares (13,093 shares) dependent upon the Corporation's core return on equity and core earnings per share growth ranking at the end of the vesting term. The current assumption based on the most recent peer group information results in the shares vesting at 140% of the target, or 16,930 shares. The Corporation has recognized compensation expense based on this assumption and will make the necessary adjustments each time the percentage of the target shares is adjusted. If the goals are not met, no compensation cost will be recognized and any recognized compensation costs will be reversed. The performance share awards provide for accelerated vesting if there is a change in control, death, disability or retirement (as defined in the plans).

A summary of the status of Washington Trust's performance share awards as of September 30, 2008, and changes during the nine months ended September 30, 2008, is presented below:

	Number of Shares		Weighted Average Grant Date Fair Value
Performance shares at January 1, 2008	–	$	–
Granted	16,930		24.12
Vested	–		–
Forfeited	–		–
Performance shares at September 30, 2008	16,930	$	24.12

As of September 30, 2008, there was $2.1 million of total unrecognized compensation cost related to nonvested share-based compensation arrangements (including share options, nonvested share awards and performance share awards) granted under the plans. That cost is expected to be recognized over a weighted average period of 2.6 years.

(13) 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.

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

(Dollars in thousands)

	Commercial Banking		Wealth Management Services		Corporate		Consolidated Total	
Three months ended September 30,	2008	2007	2008	2007	2008	2007	2008	2007
Net interest income	$ 15,875	$ 13,797	$ (13)	$ (18)	$ 782	$ 1,531	$ 16,644	$ 15,310
Noninterest income	4,053	4,295	7,191	7,178	(654)	377	10,590	11,850
Total income	19,928	18,092	7,178	7,160	128	1,908	27,234	27,160
Provision for loan losses	1,100	300	–	–	–	–	1,100	300
Depreciation and amortization expense	635	618	409	423	46	45	1,090	1,086
Other noninterest expenses	10,637	10,076	4,707	4,420	2,037	1,730	17,381	16,226
Total noninterest expenses	12,372	10,994	5,116	4,843	2,083	1,775	19,571	17,612
Income before income taxes	7,556	7,098	2,062	2,317	(1,955)	133	7,663	9,548
Income tax expense (benefit)	2,647	2,495	807	898	(1,831)	(401)	1,623	2,992
Net income (loss)	$ 4,909	$ 4,603	$ 1,255	$ 1,419	$ (124)	$ 534	$ 6,040	$ 6,556
Total assets at period end	1,835,842	1,587,328	50,108	44,254	881,932	800,180	2,767,882	2,431,762
Expenditures for long-lived assets	1,170	123	106	38	30	81	1,306	242

(Dollars in thousands)

	Commercial Banking		Wealth Management Services		Corporate		Consolidated Total	
Nine months ended September 30,	2008	2007	2008	2007	2008	2007	2008	2007
Net interest income	$ 45,849	40,411	$ (27)	$ (46)	$ 2,105	4,742	$ 47,927	$ 45,107
Noninterest income	11,341	11,058	22,099	21,541	353	1,622	33,793	34,221
Total income	57,190	51,469	22,072	21,495	2,458	6,364	81,720	79,328
Provision for loan losses	2,950	900	–	–	–	–	2,950	900
Depreciation and	1,880	1,841	1,232	1,292	135	133	3,247	3,266

amortization expense								
Other noninterest expenses	30,352	28,363	14,085	13,332	5,983	7,220	50,420	48,915
Total noninterest expenses	35,182	31,104	15,317	14,624	6,118	7,353	56,617	53,081
Income before income taxes	22,008	20,365	6,755	6,871	(3,660)	(989)	25,103	26,247
Income tax expense (benefit)	7,720	7,158	2,623	2,661	(3,191)	(1,585)	7,152	8,234
Net income (loss)	$ 14,288	$ 13,207	$ 4,132	$ 4,210	$ (469)	$ 596	$ 17,951	$ 18,013
Total assets at period end	1,835,842	1,587,328	50,108	44,254	881,932	800,180	2,767,882	2,431,762
Expenditures for long-lived assets	2,182	3,326	253	200	126	189	2,561	3,715

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

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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.

Included in the Corporate column in the tables above was an income tax benefit of $841 thousand which was recognized in the third quarter of 2008 based on an increase in net deferred tax assets resulting from a change in a state corporate income tax rate and calculation method enacted during the quarter.

(14) Comprehensive Income

(Dollars in thousands)

Three months ended September 30,	2008	2007
Net income	$ 6,040	$ 6,556
Unrealized holding (losses) gains on securities available for sale, net of income tax benefit of $3,216 in 2008 and income tax expense of $1,320 in 2007	(5,973)	2,452
Unrealized losses on cash flow hedge derivative instruments, net of income tax benefit of $103 in 2008	(190)	–
Less reclassification adjustments:		
Losses on securities, net of income tax benefit of $343 in 2008	638	–
Cash flow hedge derivative instruments, net of income tax expense of $6	11	–
Net periodic pension cost, net of income tax expense of $23 in 2008 and $37 in 2007	42	70
Total comprehensive income	$ 568	$ 9,078

(Dollars in thousands)

Nine months ended September 30,	2008	2007
Net income	$ 17,951	$ 18,013
Unrealized holding losses on securities available for sale, net of income tax benefit of $7,124 in 2008 and $1,127 in 2007	(13,232)	(2,093)
Unrealized gains on cash flow hedge derivative instruments, net of income tax expense of $4 in 2008	8	–
Less reclassification adjustments:		
Losses (gains) on securities, net of income tax benefit of $378 in 2008 and income tax expense of $148 in 2007	702	(188)
Cash flow hedge derivative instruments, net of income tax expense of $12	22	–
Net periodic pension cost, net of income tax expense of $68 in 2008 and $112 in 2007	127	209

Total comprehensive income	$ 5,578	$ 15,941

(15) 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, nonvested 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)

	Three Months		Nine Months	
Periods ended September 30,	2008	2007	2008	2007
Net income	$ 6,040	$ 6,556	$ 17,951	$ 18,013
Weighted average basic shares	13,409.5	13,323.6	13,383.0	13,358.1
Dilutive effect of:				
Options	134.0	190.2	141.3	211.1
Other	44.8	50.3	40.2	43.5
Weighted average diluted shares	13,588.3	13,564.1	13,564.5	13,612.7
Earnings per share:				
Basic	$ 0.45	$ 0.49	$ 1.34	$ 1.35
Diluted	$ 0.44	$ 0.48	$ 1.32	$ 1.32

(16) 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.

(17) Subsequent Events

On October 2, 2008, the Corporation announced that it had entered into a purchase agreement with select institutional investors pursuant to which it raised $50 million in a private placement of its own common stock. Net proceeds were approximately $47 million after deducting offering-related fees and expenses. The closing took place on October 7, 2008. The Corporation issued a total of 2.5 million shares of common stock at a price of $20 per share in the private placement. On October 20, 2008, the Corporation filed a registration statement with the SEC to register these shares for resale. Washington Trust intends to use the net proceeds from the capital raise for general corporate purposes and to support strategic growth initiatives in its commercial and wealth management business lines.

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

Forward-Looking Statements

This report contains statements that are "forward-looking statements." We may also make written or oral forward-looking statements in other documents we file with the SEC, in our annual reports to shareholders, in press releases and other written materials, and in oral statements made by our officers, directors or employees. You can identify forward-looking statements by the use of the words "believe," "expect," "anticipate," "intend," "estimate," "assu "outlook," "will," "should," and other expressions that predict or indicate future events and trends and which do not relate to historical matters. You should not rely on forward-looking statements, because they involve known and unknown risks, uncertainties and other factors, some of which are beyond the control of the Corporation. These risks, uncertainties and other factors may cause the actual results, performance or achievements of the Corporation to be materially different from the anticipated future results, performance or achievements expressed or implied by the forward-looking statements.

Some of the factors that might cause these differences include the following: changes in general national, regional or international economic conditions or conditions affecting the banking or financial services industries or financial capital markets, volatility and disruption in national and international financial markets, government intervention in the U.S. financial system, reductions in net interest income resulting from interest rate volatility as well as changes in the balance and mix of loans and deposits, reductions in the market value of wealth management assets under administration, changes in the value of securities and other assets, reductions in loan demand, changes in loan collectibility, 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. In addition, the factors described under "Risk Factors" in Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2007, as filed with the SEC, may result in these differences. You should carefully review all of these factors, and you should be aware that there may be other factors that could cause these differences. These forward-looking statements were based on information, plans and estimates at the date of this report, and we assume no obligation to update any forward-looking statements to reflect changes in underlying assumptions or factors, new information, future events or other changes.

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. As disclosed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2007, we have identified the allowance for loan losses, accounting for acquisitions and review of goodwill and intangible assets for impairment, and other-than-temporary impairment of investment securities 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

On October 2, 2008, the Corporation announced that it had issued 2.5 million shares in a private placement of its own common stock with net proceeds of approximately $47 million after deducting offering-related fees and expenses. Washington Trust intends to use the net proceeds from the capital raise for general corporate purposes and to support strategic growth initiatives in its commercial and wealth management business lines. See Note 17 to the Consolidated Financial Statements for additional information.

Overview

Net income for the third quarter of 2008 amounted to $6.0 million, or 44 cents per diluted share; compared to $6.6 million, or 48 cents per diluted share, reported for the third quarter a year ago. The returns on average equity and average assets for the third quarter of 2008 were 12.94% and 0.88%, respectively, compared to 14.99% and 1.10%, respectively, for the same period in 2007.

Net income for the nine months ended September 30, 2008 amounted to $18.0 million, or $1.32 per diluted share, substantially the same as the amounts reported for the same period in 2007. The returns on average equity and average assets for the first nine months of 2008 were 12.68% and 0.90%, respectively, compared to 13.74% and 1.01%, respectively, for the same period in 2007.

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The loan loss provision charged to earnings amounted to $1.1 million and $2.95 million for the three and nine months ended September 30, 2008, respectively, compared to $300 thousand and $900 thousand for the same periods in 2007. The higher loan loss provision was due largely to growth in the loan portfolio as well as an ongoing evaluation of credit quality and general economic conditions.

Losses on write-downs of investments to fair value of $982 thousand ($669 thousand after tax; 5 cents per diluted share) were charged to earnings in the third quarter of 2008 on FHLMC and FNMA perpetual preferred stock holdings deemed to be other-than-temporarily impaired. There were no securities gains or losses recognized in the third quarter of 2007. During the nine months ended September 30, 2008, other-than-temporary impairment charges of $3.0 million ($2.0 million after tax; 15 cents per diluted share) have been recognized on equity security perpetual preferred stock holdings issued by FHLMC, FNMA and two other corporate issuers. Included in net gains on securities in the nine months ended September 30, 2008 were realized gains of $232 thousand on the sale of commercial debt securities and realized gains of $1.7 million on the sale of other equity securities. For the nine months ended September 30, 2007, net gains on securities totaled $336 thousand.

An income tax benefit of $841 thousand, or 6 cents per diluted share, was recognized in the third quarter of 2008 based on an increase in net deferred tax assets resulting from a change in state corporate income tax rate and calculation method enacted during the quarter.

Net interest income for the third quarter and first nine months of 2008 increased by 9% and 6%, respectively, from the same periods in 2007 reflecting higher earning-asset levels and lower deposit costs.

Our primary source of noninterest income is revenue from wealth management services. Wealth management revenues for the third quarter of 2008 were essentially flat with the same quarter a year ago. On a year to date basis, wealth management revenues increased by 3% from 2007. These revenues are dependent to a large extent on the value of assets under administration. Wealth management assets under administration have been affected by lower valuations in the financial markets and declined by $299.1 million, or 8%, in the third quarter of 2008 to $3.6 billion at September 30, 2008. Assets under administration were down by 10% from December 31, 2007 and down by 10% from September 30, 2007.

Noninterest expenses for the third quarter and first nine months of 2008 were up 7% and 3%, respectively, from the same periods in 2007. Included in 2007 results were $1.1 million in debt prepayment charges, recorded in noninterest expense in the first quarter of 2007 as a result of prepayments of higher cost FHLB advances. There have been no debt prepayment penalty charges recognized in 2008.

Results of Operations

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 and first nine months of 2008 increased $1.3 million and $2.8 million, respectively, from the same periods a year earlier. Included in net interest income in first quarter of 2007 was an interest recovery of $322 thousand received on a previously charged-off loan.

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.

FTE net interest income for the third quarter and first nine months of 2008 increased 8% and 6%, respectively, from the same periods in 2007. The net interest margin (FTE net interest income as a percentage of average interest–earnings assets) for the third quarter of 2008 was 2.62%, down 19 basis points from the same quarter a year earlier. The net interest margin for the first nine months of 2008 was 2.64%, down 15 basis points from the same period in 2007. Excluding the 3 basis points attributable to the 2007 interest recovery, the net interest margin for the first nine months of

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2008 declined 12 basis points from the same period a year earlier. The decline in the net interest margin reflects decreases in yields on variable rate commercial and consumer loans resulting from actions taken by the Federal Reserve to reduce short-term interest rates, with less commensurate reduction in deposit rates paid during the same period.

Average interest-earning assets for the three and nine months ended September 30, 2008 increased $365.7 million and $272.0 million, respectively, from the same periods a year earlier. This increase was largely due to growth in the loan portfolio. Total average loans for the three and nine months ended September 30, 2008 increased $233.7 million and $177.3 million, respectively, from the same periods in 2007, primarily due to growth in the commercial loan category. The yield on total loans for the third quarter and first nine months of 2008 decreased 76 basis points and 59 basis points, respectively, from the comparable 2007 periods, reflecting declines in short-term interest rates. Total average securities for the three and nine months ended September 30, 2008 increased $132.0 million and $94.7 million, respectively, from the same periods last year due largely to purchases of mortgage-backed securities issued by U.S. government agencies and government-sponsored enterprises during a period of substantial spread widening for these and many other classes of investment securities. The FTE rate of return on securities for the third quarter and first nine months of 2008 decreased 57 basis points and 40 basis points, respectively, from the comparable 2007 periods. The decrease in the total yield on securities was largely attributable to a decline in dividend yield earned on the Corporation's investment in FHLB stock.

For the three and nine months ended September 30, 2008, average interest-bearing liabilities increased $355.3 million and $263.2 million, respectively, from the amounts reported for the same periods in 2007 largely due to increases in FHLB advances. The average balance of FHLB advances for the three and nine months ended September 30, 2008 increased $290.5 million and $260.0 million, respectively, while the average rate paid on FHLB advances decreased 24 basis points and 14 basis points, respectively, from the same periods a year earlier. The average balance of time deposits for the third quarter and first nine months of 2008 increased $74.4 million and $53 thousand, respectively, from the same periods in 2007. The quarterly increase was largely due to increases 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 months ended September 30, 2008 increased $53.5 million from the same period in 2007. See additional discussion on brokered certificates of deposit in the "Financial Condition" section under the caption "Deposits". The average rate paid on brokered certificates of deposit for the three months ended September 30, 2008 decreased 13 basis points from the comparable period in 2007. See Note 7 to the Consolidated Financial Statements for additional discussion on junior subordinated debentures issued in the second quarter of 2008.

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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,	2008	2007
	Average	