WESTAMERICA BANCORPORATION
Form 10-K
February 26, 2010

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**
**WASHINGTON, D.C. 20549**
**FORM 10-K**

(Mark one)

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

**For the fiscal year ended December 31, 2009**

**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: 001-9383**

**WESTAMERICA BANCORPORATION**

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

| | |
|---|---|
| **CALIFORNIA** | **94-2156203** |
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification Number) |

1108 FIFTH AVENUE, SAN RAFAEL, CALIFORNIA 94901
(Address of principal executive offices) (zip code)
Registrant s telephone number, including area code: (707) 863-6000
Securities registered pursuant to Section 12(b) of the Act:

| Title of class: | Name of each exchange on which registered: |
|---|---|
| Common Stock, no par value | The NASDAQ Stock Market LLC |

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES þ NO o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES o NO þ

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES þ NO o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES o NO o

Indicate by check mark if disclosure of delinquent filers pursuant to item 405 of Regulation S-K (section 229.405) is not contained herein, and will not be contained, to the best of the registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. þ

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

Large accelerated filer þ Accelerated filer o 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). YES o NO þ

The aggregate market value of the Common Stock held by non-affiliates of the registrant as of June 30, 2009 as reported on the NASDAQ Global Select Market, was $1,075,778,908.29. Shares of Common Stock held by each executive officer and director and by each person who owns 5% or more of the outstanding Common Stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

Number of shares outstanding of each of the registrant s classes of common stock, as of the close of business on February 19, 2010 29,227,611 Shares

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement relating to registrant s Annual Meeting of Shareholders, to be held on April 22, 2010, are incorporated by reference in Items 10, 11, 12, 13 and 14 of Part III to the extent described therein.

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**PART IV**

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FORWARD-LOOKING STATEMENTS

This report on Form 10-K contains forward-looking statements about Westamerica Bancorporation for which it claims the protection of the safe harbor provisions contained in the Private Securities Litigation Reform Act of 1995. Examples of forward-looking statements include, but are not limited to: (i) projections of revenues, expenses, income or loss, earnings or loss per share, the payment or nonpayment of dividends, capital structure and other financial items; (ii) statements of plans, objectives and expectations of the Company or its management or board of directors, including those relating to products or services; (iii) statements of future economic performance; and (iv) statements of assumptions underlying such statements. Words such as believes , anticipates , expects , intends , targeted , pr continue , remain , will , should , may and other similar expressions are intended to identify forward-looking stat but are not the exclusive means of identifying such statements.

These forward-looking statements are based on Management s current knowledge and belief and include information concerning the Company s possible or assumed future financial condition and results of operations. A number of factors, some of which are beyond the Company s ability to predict or control, could cause future results to differ materially from those contemplated. These factors include but are not limited to (1) the length and severity of current difficulties in the national and California economies and the effects of federal government efforts to address those difficulties; (2) liquidity levels in capital markets; (3) fluctuations in asset prices including, but not limited to stocks, bonds, real estate, and commodities; (4) the effect of acquisitions and integration of acquired businesses including the recent acquisition of County Bank assets and assumption of County Bank liabilities from the Federal Deposit Insurance Corporation; (5) economic uncertainty created by terrorist threats and attacks on the United States, the actions taken in response, and the uncertain effect of these events on the national and regional economies; (6) changes in the interest rate environment; (7) changes in the regulatory environment; (8) competitive pressure in the banking industry; (9) operational risks including data processing system failures or fraud; (10) volatility of interest rate sensitive loans, deposits and investments; (11) asset/liability management risks and liquidity risks; and (12) changes in the securities markets. The Company undertakes no obligation to update any forward-looking statements in this report. See also Risk Factors in Item 1A and other risk factors discussed elsewhere in this Report.

# PART I

## ITEM 1. BUSINESS

Westamerica Bancorporation (the Company ) is a bank holding company registered under the Bank Holding Company Act of 1956, as amended ( BHCA ). Its legal headquarters are located at 1108 Fifth Avenue, San Rafael, California 94901. Principal administrative offices are located at 4550 Mangels Boulevard, Fairfield, California 94534 and its telephone number is (707) 863-6000. The Company provides a full range of banking services to individual and corporate customers in Northern and Central California through its subsidiary bank, Westamerica Bank ( WAB or the Bank ). The principal communities served are located in Northern and Central California, from Mendocino, Lake and Nevada Counties in the north to Kern County in the south. The Company s strategic focus is on the banking needs of small businesses. In addition, the Bank owns 100% of the capital stock of Community Banker Services Corporation ( CBSC ), a company engaged in providing the Company and its subsidiaries with data processing services and other support functions.

The Company was incorporated under the laws of the State of California in 1972 as Independent Bankshares Corporation pursuant to a plan of reorganization among three previously unaffiliated Northern California banks. The Company operated as a multi-bank holding company until mid-1983, at which time the then six subsidiary banks were merged into a single bank named Westamerica Bank and the name of the holding company was changed to Westamerica Bancorporation.

The Company acquired five additional banks within its immediate market area during the early to mid 1990 s. In April 1997, the Company acquired ValliCorp Holdings, Inc., parent company of ValliWide Bank, the largest independent bank holding company headquartered in Central California. Under the terms of all of the merger agreements, the Company issued shares of its common stock in exchange for all of the outstanding shares of the acquired institutions. The subsidiary banks acquired were merged with and into WAB. These five aforementioned business combinations were accounted for as poolings-of-interests.

In August, 2000, the Company acquired First Counties Bank. In June of 2002 the Company acquired Kerman State Bank. On March 1, 2005, the Company acquired Redwood Empire Bancorp, the parent company of National Bank of the Redwoods (NBR). These acquisitions were accounted for using the purchase accounting method.

On February 6, 2009, the Bank entered into a Purchase and Assumption Agreement (the Agreement ) with the Federal Deposit Insurance Corporation as Receiver ( Receiver ) of County Bank ( County ) and in its corporate capacity. At February 6, 2009, County s accounting records reflected total assets to be purchased by the Bank of approximately $1.6 billion and total deposits to be assumed by the Bank of approximately $1.2 billion. Under the terms of the Agreement, the Bank purchased substantially all assets of County, including loans, investment securities and other assets, excluding premises, equipment and company owned life insurance. The Bank exercised its rights under a short-term option to purchase certain premises and equipment from the Receiver. Under the terms of the Agreement, the Bank also assumed all the deposits, secured liabilities, and certain other liabilities of County. The Agreement also provided a loss sharing arrangement over certain assets, primarily loans and repossessed loan collateral. Losses on such covered assets up to $269 million are shared 80% by the Receiver and 20% by the Bank. Losses on covered assets exceeding $269 million are shared 95% by the Receiver and 5% by the Bank.

On February 13, 2009, the Company entered into a Letter Agreement and related Securities Purchase Agreement (collectively the Securities Purchase Agreement ) with the United States Treasury ( Treasury ) to issue 83,726 preferred shares at $1,000 per share, or $83,726,000 in total issuance ( Treasury Preferred Stock ). The Company retired 41,863 shares and 41,863 shares of Treasury Preferred Stock on September 2, 2009 and November 18, 2009, respectively. While outstanding, the Treasury Preferred Stock placed certain restrictions on the Company: dividends to common shareholders could not be increased, share repurchases were limited to repurchases related to employee benefit programs, and executive compensation exceeding $500,000 could not be deducted for federal income tax purposes. In addition, executive compensation programs could not be structured to reward excessive risk-taking. The Company also issued a warrant to purchase 246,640 shares of its common stock at an exercise price of $50.92 per share ( TARP Warrant ) in conjunction with the Treasury Preferred Stock issuance. The TARP Warrants remain outstanding at December 31, 2009.

At December 31, 2009, the Company had consolidated assets of approximately $5.0 billion, deposits of approximately $4.1 billion and shareholders equity of approximately $505.4 million. The Company and its subsidiaries employed approximately 1,051 full-time equivalent staff as of December 31, 2009.

The Company s annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports as well as beneficial ownership reports on Forms 3, 4 and 5 are available through the SEC s website (http://www.sec.gov). Such documents are also available free of charge from the Company, as well as the Company s director, officer and employee Code of Conduct and Ethics, by request to:

Westamerica Bancorporation
Corporate Secretary A-2M
Post Office Box 1200
Suisun City, California 94585-1200

**Supervision and Regulation**

The following is not intended to be an exhaustive description of the statutes and regulations applicable to the Company s or the Bank s business. The description of statutory and regulatory provisions is qualified in its entirety by reference to the particular statutory or regulatory provisions. Moreover, major new legislation and other regulatory changes affecting the Company, the Bank, and the financial services industry in general have occurred in the last several years and can be expected to occur in the future. The nature, timing and impact of new and amended laws and regulations cannot be accurately predicted.

*Regulation and Supervision of Bank Holding Companies*

The Company is a bank holding company subject to the BHCA. The Company reports to, is registered with, and may be examined by, the Board of Governors of the Federal Reserve System ( FRB ). The FRB also has the authority to examine the Company s subsidiaries. The costs of any examination by the FRB are payable by the Company. The Company is a bank holding company within the meaning of Section 3700 of the California Financial Code. As such, the Company and the Bank are subject to examination by, and may be required to file reports with, the California Commissioner of Financial Institutions (the Commissioner ).

The FRB has significant supervisory and regulatory authority over the Company and its affiliates. The FRB requires the Company to maintain certain levels of capital. See Capital Standards. The FRB also has the authority to take enforcement action against any bank holding company that commits any unsafe or unsound practice, or violates certain laws, regulations or conditions imposed in writing by the FRB. Under the BHCA, the Company is required to obtain the prior approval of the FRB before it acquires, merges or consolidates with any bank or bank holding company. Any company seeking to acquire, merge or consolidate with the Company also would be required to obtain the prior approval of the FRB.

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The Company is generally prohibited under the BHCA from acquiring ownership or control of more than 5% of any class of voting shares of any company that is not a bank or bank holding company and from engaging directly or indirectly in activities other than banking, managing banks, or providing services to affiliates of the holding company. However, a bank holding company, with the approval of the FRB, may engage, or acquire the voting shares of companies engaged, in activities that the FRB has determined to be closely related to banking or managing or controlling banks. A bank holding company must demonstrate that the benefits to the public of the proposed activity will outweigh the possible adverse effects associated with such activity.

The FRB generally prohibits a bank holding company from declaring or paying a cash dividend that would impose undue pressure on the capital of subsidiary banks or would be funded only through borrowing or other arrangements which might adversely affect a bank holding company s financial position. Under the FRB policy, a bank holding company should not continue its existing rate of cash dividends on its common stock unless its net income is sufficient to fully fund each dividend and its prospective rate of earnings retention appears consistent with its capital needs, asset quality and overall financial condition. See the section entitled Restrictions on Dividends and Other Distributions for additional restrictions on the ability of the Company and the Bank to pay dividends.

Transactions between the Company and the Bank are restricted under Regulation W, adopted in 2003. The regulation codifies prior interpretations of the FRB and its staff under Sections 23A and 23B of the Federal Reserve Act. In general, subject to certain specified exemptions, a bank or its subsidiaries are limited in their ability to engage in covered transactions with affiliates: (a) to an amount equal to 10% of the bank s capital and surplus, in the case of covered transactions with any one affiliate; and (b) to an amount equal to 20% of the bank s capital and surplus, in the case of covered transactions with all affiliates. The Company is considered to be an affiliate of the Bank.

A covered transaction includes, among other things, a loan or extension of credit to an affiliate; a purchase of securities issued by an affiliate; a purchase of assets from an affiliate, with some exceptions; and the issuance of a guarantee, acceptance or letter of credit on behalf of an affiliate.

Federal regulations governing bank holding companies and change in bank control (Regulation Y) provide for a streamlined and expedited review process for bank acquisition proposals submitted by well-run bank holding companies. These provisions of Regulation Y are subject to numerous qualifications, limitations and restrictions. In order for a bank holding company to qualify as well-run, both it and the insured depository institutions which it controls must meet the well capitalized and well managed criteria set forth in Regulation Y.

On March 11, 2000, the Gramm-Leach-Bliley Act (the GLBA ), or the Financial Services Act of 1999 became effective. The GLBA repealed provisions of the Glass-Steagall Act, which had prohibited commercial banks and securities firms from affiliating with each other and engaging in each other s businesses. Thus, many of the barriers prohibiting affiliations between commercial banks and securities firms have been eliminated.

The BHCA was also amended by the GLBA to allow new financial holding companies ( FHCs ) to offer banking, insurance, securities and other financial products to consumers. Specifically, the GLBA amended section 4 of the BHCA in order to provide for a framework for the engagement in new financial activities. A bank holding company ( BHC ) may elect to become an FHC if all its subsidiary depository institutions are well capitalized and well managed. If these requirements are met, a BHC may file a certification to that effect with the FRB and declare that it elects to become an FHC. After the certification and declaration is filed, the FHC may engage either de novo or through an acquisition in any activity that has been determined by the FRB to be financial in nature or incidental to such financial activity. BHCs may engage in financial activities without prior notice to the FRB if those activities qualify under the list of permissible activities in section 4(k) of the BHCA. However, notice must be given to the FRB within 30 days after an FHC has commenced one or more of the financial activities. The Company has not elected to become an FHC.

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*Regulation and Supervision of Banks*

The Bank is a California state-chartered bank and its deposits are insured by the Federal Deposit Insurance Corporation (the FDIC ). The Bank is subject to regulation, supervision and regular examination by the California Department of Financial Institutions ( DFI ), and the FDIC. The regulations of these agencies affect most aspects of the Bank s business and prescribe permissible types of loans and investments, the amount of required reserves, requirements for branch offices, the permissible scope of its activities and various other requirements.

In addition to federal banking law, the Bank is also subject to applicable provisions of California law. Under California law, the Bank is subject to various restrictions on, and requirements regarding, its operations and administration including the maintenance of branch offices and automated teller machines, capital requirements, deposits and borrowings, shareholder rights and duties, and investment and lending activities.

California law permits a state-chartered bank to invest in the stock and securities of other corporations, subject to a state-chartered bank receiving either general authorization or, depending on the amount of the proposed investment, specific authorization from the Commissioner. While a member of the Federal Reserve System, the Bank s investment authority was limited by regulations promulgated by the FRB. In addition, the Federal Deposit Insurance Corporation Improvement Act ( FDICIA ) imposes limitations on the activities and equity investments of state chartered, federally insured banks. FDICIA also prohibits a state bank from making an investment or engaging in any activity as a principal that is not permissible for a national bank, unless the Bank is adequately capitalized and the FDIC approves the investment or activity after determining that such investment or activity does not pose a significant risk to the deposit insurance fund.

*Capital Standards*

The federal banking agencies have risk-based capital adequacy guidelines intended to provide a measure of capital adequacy that reflects the degree of risk associated with a banking organization s operations for both transactions resulting in assets being recognized on the balance sheet as assets, and the extension of credit facilities such as letters of credit and recourse arrangements, which are recorded as off balance sheet items. Under these guidelines, nominal dollar amounts of assets and credit equivalent amounts of off balance sheet items are multiplied by one of several risk adjustment percentages, which range from 0% for assets with low credit risk, such as certain U.S. government securities, to 100% for assets with relatively higher credit risk, such as certain loans.

A banking organization s risk-based capital ratios are obtained by dividing its qualifying capital by its total risk-adjusted assets and off balance sheet items.

The federal banking agencies take into consideration concentrations of credit risk and risks from nontraditional activities, as well as an institution s ability to manage those risks, when determining the adequacy of an institution s capital. This evaluation is made as a part of the institution s regular safety and soundness examination. The federal banking agencies also consider interest rate risk (related to the interest rate sensitivity of an institution s assets and liabilities, and its off balance sheet financial instruments) in the evaluation of a bank s capital adequacy.

As of December 31, 2009, the Company s and the Bank s respective ratios exceeded applicable regulatory requirements. See Note 10 to the consolidated financial statements for capital ratios of the Company and the Bank, compared to the standards for well capitalized depository institutions and for minimum capital requirements.

*Prompt Corrective Action and Other Enforcement Mechanisms*

FDICIA requires each federal banking agency to take prompt corrective action to resolve the problems of insured depository institutions, including but not limited to those that fall below one or more prescribed minimum capital ratios.

An institution that, based upon its capital levels, is classified as well capitalized, adequately capitalized or undercapitalized may be treated as though it were in the next lower capital category if the appropriate federal banking agency, after notice and opportunity for hearing, determines that an unsafe or unsound condition or an unsafe or unsound practice warrants such treatment. At each successive lower capital category, an insured depository institution is subject to more restrictions. In addition to measures taken under the prompt corrective action provisions, commercial banking organizations may be subject to potential enforcement actions by the federal banking agencies for unsafe or unsound practices in conducting their businesses or for violations of any law, rule, regulation or any condition imposed in writing by the agency or any written agreement with the agency.

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*Safety and Soundness Standards*

The Company s ability to pay dividends to its shareholders is subject to the restrictions set forth in the California General Corporation Law or the CGCL. The CGCL provides that a corporation may make a distribution to its shareholders if the corporation s retained earnings equal or exceed the amount of the proposed distribution. The CGCL further provides that, in the event that sufficient retained earnings are not available for the proposed distribution, a corporation may nevertheless make a distribution to its shareholders if the sum of the assets of the corporation (exclusive of goodwill, capitalized research and development expenses and deferred charges) would be at least equal to 1.25 times its liabilities (not including deferred taxes, deferred income and other deferred credits).

FDICIA also implemented certain specific restrictions on transactions and required federal banking regulators to adopt overall safety and soundness standards for depository institutions related to internal control, loan underwriting and documentation and asset growth. Among other things, FDICIA limits the interest rates paid on deposits by undercapitalized institutions, restricts the use of brokered deposits, limits the aggregate extensions of credit by a depository institution to an executive officer, director, principal shareholder or related interest, and reduces deposit insurance coverage for deposits offered by undercapitalized institutions for deposits by certain employee benefits accounts. The federal banking agencies may require an institution to submit to an acceptable compliance plan as well as have the flexibility to pursue other more appropriate or effective courses of action given the specific circumstances and severity of an institution s noncompliance with one or more standards.

Federal banking agencies require banks to maintain adequate valuation allowances for potential credit losses. The Company has an internal staff that continually reviews loan quality and reports to the Board of Directors. This analysis includes a detailed review of the classification and categorization of problem loans, assessment of the overall quality and collectibility of the loan portfolio, consideration of loan loss experience, trends in problem loans, concentration of credit risk, and current economic conditions, particularly in the Bank s market areas. Based on this analysis, Management, with the review and approval of the Board, determines the adequate level of allowance required. The allowance is allocated to different segments of the loan portfolio, but the entire allowance is available for the loan portfolio in its entirety.

*Restrictions on Dividends and Other Distributions*

The power of the board of directors of an insured depository institution to declare a cash dividend or other distribution with respect to capital is subject to statutory and regulatory restrictions which limit the amount available for such distribution depending upon the earnings, financial condition and cash needs of the institution, as well as general business conditions. FDICIA prohibits insured depository institutions from paying management fees to any controlling persons or, with certain limited exceptions, making capital distributions, including dividends, if, after such transaction, the institution would be undercapitalized.

In addition to the restrictions imposed under federal law, banks chartered under California law generally may only pay cash dividends to the extent such payments do not exceed the lesser of retained earnings of the bank or the bank s net income for its last three fiscal years (less any distributions to shareholders during this period). In the event a bank desires to pay cash dividends in excess of such amount, the bank may pay a cash dividend with the prior approval of the Commissioner in an amount not exceeding the greatest of the bank s retained earnings, the bank s net income for its last fiscal year or the bank s net income for its current fiscal year.

The federal banking agencies also have the authority to prohibit a depository institution from engaging in business practices which are considered to be unsafe or unsound, possibly including payment of dividends or other payments under certain circumstances even if such payments are not expressly prohibited by statute.

*Premiums for Deposit Insurance and Assessments for Examinations*

The Bank s deposits are insured by the Deposit Insurance Fund (DIF) administered by the FDIC. FDICIA established several mechanisms to increase funds to protect deposits insured by the DIF. The FDIC is authorized to assess premiums on depository institutions which are members of the DIF, and borrow from the Treasury. Any borrowings not repaid by asset sales are to be repaid through insurance premiums assessed to member institutions. Such premiums must be sufficient to repay any borrowed funds within 15 years and provide insurance fund reserves of $1.25 for each $100 of insured deposits. FDICIA also provides authority for special assessments against insured deposits.

Congress adopted the Federal Deposit Insurance Reform Act of 2005 as part of the Deficit Reduction Act of 2005 and the President signed it on February 8, 2006 and a companion bill, the Federal Deposit Insurance Reform Conforming Amendments Act of 2005, on February 15, 2006. This legislation provided for:

- merging the DIF and SAIF deposit insurance funds;
- annually adjusting the minimum insurance fund reserve ratio between $1.15 and $1.50 per $100 of insured deposits;
- increasing deposit coverage for retirement accounts to $250,000,
- indexing the insurance level for inflation, with any increases approved by the FDIC and National Credit Union Administration (NCUA) on a five-year cycle beginning in 2010 after review of the state of the deposit insurance fund and related factors;
- credits of up to $4.7 billion to offset premiums for banks that capitalized the FDIC by 1996; and
- a historical basis concept for distributing credits and dividends to reflect past contributions to the insurance funds.

The FDIC has designated the DIF long-term target reserve ratio at 1.25% of insured deposits. Due to recent bank failures, the FDIC insurance fund reserve ratio has fallen below 1.15%, the statutory minimum. Effective January 1, 2009, the FDIC adopted a restoration plan that uniformly increased insurance assessments. The FDIC adopted changes to the deposit insurance assessment system beginning with the second quarter of 2009 to make the increase in assessments fairer by requiring riskier institutions to pay a larger share. Institutions would be classified into one of four risk categories. Within each category, the FDIC will be able to assess higher rates to institutions with a significant reliance on secured liabilities, which generally raises the FDIC s loss in the event of failure without providing additional assessment revenue. The proposal also would assess higher rates for institutions with a significant reliance on brokered deposits but, for well-managed and well-capitalized institutions, only when accompanied by rapid asset growth. The proposal also would provide incentives in the form of a reduction in assessment rates for institutions to hold long-term unsecured debt and, for smaller institutions, high levels of Tier 1 capital. Together, the changes improved the way the system differentiates risk among insured institutions.

Under the EESA, adopted on October 3, 2008, certain increases in FDIC deposit insurance have also been approved, as amended. From October 3, 2008, until December 31, 2013, the amount of deposit insurance provided by the FDIC is increased from $100,000 to $250,000. This temporary increase is automatic. In November 2008, the FDIC adopted the Transaction Account Guaranty Program ( TAGP ) that provides, in exchange for additional assessments, unlimited deposit insurance on funds in noninterest-bearing transaction deposit accounts, certain attorney trust accounts, and NOW accounts paying no more than 50 basis points of interest regardless of dollar amount. The Bank elected to cease participation in the TAGP as of December 31, 2009. Given the current deficient funded condition of the DIF and expected continued bank failures, the Bank expects premiums for deposit insurance to remain elevated. In addition, in May 2009, the FDIC imposed a special assessment of 5 basis points ( bp ) of each institution s assets minus Tier 1 capital as of June 30, 2009, not to exceed 10 bp times its assessment base for the quarter. In November 2009, the FDIC adopted a rule requiring prepayment of assessments for 2010, 2011 and 2012.

*Community Reinvestment Act and Fair Lending Developments*

The Bank is subject to certain fair lending requirements and reporting obligations involving home mortgage lending operations and Community Reinvestment Act ( CRA ) activities. The CRA generally requires the federal banking agencies to evaluate the record of financial institutions in meeting the credit needs of their local communities, including low and moderate income neighborhoods. In addition to substantive penalties and corrective measures that may be required for a violation of certain fair lending laws, the federal banking agencies may take compliance with such laws and CRA into account when regulating and supervising other activities.

*Financial Privacy Legislation and Customer Information Security*

The GLBA, in addition to the previously described changes in permissible nonbanking activities permitted to banks, BHCs and FHCs, also required the federal banking agencies, among other federal regulatory agencies, to adopt regulations governing the privacy of consumer financial information. The Bank is subject to the FRB s regulations in this area. The federal bank regulatory agencies have established standards for safeguarding nonpublic personal information about customers that implement provisions of the GLBA (the Guidelines ). Among other things, the

Guidelines require each financial institution, under the supervision and ongoing oversight of its Board of Directors or an appropriate committee thereof, to develop, implement and maintain a comprehensive written information security program designed to ensure the security and confidentiality of customer information, to protect against any anticipated threats or hazards to the security or integrity of such information, and to protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer.

*U.S.A. PATRIOT Act*

On October 26, 2001, the President signed into law the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 or the USA Patriot Act. Title III of the Act is the International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001. It includes numerous provisions for fighting international money laundering and blocking terrorist access to the U.S. financial system. The goal of Title III is to prevent the U.S. financial system and the U.S. clearing mechanisms from being used by parties suspected of terrorism, terrorist financing and money laundering.

The provisions of Title III of the USA Patriot Act which affect banking organizations, including the Bank, are generally set forth as amendments to the Bank Secrecy Act. These provisions relate principally to U.S. banking organizations relationships with foreign banks and with persons who are resident outside the United States. The USA Patriot Act does not impose any filing or reporting obligations for banking organizations, but does require certain additional due diligence and recordkeeping practices.

*Sarbanes-Oxley Act of 2002*

On July 30, 2002, the U.S. Congress enacted the Sarbanes-Oxley Act of 2002 ( Sarbanes-Oxley ). The stated goals of Sarbanes-Oxley are to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies and to protect investors by improving the accuracy and reliability of corporate disclosures pursuant to the securities laws. Sarbanes-Oxley generally applies to all companies, both U.S. and non-U.S., that file or are required to file periodic reports under the Securities Exchange Act of 1934 (the Exchange Act ).

Sarbanes-Oxley includes very specific additional disclosure requirements and corporate governance rules, required the SEC and securities exchanges to adopt extensive additional disclosure, corporate governance and other related rules and mandates further studies of certain issues. Sarbanes-Oxley represents significant federal involvement in matters traditionally left to state regulatory systems, such as the regulation of the accounting profession, and to state corporate law, such as the relationship between a board of directors and management and between a board of directors and its committees and public company shareholders.

Sarbanes-Oxley addresses, among other matters: (i) independent audit committees for reporting companies whose securities are listed on national exchanges or automated quotation systems (the Exchanges ) and expanded duties and responsibilities for audit committees; (ii) certification of financial statements by the chief executive officer and the chief financial officer; (iii) the forfeiture of bonuses or other incentive-based compensation and profits from the sale of an issuer s securities by directors and senior officers in the twelve month period following initial publication of any financial statements that later require restatement; (iv) a prohibition on insider trading during pension plan black out periods; (v) disclosure of off-balance sheet transactions; (vi) a prohibition on personal loans to directors and officers under most circumstances with exceptions for certain normal course transactions by regulated financial institutions; (vii) expedited electronic filing requirements related to trading by insiders in an issuer s securities on Form 4; (viii) disclosure of a code of ethics and filing a Form 8-K for a change or waiver of such code; (ix) accelerated filing of periodic reports; (x) the formation of the Public Company Accounting Oversight Board ( PCAOB ) to oversee public accounting firms and the audit of public companies that are subject to the securities laws; (xi) auditor independence; (xii) internal control evaluation and reporting; and (xiii) various increased criminal penalties for violations of securities laws.

Given the extensive role of the SEC, the PCAOB and the Exchanges in implementing rules relating to Sarbanes-Oxley s requirements, the federalization of certain elements traditionally within the sphere of state corporate law, the impact of Sarbanes-Oxley on reporting companies has been and will continue to be significant.

*Programs To Mitigate Identity Theft*

In November 2007, federal banking agencies together with the NCUA and FTC adopted regulations under the Fair and Accurate Credit Transactions Act of 2003 to require financial institutions and other creditors to develop and implement a written identity theft prevention program to detect, prevent and mitigate identity theft in connection with certain new and existing accounts. Covered accounts generally include consumer accounts and other accounts that present a reasonably foreseeable risk of identity theft. Each institution s program must include policies and procedures designed to: (i) identify indicators, or red flags, of possible risk of identity theft based; (ii) detect the occurrence of red flags; (iii) respond appropriately to red flags that are detected; and (iv) ensure that the program is updated periodically as appropriate to address changing circumstances. The regulations include guidelines that each institution must consider and, to the extent appropriate, include in its program.

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*Pending Legislation*

Changes to state laws and regulations (including changes in interpretation or enforcement) can affect the operating environment of BHCs and their subsidiaries in substantial and unpredictable ways. From time to time, various legislative and regulatory proposals are introduced. These proposals, if codified, may change banking statutes and regulations and the Company s operating environment in substantial and unpredictable ways. If codified, these proposals could increase or decrease the cost of doing business, limit or expand permissible activities or affect the competitive balance among banks, savings associations, credit unions and other financial institutions. The Company cannot accurately predict whether those changes in laws and regulations will occur, and, if those changes occur, the ultimate effect they would have upon our financial condition or results of operations. It is likely, however, that the current level of enforcement and compliance-related activities of federal and state authorities will continue and potentially increase.

**Competition**

In the past, the Bank s principal competitors for deposits and loans have been major banks and smaller community banks, savings and loan associations and credit unions. To a lesser extent, competition was also provided by thrift and loans, mortgage brokerage companies and insurance companies. Other institutions, such as brokerage houses, mutual fund companies, credit card companies, and certain retail establishments have offered investment vehicles which also compete with banks for deposit business. Federal legislation in recent years has encouraged competition between different types of financial institutions and fostered new entrants into the financial services market.

The enactment of the Interstate Banking and Branching Act in 1994 and the California Interstate Banking and Branching Act of 1995 have increased competition within California. Regulatory reform, as well as other changes in federal and California law, will also affect competition. While the future impact of these changes, and of other proposed changes, cannot be predicted with certainty, it is clear that the business of banking will remain highly competitive.

Legislative changes, as well as technological and economic factors, can be expected to have an ongoing impact on competitive conditions within the financial services industry. As an active participant in the financial markets, the Company believes that it continually adapts to these changing competitive conditions.

**ITEM 1A. RISK FACTORS**

Readers and prospective investors in the Company s securities should carefully consider the following risk factors as well as the other information contained or incorporated by reference in this report.

The risks and uncertainties described below are not the only ones facing the Company. Additional risks and uncertainties that Management is not aware of or focused on or that Management currently deems immaterial may also impair the Company s business operations. This report is qualified in its entirety by these risk factors.

If any of the following risks actually occur, the Company s financial condition and results of operations could be materially and adversely affected. If this were to happen, the value of the company s securities could decline significantly, and investors could lose all or part of their investment in the Company s common stock.

## Market and Interest Rate Risk

***Changes in interest rates could reduce income and cash flow.***

The discussion in this report under Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations Asset and Liability Management and - Liquidity and Item 7A Quantitative and Qualitative Disclosures About Market Risk is incorporated by reference in this paragraph. The Company s income and cash flow depend to a great extent on the difference between the interest earned on loans and investment securities compared to the interest paid on deposits and other borrowings, and the Company s success in competing for loans and deposits. The Company cannot control or prevent changes in the level of interest rates. They fluctuate in response to general economic conditions and the policies of various governmental and regulatory agencies, in particular, the Federal Open Market Committee of the FRB. Changes in monetary policy, including changes in interest rates, will influence the origination of loans, the purchase of investments, the generation of deposits and other borrowings, and the rates received on loans and investment securities and paid on deposits and other liabilities.

***Changes in capital market conditions could reduce asset valuations.***

Capital market conditions, including liquidity, investor confidence, bond issuer credit worthiness perceived counter-party risk, the supply of and demand for financial instruments, the financial strength of market participants, and other factors, can materially impact the value of the Company s assets. An impairment in the value of the Company s assets could result in asset write-downs, reducing the Company s asset values, earnings, and equity.

***Current market developments may adversely affect the Company s industry, business and results of operations.***

Declines in the housing market during recent years, with falling home prices and increasing foreclosures and unemployment, have resulted in significant write-downs of asset values by financial institutions, including government-sponsored entities and major commercial and investment banks. These write-downs have caused many financial institutions to seek additional capital, to merge with larger and stronger institutions and, in some cases, to fail. Many lenders and institutional investors, concerned about the stability of the financial markets generally and the strength of counterparties, have reduced or ceased to provide funding to borrowers, including other financial institutions. The resulting lack of available credit, volatility in the financial markets and reduced business activity could materially and adversely affect the Company s business, financial condition and results of operations.

***The soundness of other financial institutions could adversely affect the Company.***

Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships. The Company routinely executes transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, investment banks, and other institutional clients. Many of these transactions expose the Company to credit risk in the event of default of the Company s counterparty or client. In addition, the Company s credit risk may be increased when the collateral the Company holds cannot be realized or is liquidated at prices not sufficient to recover the full amount of the secured obligation. There is no assurance that any such losses would not materially and adversely affect the Company s results of operations or earnings.

***There can be no assurance that the recently enacted legislation will help stabilize the U.S. financial system.***

On October 3, 2008, President Bush signed into law the Emergency Economic Stabilization Act of 2008 (the EESA ), which evolved from the Treasury s initial proposal in response to the financial crises affecting the banking system and financial markets and going concern threats to investment banks and other financial institutions. On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act of 2009 (the ARRA ) into law. The Treasury and banking regulators are implementing a number of programs under this legislation to address capital and liquidity issues in the banking system. There can be no assurance, however, as to the actual impact that the EESA or ARRA will have on the financial markets. The failure of the EESA or ARRA to help stabilize the financial markets and a worsening of financial market conditions could materially and adversely affect the Company s business, financial condition, results of operations, access to credit or the trading price of the Company s common stock.

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**Risks Related to the Nature and Geographical Location of the Company s Business**

***The Company invests in loans that contain inherent credit risks that may cause the Company to incur losses.***

The Company can provide no assurance that the credit quality of the loan portfolio will not deteriorate in the future and that such deterioration will not adversely affect the Company.

***The Company s operations are concentrated geographically in California, and poor economic conditions may cause the Company to incur losses.***

Substantially all of the Company s business is located in California. A portion of the loan portfolio of the Company is dependent on real estate. At December 31, 2009, real estate served as the principal source of collateral with respect to approximately 53% of the Company s loan portfolio. The Company s financial condition and operating results will be subject to changes in economic conditions in California. In the early to mid-1990s, California experienced a significant and prolonged downturn in its economy, which adversely affected financial institutions. The California economy is currently weak following a severe recession which may last for a prolonged period of time. In 2007 and throughout 2008, much of the California and national real estate market experienced a decline in values of varying degrees. This decline is having an adverse impact on the businesses of some of the Company s borrowers and on the value of the collateral for many of the Company s loans. Economic conditions in California are subject to various uncertainties at this time, including the decline in construction and real estate sectors, the California state government s budgetary difficulties and continuing fiscal difficulties. The Company can provide no assurance that conditions in the California economy will not deteriorate in the future and that such deterioration will not adversely affect the Company.

***The markets in which the Company operates are subject to the risk of earthquakes and other natural disasters.***

Most of the properties of the Company are located in California. Also, most of the real and personal properties which currently secure some of the Company s loans are located in California. California is a state which is prone to earthquakes, brush fires, flooding and other natural disasters. In addition to possibly sustaining damage to its own properties, if there is a major earthquake, flood, fire or other natural disaster, the Company faces the risk that many of its borrowers may experience uninsured property losses, or sustained job interruption and/or loss which may materially impair their ability to meet the terms of their loan obligations. A major earthquake, flood, fire or other natural disaster in California could have a material adverse effect on the Company s business, financial condition, results of operations and cash flows.

***As a financial services company, adverse changes in general business or economic conditions could have a material adverse effect on the Company s financial condition and results of operations.***

A sustained or continuing weakness or weakening in business and economic conditions generally or specifically in the principal markets in which the Company does business could have one or more of the following adverse impacts on the Company s business:

- a decrease in the demand for loans and other products and services offered by the Company;
- an increase or decrease in the usage of unfunded commitments;
- an impairment of certain intangible assets, such as goodwill;
- an impairment of certain investment securities, such as state and local municipal securities;
- an impairment of life insurance policies owned by the Company;
- an increase in the number of clients and counterparties who become delinquent, file for protection under bankruptcy laws or default on their loans or other obligations to the Company.
- an increase in the number of delinquencies, bankruptcies or defaults could result in a higher level of nonperforming assets, net charge-offs, provision for loan losses, and valuation adjustments on loans held for sale.

***The Company s Business May Be Adversely Affected by Conditions in the Financial Markets and Economic Conditions Generally.***

The United States economy has been in a recession and the strength of the current recovery is uncertian. Business activity across a wide range of industries and regions is greatly reduced and local governments and many businesses are in serious difficulty due to high unemployment.

Since mid-2007, and particularly during the second half of 2008, the financial services industry and the securities markets generally were materially and adversely affected by significant declines in the values of nearly all asset classes and by a serious lack of liquidity. This was initially triggered by declines in home prices and the values of subprime mortgages, but spread to all mortgage and real estate asset classes, to leveraged bank loans and to nearly all asset classes, including equities.

Market conditions have also led to the failure or merger of a number of financial institutions. Financial institution failures or near-failures have resulted in further losses as a consequence of defaults on securities issued by them and defaults under contracts entered into with such entities as counterparties. Furthermore, declining asset values, defaults on mortgages and consumer loans, have combined to increase credit spreads, and to cause rating agencies to lower credit ratings. Some banks and other lenders have suffered significant losses and have become reluctant to lend, even on a secured basis, due to the increased risk of default and the impact of declining asset values on the value of collateral. The foregoing has significantly weakened the strength and liquidity of some financial institutions worldwide. In 2008, the U.S. government, the Federal Reserve and other regulators took numerous steps to increase liquidity and to restore investor confidence, including investing approximately $200 billion in the equity of other banking organizations.

The Company s financial performance generally, and in particular the ability of borrowers to pay interest on and repay principal of outstanding loans and the value of collateral securing those loans, is highly dependent upon on the business environment in the markets where the Company operates, in the State of California and in the United States as a whole. A favorable business environment is generally characterized by, among other factors, economic growth, efficient capital markets, low inflation, high business and investor confidence, and strong business earnings. Unfavorable or uncertain economic and market conditions can be caused by: declines in economic growth, business activity or investor or business confidence; limitations on the availability or increases in the cost of credit and capital; increases in inflation or interest rates; natural disasters; or a combination of these or other factors.

Overall, during 2009, the business environment has been adverse for many households, businesses and government entities in the United States and worldwide. It is expected that the business environment in the State of California, the United States and worldwide will continue to remain weak for the foreseeable future. There can be no assurance that these conditions will improve in the near term. Such conditions could adversely affect the credit quality of the Company s loans, the demand for loans, loan volumes and related revenue, results of operations and financial condition.

***The Value of Securities in the Company s Investment Securities Portfolio May be Negatively Affected by Continued Disruptions In Securities Markets.***

The market for some of the investment securities held in the Company s portfolio has been extremely volatile over the past several years. Volatile market conditions may detrimentally affect the value of these securities, such as through reduced valuations due to the perception of heightened credit and liquidity risks. There can be no assurance that the declines in market value will not result in other than temporary impairments of these assets, which would lead to accounting charges that could have a material adverse effect on the Company s net income and capital levels.

**Regulatory Risks**

***Restrictions on dividends and other distributions could limit amounts payable to the Company.***

As a holding company, a substantial portion of the Company s cash flow typically comes from dividends paid by the Bank. Various statutory provisions restrict the amount of dividends the Company s subsidiaries can pay to the Company without regulatory approval. In addition, if any of the Company s subsidiaries were to liquidate, that subsidiary s creditors will be entitled to receive distributions from the assets of that subsidiary to satisfy their claims against it before the Company, as a holder of an equity interest in the subsidiary, will be entitled to receive any of the assets of the subsidiary.

***Adverse effects of changes in banking or other laws and regulations or governmental fiscal or monetary policies could adversely affect the Company.***

The Company is subject to significant federal and state regulation and supervision, which is primarily for the benefit and protection of the Company s customers and not for the benefit of investors. In the past, the Company s business has been materially affected by these regulations. This trend is likely to continue in the future. As an example, the Federal Reserve Board has amended Regulation E, which implements the Electronic Fund Transfer Act, and the official staff commentary to the regulation, which interprets the requirements of Regulation E. The final rule limits the ability of a financial institution to assess an overdraft fee for paying automated teller machine (ATM) and one-time debit card transactions that overdraw a consumer s account, unless the consumer affirmatively consents, or opts in, to the institution s payment of overdrafts for these transactions. The rule has a mandatory compliance date of July 1, 2010 for new accounts and August 15, 2010 for existing accounts. Management believes that implementation of the new provisions will result in the reduction of overdraft fees collected by the Bank.

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Laws, regulations or policies, including accounting standards and interpretations currently affecting the Company and the Company s subsidiaries, may change at any time. Regulatory authorities may also change their interpretation of these statutes and regulations. Therefore, the Company s business may be adversely affected by any future changes in laws, regulations, policies or interpretations or regulatory approaches to compliance and enforcement including future acts of terrorism, major U.S. corporate bankruptcies and reports of accounting irregularities at U.S. public companies. Additionally, the Company s business is affected significantly by the fiscal and monetary policies of the federal government and its agencies. The Company is particularly affected by the policies of the FRB, which regulates the supply of money and credit in the United States of America. Under long- standing policy of the FRB, a BHC is expected to act as a source of financial strength for its subsidiary banks. As a result of that policy, the Company may be required to commit financial and other resources to its subsidiary bank in circumstances where the Company might not otherwise do so. Among the instruments of monetary policy available to the FRB are (a) conducting open market operations in U.S. government securities, (b) changing the discount rates of borrowings by depository institutions, (c) changing interest rates paid on balances financial institutions deposit with the FRB, and (d) imposing or changing reserve requirements against certain borrowings by banks and their affiliates. These methods are used in varying degrees and combinations to directly affect the availability of bank loans and deposits, as well as the interest rates charged on loans and paid on deposits. The policies of the FRB may have a material effect on the Company s business, results of operations and financial condition.

***Federal and state governments could pass legislation responsive to current credit conditions.***

As an example, the Company could experience higher credit losses because of federal or state legislation or regulatory action that reduces the amount the Bank s borrowers are otherwise contractually required to pay under existing loan contracts. Also, the Company could experience higher credit losses because of federal or state legislation or regulatory action that limits the Bank s ability to foreclose on property or other collateral or makes foreclosure less economically feasible.

The FDIC insures deposits at insured financial institutions up to certain limits. The FDIC charges insured financial institutions premiums to maintain the Deposit Insurance Fund. Current economic conditions have increased expectations for bank failures, in which case the FDIC would take control of failed banks and ensure payment of deposits up to insured limits using the resources of the Deposit Insurance Fund. In such case, the FDIC may increase premium assessments to maintain adequate funding of the Deposit Insurance Fund.

The behavior of depositors in regard to the level of FDIC insurance could cause our existing customers to reduce the amount of deposits held at the Bank, and could cause new customers to open deposit accounts at the Bank. The level and composition of the Bank s deposit portfolio directly impacts the Bank s funding cost and net interest margin.

The FRB has been providing vast amounts of liquidity into the banking system due to current economic and capital market conditions. A reduction in the FRB s activities or capacity could reduce liquidity in the markets, thereby increasing funding costs to the Bank or reducing the availability of funds to the Bank to finance its existing operations.

**Systems, Accounting and Internal Control Risks**

***The accuracy of the Company s judgments and estimates about financial and accounting matters will impact operating results and financial condition.***

The discussion under Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies in this report and the information referred to in that discussion is incorporated by reference in this paragraph. The Company makes certain estimates and judgments in preparing its financial statements. The quality and accuracy of those estimates and judgments will have an impact on the Company s operating results and financial condition.

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***The Company s information systems may experience an interruption or breach in security.***

The Company relies heavily on communications and information systems to conduct its business. Any failure, interruption or breach in security of these systems could result in failures or disruptions in the Company s customer relationship management and systems. There can be no assurance that any such failures, interruptions or security breaches will not occur or, if they do occur, that they will be adequately corrected by the Company. The occurrence of any such failures, interruptions or security breaches could damage the Company s reputation, result in a loss of customer business, subject the Company to additional regulatory scrutiny, or expose the Company to litigation and possible financial liability, any of which could have a material adverse effect on the Company s financial condition and results of operations.

***The Company s controls and procedures may fail or be circumvented.***

Management regularly reviews and updates the Company s internal control over financial reporting, disclosure controls and procedures, and corporate governance policies and procedures. The Company maintains controls and procedures to mitigate against risks such as processing system failures and errors, and customer or employee fraud, and maintains insurance coverage for certain of these risks. Any system of controls and procedures, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Events could occur which are not prevented or detected by the Company s internal controls or are not insured against or are in excess of the Company s insurance limits. Any failure or circumvention of the Company s controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on the Company s business, results of operations and financial condition.

***The Company may have underestimated losses on loans of the former County Bank.***

On February 6, 2009, the Bank acquired approximately $1.6 billion in assets, including loans, and $1.2 billion in deposits of the former County Bank, of Merced, California, from the FDIC as its receiver. County Bank s loan portfolio had suffered substantial deterioration over the previous year, and the Company can provide no assurance that it will not continue to deteriorate now that it is part of the Bank s portfolio. If Management s estimates of purchased loan fair values as of February 6, 2009 are higher than ultimate cash flows, the recorded carrying amount of the loans may need to be reduced with a corresponding charge to earnings, net of FDIC loss indemnification.

***Shares of Company common stock eligible for future sale could have a dilutive effect on the market for Company common stock and could adversely affect the market price.***

The Articles of Incorporation of the Company authorize the issuance of 150 million shares of common stock (and two additional classes of 1 million shares each, denominated Class B Common Stock and Preferred Stock , respectively) of which approximately 29.2 million were outstanding at December 31, 2009. Pursuant to its stock option plans, at December 31, 2009, the Company had outstanding options exercisable for 2.1 million shares of common stock. As of December 31, 2009, 3.4 million shares of Company common stock remained available for grants under the Company s stock option plans. Sales of substantial amounts of Company common stock in the public market could adversely affect the market price of its common stock. The Company repurchases and retires its common stock in accordance with Board of Directors-approved share repurchase programs. At December 31, 2009, approximately 2.0 million shares remained available to repurchase under such plans.

***The Company s payment of dividends on common stock could be eliminated or reduced.***

Holders of the Company s common stock are entitled to receive dividends only when, as and if declared by the Company s Board of Directors. Although the Company has historically paid cash dividends on the Company s common stock, the Company is not required to do so and the Company s Board of Directors could reduce or eliminate the Company s common stock dividend in the future.

***The Company could repurchase shares of its common stock at price levels considered excessive.***

The Company has been active in repurchasing and retiring shares of its common stock when alternative uses of excess capital, such as acquisitions, have been limited. The Company could repurchase shares of its common stock at price levels considered excessive, thereby spending more cash on such repurchases as deemed reasonable and effectively retiring fewer shares than would be retired if repurchases were affected at lower prices.

## ITEM 1B. UNRESOLVED STAFF COMMENTS

None

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## ITEM 2. PROPERTIES

**Branch Offices and Facilities**

WAB is engaged in the banking business through 97 offices in 22 counties in Northern and Central California including 14 offices in Fresno County, 11 each in Marin and Sonoma Counties, seven each in Merced, Napa and Stanislaus Counties, five each in Lake, Contra Costa and Solano Counties, four in Kern County, three each in Alameda, Sacramento and Tulare Counties, two each in Mendocino, Nevada, and Placer Counties, and one each in San Francisco, Tuolumne, Kings, Madera, Mariposa and Yolo Counties. WAB believes all of its offices are constructed and equipped to meet prescribed security requirements.

The Company owns 35 branch office locations and one administrative facility and leases 76 facilities. Most of the leases contain multiple renewal options and provisions for rental increases, principally for changes in the cost of living index, property taxes and maintenance.

## ITEM 3. LEGAL PROCEEDINGS

Neither the Company nor any of its subsidiaries is a party to any material pending legal proceeding, nor is their property the subject of any material pending legal proceeding, other than ordinary routine legal proceedings arising in the ordinary course of the Company s business. None of these proceedings is expected to have a material adverse impact upon the Company s business, financial position or results of operations.

## ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

There were no matters submitted to a vote of the shareholders during the fourth quarter of 2009.

# PART II

## ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDERS MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Company s common stock is traded on the NASDAQ Global Select Market ( NASDAQ ) under the symbol WABC . The following table shows the high and the low sales prices for the common stock, for each quarter, as reported by NASDAQ:

| | High | Low |
|---|---|---|
| 2009: | | |
| First quarter | $ 51.29 | $ 33.08 |
| Second quarter | 56.79 | 44.13 |
| Third quarter | 54.70 | 45.42 |
| Fourth quarter | 56.80 | 47.08 |
| 2008: | | |
| First quarter | $ 56.49 | $ 39.00 |
| Second quarter | 61.49 | 50.55 |
| Third quarter | 69.00 | 35.50 |
| Fourth quarter | 60.00 | 41.17 |

As of February 22, 2010, there were approximately 8,000 shareholders of record of the Company s common stock.

The Company has paid cash dividends on its common stock in every quarter since its formation in 1972, and it is currently the intention of the Board of Directors of the Company to continue payment of cash dividends on a quarterly basis. There is no assurance, however, that any dividends will be paid since they are dependent upon earnings, cash balances, financial condition and capital requirements of the Company and its subsidiaries as well as policies of the FRB pursuant to the BHCA. See Item 1, Business Supervision and Regulation. As of December 31, 2009, $133 million was allowable for payment of dividends by the Company to its shareholders, under applicable laws and regulations.

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The notes to the consolidated financial statements included in this report contain additional information regarding the Company s capital levels, regulations affecting subsidiary bank dividends paid to the Company, the Company s earnings, financial condition and cash flows, and cash dividends declared and paid on common stock.

As discussed in Note 9 to the consolidated financial statements, in December 1986, the Company declared a dividend distribution of one common share purchase right (the Right ) for each outstanding share of common stock. The Rights expired on December 31, 2009.

On February 13, 2009, the Company issued to Treasury a warrant to purchase 246,640 shares of its common stock at an exercise price of $50.92 per share.

**Stock performance**

The following chart compares the cumulative return on the Company s stock during the ten years ended December 31, 2009 with the cumulative return on the S&P 500 composite stock index and NASDAQ S Bank Index. The comparison assumes $100 invested in each on December 31, 1999 and reinvestment of all dividends.

| | Period ending | | | | | |
|---|---|---|---|---|---|---|
| | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 |
| Westamerica Bancorporation (WABC) | $ 100.00 | $ 158.30 | $ 148.88 | $ 154.51 | $ 195.77 | $ 234.08 |
| S&P 500 (SPX) | 100.00 | 90.87 | 80.13 | 62.42 | 80.32 | 89.03 |
| NASDAQ Bank Index (CBNK) | 100.00 | 117.79 | 132.49 | 141.69 | 188.51 | 214.20 |

| | Period ending | | | | |
|---|---|---|---|---|---|
| | 2005 | 2006 | 2007 | 2008 | 2009 |
| Westamerica Bancorporation (WABC) | $ 217.94 | $ 213.35 | $ 193.42 | $ 227.75 | $ 253.64 |
| S&P 500 (SPX) | 93.42 | 108.22 | 114.13 | 71.99 | 91.05 |
| NASDAQ Bank Index (CBNK) | 210.05 | 239.16 | 191.78 | 150.57 | 126.02 |

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The following chart compares the cumulative return on the Company s stock during the five years ended December 31, 2009 with the cumulative return on the S&P 500 composite stock index and NASDAQ S Bank Index. The comparison assumes $100 invested in each on December 31, 2004 and reinvestment of all dividends.

| | Period ending | | | | | |
|---|---|---|---|---|---|---|
| | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
| Westamerica Bancorporation (WABC) | $ 100.00 | $ 93.10 | $ 91.14 | $ 82.63 | $ 97.29 | $ 108.36 |
| S&P 500 (SPX) | 100.00 | 104.92 | 121.54 | 128.18 | 80.86 | 102.26 |
| NASDAQ Bank Index (CBNK) | 100.00 | 98.06 | 111.66 | 89.53 | 70.29 | 58.83 |

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**ISSUER PURCHASES OF EQUITY SECURITIES**

The table below sets forth the information with respect to purchases made by or on behalf of Westamerica Bancorporation or any affiliated purchaser (as defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934), of common stock during the quarter ended December 31, 2009 (in thousands, except per share data).

| Period | (a) Total Number of Shares Purchased | (b) Average Price Paid per Share | (c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs* | (d) Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs |
|---|---|---|---|---|
| October 1 through October 31 | 3 | $ 50.65 | 3 | 1,995 |
| November 1 through November 30 | 5 | 51.79 | 5 | 1,990 |
| December 1 through December 31 | 3 | 54.31 | 3 | 1,987 |
| Total | 11 | 52.16 | 11 | 1,987 |

* Includes 3 thousand, 5 thousand and 3 thousand shares purchased in October, November and December, respectively, by the Company in private transactions with the independent administrator of the Company s Tax Deferred Savings/Retirement Plan (ESOP). The Company includes the shares purchased in such transactions within the total number of shares authorized for purchase pursuant to the currently existing publicly announced program.

The Company repurchases shares of its common stock in the open market to optimize the Company s use of equity capital and enhance shareholder value and with the intention of lessening the dilutive impact of issuing new shares to meet stock performance, option plans, and other ongoing requirements.

On February 13, 2009, the Company utilized the Troubled Asset Relief Program and issued 83,726 preferred shares to the United States Treasury at $1,000 per share ( Treasury Preferred Stock ). Under the terms of the Treasury Preferred Stock, share repurchases were limited to repurchase related to employee benefit programs. On September 2, 2009, 41,863 shares of Treasury Preferred Stock were redeemed and on November 18, 2009, the remaining 41,863 shares were redeemed. The redemption of the Treasury Preferred Stock has removed the repurchase limitations.

Shares were repurchased during the fourth quarter of 2009 pursuant to a program approved by the Board of Directors on August 27, 2009 authorizing the purchase of up to 2 million shares of the Company s common stock from time to time prior to September 1, 2010.

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**ITEM 6. SELECTED FINANCIAL DATA**

The following financial information for the five years ended December 31, 2009 has been derived from the Company s Consolidated Financial Statements. This information should be read in conjunction with the Consolidated Financial Statements and related notes thereto included elsewhere herein.

**WESTAMERICA BANCORPORATION**
**FINANCIAL SUMMARY**
*(In thousands, except per share data)*

| *Year ended December 31:* | *2009* | *2008* | *2007* | *2006* | *2005** |
|---|---|---|---|---|---|
| **Interest income** | $ 241,949 | $ 208,469 | $ 235,872 | $ 246,515 | $ 242,797 |
| **Interest expense** | 19,380 | 33,243 | 72,555 | 65,268 | 43,649 |
| **Net interest income** | 222,569 | 175,226 | 163,317 | 181,247 | 199,148 |
| **Provision for loan losses** | 10,500 | 2,700 | 700 | 445 | 900 |
| **Noninterest income:** | | | | | |
| Net losses from securities | | (56,955) | | | (4,903) |
| Gain on acquisition | 48,844 | | | | |
| Deposit service charges and other | 63,167 | 54,899 | 59,278 | 55,347 | 59,443 |
| **Total noninterest income (loss)** | 112,011 | (2,056) | 59,278 | 55,347 | 54,540 |
| **Noninterest expense** | | | | | |
| Visa litigation | | (2,338) | 2,338 | | |
| Other noninterest expense | 140,776 | 103,099 | 99,090 | 101,724 | 107,250 |
| **Total noninterest expense** | 140,776 | 100,761 | 101,428 | 101,724 | 107,250 |
| **Income before income taxes** | 183,304 | 69,709 | 120,467 | 134,425 | 145,538 |
| **Provision for income taxes** | 57,878 | 9,874 | 30,691 | 35,619 | 39,497 |
| **Net income** | 125,426 | 59,835 | 89,776 | 98,806 | 106,041 |
| **Preferred stock dividends and discount accretion** | 3,963 | | | | |
| **Net income applicable to common equity** | $ 121,463 | $ 59,835 | $ 89,776 | $ 98,806 | $ 106,041 |
| **Earnings per share:** | | | | | |
| Basic | $ 4.17 | $ 2.07 | $ 3.02 | $ 3.17 | $ 3.28 |
| Diluted | 4.14 | 2.04 | 2.98 | 3.11 | 3.22 |
| **Per share:** | | | | | |
| Dividends paid | $ 1.41 | $ 1.39 | $ 1.36 | $ 1.30 | $ 1.22 |
| Book value at December 31 | 17.31 | 14.19 | 13.60 | 13.89 | 13.65 |
| **Average common shares outstanding** | 29,105 | 28,892 | 29,753 | 31,202 | 32,291 |
| **Average diluted common shares outstanding** | 29,353 | 29,273 | 30,165 | 31,739 | 32,897 |
| | 29,208 | 28,880 | 29,018 | 30,547 | 31,882 |

| | | | | | |
|---|---|---|---|---|---|
| **Shares outstanding at December 31** | | | | | |
| **At December 31:** | | | | | |
| Non-covered loans, net | $ 2,160,045 | $ 2,337,956 | $ 2,450,470 | $ 2,476,404 | $ 2,616,372 |
| Covered loans | 855,301 | | | | |
| Investments | 1,111,143 | 1,237,779 | 1,578,109 | 1,780,617 | 1,999,604 |
| Intangible assets and goodwill | 157,366 | 136,907 | 140,148 | 143,801 | 148,077 |
| Total assets | 4,975,501 | 4,032,934 | 4,558,959 | 4,769,335 | 5,157,559 |
| Total deposits | 4,060,208 | 3,095,054 | 3,264,790 | 3,516,734 | 3,846,101 |
| Short-term borrowed funds | 227,178 | 457,275 | 798,599 | 731,977 | 775,173 |
| Federal Home Loan Bank advances | 85,470 | | | | |
| Debt financing and notes payable | 26,497 | 26,631 | 36,773 | 36,920 | 40,281 |
| Shareholders equity | 505,448 | 409,852 | 394,603 | 424,235 | 435,064 |
| **Financial Ratios:** | | | | | |
| **For the year:** | | | | | |
| Return on assets | 2.39% | 1.42% | 1.93% | 2.01% | 2.09% |
| Return on common equity | 25.84% | 14.77% | 22.11% | 23.38% | 25.70% |
| Net interest margin ** | 5.42% | 5.13% | 4.40% | 4.57% | 4.82% |
| Net loan losses to average non-covered loans | 0.60% | 0.44% | 0.14% | 0.04% | 0.03% |
| Efficiency ratio *** | 39.74% | 51.88% | 41.46% | 39.12% | 38.52% |
| **At December 31:** | | | | | |
| Equity to assets | 10.16% | 10.16% | 8.66% | 8.90% | 8.44% |
| Total capital to risk-adjusted assets | 14.50% | 11.76% | 10.64% | 11.09% | 10.40% |
| Allowance for loan losses to non-covered loans | 1.86% | 1.87% | 2.10% | 2.19% | 2.09% |

The above financial summary has been derived from the Company s audited consolidated financial statements. This information should be read in conjunction with those statements, notes and the other information included elsewhere herein.

* Adjusted to adopt the revised provisions for accounting for stock compensation.

** Yields on securities and certain loans have been adjusted upward to a fully taxable equivalent ( FTE ) basis, which is a non-GAAP financial measure, in order to reflect the effect of income which is exempt from federal income taxation at the current statutory tax rate.

*** The efficiency ratio is defined as noninterest expense divided by total revenue (net interest income on an FTE basis, which is a non-GAAP financial measure, and noninterest income).

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## ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion addresses information pertaining to the financial condition and results of operations of Westamerica Bancorporation and subsidiaries (the Company ) that may not be otherwise apparent from a review of the consolidated financial statements and related footnotes. It should be read in conjunction with those statements and notes found on pages 52 through 86, as well as with the other information presented throughout the Report.

**Critical Accounting Policies**

The Company s consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States and follow general practices within the banking industry. Application of these principles requires the Company to make certain estimates, assumptions, and judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions, and judgments are based on information available as of the date of the financial statements; accordingly, as this information changes, the financial statements could reflect different estimates, assumptions, and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the financial statements at fair value warrants an impairment writedown or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. The fair values and the information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or are provided by other third-party sources, when available. When third-party information is not available, valuation adjustments are estimated in good faith by Management.

The most significant accounting policies followed by the Company are presented in Note 1 to the consolidated financial statements. These policies, along with the disclosures presented in the other financial statement notes and in this discussion, provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined. Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions, and estimates underlying those amounts, Management has identified the allowance for loan losses accounting and purchased loan accounting to be the accounting areas requiring the most subjective or complex judgments, and as such could be most subject to revision as new information becomes available. A discussion of the factors affecting accounting for the allowance for loan losses and purchased loans is included in the Loan Portfolio Credit Risk discussion below.

**Acquisition**

On February 6, 2009, Westamerica Bank ( Bank ) acquired the banking operations of County Bank ( County ) from the Federal Deposit Insurance Corporation ( FDIC ). The Bank acquired approximately $1.62 billion assets and assumed approximately $1.58 billion liabilities. The Bank and the FDIC entered loss sharing agreements regarding future losses incurred on acquired loans and foreclosed loan collateral. Under the terms of the loss sharing agreements, the FDIC absorbs 80 percent of losses and is entitled to 80 percent of loss recoveries on the first $269 million of losses, and absorbs 95 percent of losses and is entitled to 95 percent of loss recoveries on losses exceeding $269 million. The term for loss sharing on residential real estate loans is ten years, while the term for loss sharing on non-residential real estate loans is five years in respect to losses and eight years in respect to loss recoveries. The County acquisition was accounted for under the acquisition method of accounting in accordance with FASB ASC 805, Business Combinations. The Company recorded a bargain purchase gain totaling $48.8 million resulting from the acquisition, which is a component of noninterest income on the statement of income. The amount of the gain is equal to the amount by which the estimated fair value of assets purchased exceeded the estimated fair value of liabilities assumed. See Note 2 of the Notes to Consolidated Financial Statements for additional information regarding the acquisition.

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## Net Income

For 2009, the Company reported net income applicable to common equity of $121.5 million or $4.14 diluted earnings per common share ( EPS ), compared with net income applicable to common equity of $59.8 million, or $2.04 EPS, for 2008. The 2009 results included a bargain purchase gain of $48.8 million resulting from the acquisition of County and a significant increase in FDIC insurance assessments. Further, the provision for loan losses increased in 2009 due to an increase in net loan losses and Management s assessment of losses inherent in the loan portfolio not covered by FDIC loss-sharing agreements. Operating results related to the acquired County contributed net interest income, loan fees, and noninterest income and required an increase in noninterest expense. In the third quarter 2009, the Company completed systems conversions and branch consolidations related to County, which reduced expense levels. In the first quarter of 2009 the Company issued $83.7 million in preferred stock to the United States Department of the Treasury. The Company redeemed $42 million of the preferred stock on September 2, 2009 and the remaining preferred stock on November 18, 2009. The preferred stock redemption required accelerated preferred stock discount accretion of $1.1 million, which reduced EPS $0.04. Also, in 2009, the Company eliminated $587 thousand in tax reserves due to a lapse in the statute of limitations, which reduced tax provisions and increased EPS $0.02. The 2008 results included a $62.7 million charge for securities losses related to FHLMC and FNMA preferred stock and other common stock. Additionally, results for 2008 included a $5.7 million gain on the sale of VISA common stock from Visa s initial public offering ( IPO ), $2.3 million in reduced expenses as known litigation contingencies were satisfied as a part of the VISA IPO, and approximately $1.0 million reduction in the tax provision primarily due to adjusting the estimated tax provision to actual amounts on the filed 2007 federal tax return. The net securities losses, satisfaction of litigation contingencies, and tax provision adjustment combined to reduce 2008 net income applicable to common equity by $30.7 million or EPS by $1.05.

Components of Net Income

| Year ended December 31,<br>($ in thousands except per share amounts) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Net interest and fee income * | $ 242,218 | $ 196,257 | $ 185,348 |
| Provision for loan losses | (10,500) | (2,700) | (700) |
| Noninterest income (loss) | 112,011 | (2,056) | 59,278 |
| Noninterest expense | (140,776) | (100,761) | (101,428) |
| Income before income taxes * | 202,953 | 90,740 | 142,498 |
| Taxes * | (77,527) | (30,905) | (52,722) |
| Net income | 125,426 | 59,835 | 89,776 |
| Preferred dividends and discount accretion | (3,963) | | |
| Net income applicable to common equity | $ 121,463 | $ 59,835 | $ 89,776 |
| Net income applicable to common equity per average fully-diluted common share | $ 4.14 | $ 2.04 | $ 2.98 |
| Net income applicable to common equity as a percentage of average shareholders equity | 25.84% | 14.77% | 22.11% |
| Net income applicable to common equity as a percentage of average total assets | 2.39% | 1.42% | 1.93% |

* Fully taxable equivalent (FTE)

Comparing 2009 to 2008, net income applicable to common equity increased $61.6 million, due to higher net interest income (FTE), higher service charges on deposit accounts, the bargain purchase gain and the 2008 securities losses and impairment charges, partially offset by increases in the provision for loan losses, noninterest expense and income tax provision (FTE) and the 2008 gain on sale of Visa common stock and reversal of noninterest expense related to Visa litigation contingencies. The higher net interest income (FTE) was mainly generated by loans acquired from County, lower rates paid on interest-bearing deposits and other short-term borrowings, and lower average balances of borrowings, partially offset by lower yields on loans, lower average investments and higher average balances of interest-bearing deposits. The provision for loan losses increased $7.8 million reflecting higher net loan losses and Management s assessment of losses inherent in the loan portfolio not covered by loss-sharing agreements with the FDIC. Noninterest income increased $114.1 million in 2009 compared with 2008 largely due to higher service charges on deposit accounts earned from assumed deposits, the bargain purchase gain and the 2008 securities losses, partially offset by the 2008 gain on Visa common stock and reversal of Visa litigation expense. The income tax provision (FTE) increased $46.6 million due to higher profitability.

Comparing 2008 to 2007, net income decreased $29.9 million, due to securities losses and other than temporary impairment charges on FHLMC and FNMA preferred stock and other common stock and a higher loan loss provision, partially offset by higher net interest income (FTE), a gain on sale of VISA common stock and lower tax provision (FTE). The higher net interest income (FTE) was mainly caused by lower funding costs, partially offset by a lower volume of average interest-earning assets and lower yields on loans. The provision for loan losses increased $2.0 million to reflect higher net loan losses and Management s assessment of credit risk and the appropriate level of the allowance for loan losses. Noninterest income for 2008 resulted in a loss of $2.1 million compared with revenue of $59.3 million in 2007, mainly due to the losses and impairment charges on FHLMC and FNMA preferred stock and other common stock, a $950 thousand decrease in fees on the issuance of official checks and a $822 thousand gain from life insurance proceeds in 2007, partially offset by the $5.7 million gain on sale of VISA common stock. Noninterest expense decreased $667 thousand or 0.7%, primarily the net result of the reversal of a $2.3 million accrual for known Visa related litigation and lower amortization of identifiable intangible assets, partially offset by higher data processing, personnel costs and legal fees. The income tax provision (FTE) decreased $21.8 million in 2008 largely due to lower pretax income and the $1 million adjustment for the filed 2007 federal income tax return.

The Company s return on average total assets was 2.39% in 2009, compared to 1.42% and 1.93% in 2008 and 2007, respectively. Return on average common equity in 2009 was 25.84%, compared to 14.77% and 22.11% in 2008 and 2007, respectively.

**Net Interest Income**

The Company s primary source of revenue is net interest income, or the difference between interest income earned on loans and investment securities and interest expense paid on interest-bearing deposits and other borrowings. Net interest income (FTE) in 2009 increased $46.0 million or 23.4% from 2008, to $242.2 million. Comparing 2008 to 2007, net interest income (FTE) increased $10.9 million or 5.9% from 2007, to $196.3 million.

Components of Net Interest Income

| Year ended December 31,<br>(in thousands) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Interest and fee income | $ 241,949 | $ 208,469 | $ 235,872 |
| Interest expense | (19,380) | (33,243) | (72,555) |
| FTE adjustment | 19,649 | 21,031 | 22,031 |
| Net interest income (FTE) | $ 242,218 | $ 196,257 | $ 185,348 |
| Net interest margin (FTE) | 5.42% | 5.13% | 4.40% |

The Company s net interest margin expanded in 2009 compared with 2008. In 2009, the Company s loan and investment yields were less sensitive to changes in interest rates resulting in a lesser reduction in such yields compared with the rates paid on deposits and other funding sources. The Company s checking and savings deposits represented 74% of total deposits, which limits the Company s reliance on higher-costing time deposits. Declines on rates paid on deposits contributed to reduce the cost of funding as a percentage of earning assets from 0.87% in 2008 to 0.43% in 2009. Offsetting some of the benefit of the expanding margin was the reduction in the level of average interest-earning assets and lower yields on loans.

In Management s opinion, current economic conditions are not conducive for generating profitable loan growth. Weak economic conditions create a cautious view toward commercial lending, and economic pressure on consumers has reduced demand for automobile and other consumer loans. As a result, the Company has not taken an aggressive posture relative to current loan portfolio growth. The Bank has not been actively purchasing investment securities in the current environment. The resulting liquidity has been applied to reduce high-cost and interest-sensitive funding sources.

At December 31, 2009, FDIC covered loans represented 28 percent of the Company s loan portfolio. Under the terms of the FDIC loss-sharing agreements, the FDIC is obligated to reimburse the Bank 80 percent of loan interest income foregone on covered loans. Such reimbursements are limited to the lesser of 90 days contractual interest or actual unpaid contractual interest at the time a principal loss is recognized in respect to the underlying loan.

The growth in the average earning assets in 2009 compared with 2008 was attributable to the acquisition of County loans from the FDIC. The average balance of such loans for 2009 was $897.9 million. Average earning assets increased $650.0 million or 17.0% for 2009 compared with 2008. A $794.4 million increase in the average balance of the loan portfolio was attributable to increases in average balances of commercial real estate loans (up $447.2 million), taxable commercial loans (up $311.0 million) and consumer loans (up $91.0 million), partially offset by a $36.2 million decrease in the average balance of residential real estate loans and a $21.9 million decrease in the average balance of tax-exempt commercial loans. The acquired County loan portfolio did not contain significant volumes of tax-exempt commercial loans or residential real estate loans. Average investments decreased by $144.4 million due to declines in the average balances of U.S. government sponsored entity obligations (down $108.8 million), municipal securities (down $20.3 million) and a $41.9 million decline in average balances of FHLMC and FNMA stock resulting from the impairment charge in 2008, partially offset by a $18.7 million increase in the average balance of mortgage backed securities and collateralized mortgage obligations.

The average yield on earning assets in 2009 was 5.85% compared with 6.00% in 2008. The loan portfolio yield in 2009 compared with 2008 was lower by 29 basis points ( bp ), due to decreases in yields on taxable commercial loans (down 124 bp), commercial real estate loans (down 47 bp) and real estate construction loans (down 234 bp), partially offset by consumer loans (up 13 bp) and tax-exempt commercial loans (up 12 bp). The investment portfolio yield decreased by 6 bp. The decrease resulted from an 11 bp decline in yields on mortgage backed securities and collateralized mortgage obligations and a 492 bp decline in yields on corporate and other securities which was affected primarily by suspended dividends on FHLMC and FNMA preferred stock, partially offset by higher yields on U.S. government sponsored entity obligations (up 4 bp).

Comparing 2009 with 2008, interest expense decreased $13.9 million due to lower rates paid, lower average balances of short-term borrowings and higher levels of shareholders equity, offset in part by higher average balances of interest-bearing deposits. Average interest-bearing liabilities in 2009 rose by $568.1 million or 22.1% over 2008 mainly through the County acquisition. A $729.1 million growth in interest-bearing deposits was mostly attributable to increases in average balances of CDs less than $100 thousand (up $264.2 million), CDs over $100 thousand (up $118.3 million), money market checking accounts (up $154.9 million), money market savings (up $125.0 million) and regular savings (up $72.4 million). Short-term borrowings decreased $153.7 million, mainly the net result of lower average balances of federal funds purchased (down $303.8 million) and sweep accounts (down $13.2 million), partially offset by higher average balances of repurchase agreements (up $86.6 million) and FHLB advances (up $79.4 million). Average balances of long-term debt also declined $7.2 million. Rates paid on interest-bearing liabilities averaged 0.62% in 2009 compared with 1.29% in 2008. The average rate paid on interest-bearing deposits declined 53 bp to 0.54% in 2009 mainly due to lower rates on CDs less than $100 thousand (down 171 bp), CDs over $100 thousand (down 123 bp) and preferred money market savings (down 94 bp). Rates on short-term borrowings were also lower by 102 bp largely due to federal funds (down 199 bp) and repurchase agreements (down 126 bp).

The Company s net interest margin expanded in 2008 compared with 2007. The Federal Reserve s Open Market Committee (FOMC) reduced the target federal funds rate from 5.25% in August 2007 to between zero and 0.25% in December 2008 in ten increments. As a result, short-term interest rates declined and the Company managed to reduce the interest rates paid on deposits and other interest-bearing liabilities during 2008 compared with 2007. In 2008, the Company s loan and investment yields were less sensitive to changes in interest rates resulting in a lesser reduction in such yields compared with the rates paid on deposits and other funding sources. Offsetting some of the benefit of the expanding margin was the reduction in the level of average interest-earning assets and lower yields on loans resulting in a reduction of interest and fee income (FTE) of $28.4 million or 11.0% in 2008 relative to 2007.

Comparing 2008 with 2007, average earning assets decreased $390.8 million or 9.3% in 2008 compared with 2007, due to a $311.6 million decline in the investment portfolio and a $79.2 million decrease in the loan portfolio. Lower average investment balances were largely attributable to U.S. government sponsored entity obligations (down $138 million), mortgage backed securities and collateralized mortgage obligations (down $105 million), municipal securities (down $41 million) and corporate and other securities (down $30 million). The average balance of corporate and other securities declined largely due to sales and impairment of FHLMC and FNMA preferred stock. The loan portfolio decline was primarily due to decreases in the average balances of commercial real estate loans (down $44 million), residential real estate loans (down $25 million), tax-exempt commercial loans (down $17 million), partly offset by an $8 million increase in the average balance of consumer loans, primarily automobile loans.

The average yield on the Company s earning assets decreased from 6.12% in 2007 to 6.00% in 2008. The composite yield on loans fell 35 bp to 6.30% due to decreases in yields on taxable commercial loans (down 155 bp), real estate construction loans (down 332 bp), consumer loans (down 21 bp) and commercial real estate loans (down 9 bp), partially offset by higher yields on tax-exempt commercial loans (up 10 bp) and residential real estate loans (up 10 bp). Real estate construction loans, commercial lines of credit and consumer lines of credit have variable interest rates based on the prime lending rate. The prime lending rate averaged 8.11% in 2007 compared to 5.70% in 2008; the decrease reduced the yields earned on real estate construction loans, commercial lines of credit and consumer lines of credit. The investment portfolio yield increased 14 bp to 5.48%, mainly due to higher yields on U.S. Government sponsored entity obligations (up 9 bp), mortgage backed securities and collateralized mortgage obligations (up 6 bp) and municipal securities (up 5 bp), partially offset by corporate and other securities (down 105 bp). Other securities yields declined mostly due to reduced dividends on FHLMC and FNMA preferred stock. As investment portfolio balances have declined, municipal security balances have declined at a slower rate than the remainder of the investment portfolio. As a result, average municipal securities represented 52% of total average investment security balances during 2008, compared with 45% during 2007. This migration in the composition of the investment portfolio improved the overall yield of the investment portfolio since municipal security yields exceed the yield of the overall investment portfolio.

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Interest expense in 2008 decreased $39.3 million or 54.2% compared with 2007. The decrease was attributable to lower rates paid on the interest-bearing liabilities and lower average balances of those liabilities. The average rate paid on interest-bearing liabilities decreased from 2.50% in 2007 to 1.29% in 2008. Rates paid on most interest-bearing liabilities moved with general market conditions. Rates on deposits decreased 72 bp to 1.07% primarily due to decreases in rates paid on CDs over $100 thousand (down 239 bp), preferred money market savings (down 121 bp) and retail CDs (down 62 bp). Rates on short-term borrowings also decreased 246 bp mostly due to lower rates on federal funds purchased (down 296 bp) and line of credit and repurchase facilities (down 189 bp). Interest-bearing liabilities declined $337.4 million or 11.6% in 2008 over 2007. Short-term borrowings declined $210 million primarily due to a $185 million decrease in federal funds purchased. Most categories of deposits declined including money market savings (down $68 million), money market checking accounts (down $28 million), regular savings (down $18 million), Retail CDs (down $16 million) and CDs over $100 thousand (down $14 million). The decline was partially offset by a $20 million increase in preferred money market savings.

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The following tables present information regarding the consolidated average assets, liabilities and shareholders equity, the amounts of interest income earned from average earning assets and the resulting yields, and the amount of interest expense paid on average interest-bearing liabilities and the resulting rates paid. Average loan balances include nonperforming loans. Interest income includes proceeds from loans on nonaccrual status only to the extent cash payments have been received and applied as interest income. Yields on securities and certain loans have been adjusted upward to reflect the effect of income exempt from federal income taxation at the current statutory tax rate.

Distribution of Assets, Liabilities & Shareholders Equity and Yields, Rates & Interest Margin

| | Year Ended December 31, 2009 | | |
|---|---|---|---|
| (dollars in thousands) | Average Balance | Interest Income/ Expense | Rates Earned/ Paid |
| Assets | | | |
| Money market assets and funds sold | $ 841 | $ 3 | 0.36% |
| Investment securities: | | | |
| Available for sale | | | |
| Taxable | 240,829 | 9,002 | 3.74% |
| Tax-exempt (1) | 166,669 | 11,217 | 6.73% |
| Held to maturity | | | |
| Taxable | 307,763 | 13,971 | 4.54% |
| Tax-exempt (1) | 529,597 | 33,334 | 6.29% |
| Loans: | | | |
| Commercial | | | |
| Taxable | 629,027 | 36,360 | 5.78% |
| Tax-exempt (1) | 186,295 | 12,362 | 6.64% |
| Commercial real estate | 1,283,114 | 84,473 | 6.58% |
| Real estate construction | 79,425 | 3,213 | 4.05% |
| Real estate residential | 431,931 | 20,640 | 4.73% |
| Consumer | 617,169 | 37,023 | 6.00% |
| Total Loans (1) | 3,226,961 | 194,071 | 6.01% |
| Earning assets (1) | 4,472,660 | 261,598 | 5.85% |
| Other assets | 613,977 | | |
| Total assets | $ 5,086,637 | | |
| Liabilities and shareholders equity | | | |
| Deposits: | | | |
| Noninterest bearing demand | $ 1,354,534 | | |
| Savings and interest-bearing transaction | 1,648,095 | 4,677 | 0.28% |
| Time less than $100,000 | 458,117 | 4,506 | 0.98% |
| Time $100,000 or more | 607,642 | 5,366 | 0.88% |
| Total interest-bearing deposits | 2,713,854 | 14,549 | 0.54% |
| Short-term borrowed funds | 395,723 | 3,142 | 0.79% |
| Debt financing and notes payable | 26,567 | 1,689 | 6.36% |
| Total interest-bearing liabilities | 3,136,144 | 19,380 | 0.62% |

| | | | |
|---|---|---|---|
| Other liabilities | 71,635 | | |
| Shareholders equity | 524,324 | | |
| Total liabilities and shareholders equity | $ 5,086,637 | | |
| Net interest spread (2) | | | 5.23% |
| Net interest income and interest margin (1)(3) | | $ 242,218 | 5.42% |

(1) Amounts calculated on a fully taxable equivalent basis using the current statutory federal tax rate.

(2) Net interest spread represents the average yield earned on interest-earning assets less the average rate paid on interest-bearing liabilities.

(3) Net interest margin is computed by dividing net interest income by total average earning assets.

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Distribution of Assets, Liabilities & Shareholders Equity and Yields, Rates & Interest Margin

| | Year Ended December 31, 2008 | | |
|---|---|---|---|
| (dollars in thousands) | Average Balance | Interest Income/ Expense | Rates Earned/ Paid |
| Assets | | | |
| Money market assets and funds sold | $ 817 | $ 3 | 0.37% |
| Investment securities: | | | |
| Available for sale | | | |
| Taxable | 205,138 | 8,854 | 4.32% |
| Tax-exempt (1) | 196,993 | 13,795 | 7.00% |
| Held to maturity | | | |
| Taxable | 436,041 | 19,237 | 4.41% |
| Tax-exempt (1) | 551,120 | 34,328 | 6.23% |
| Loans: | | | |
| Commercial | | | |
| Taxable | 318,075 | 22,341 | 7.02% |
| Tax-exempt (1) | 208,155 | 13,575 | 6.52% |
| Commercial real estate | 835,925 | 58,913 | 7.05% |
| Real estate construction | 76,086 | 4,863 | 6.39% |
| Real estate residential | 468,140 | 22,683 | 4.85% |
| Consumer | 526,175 | 30,908 | 5.87% |
| Total Loans (1) | 2,432,556 | 153,283 | 6.30% |
| Earning assets (1) | 3,822,665 | 229,500 | 6.00% |
| Other assets | 397,098 | | |
| Total assets | $ 4,219,763 | | |
| Liabilities and shareholders equity | | | |
| Deposits: | | | |
| Noninterest bearing demand | $ 1,181,679 | | |
| Savings and interest-bearing transaction | 1,301,556 | 5,642 | 0.43% |
| Time less than $100,000 | 193,889 | 5,209 | 2.69% |
| Time $100,000 or more | 489,326 | 10,331 | 2.11% |
| Total interest-bearing deposits | 1,984,771 | 21,182 | 1.07% |
| Short-term borrowed funds | 549,438 | 9,958 | 1.81% |
| Debt financing and notes payable | 33,807 | 2,103 | 6.22% |
| Total interest-bearing liabilities | 2,568,016 | 33,243 | 1.29% |
| Other liabilities | 64,992 | | |
| Shareholders equity | 405,076 | | |
| Total liabilities and shareholders equity | $ 4,219,763 | | |
| Net interest spread (2) | | | 4.71% |

| | | |
|---|---|---|
| Net interest income and interest margin (1)(3) | $ 196,257 | 5.13% |

(1) Amounts calculated on a fully taxable equivalent basis using the current statutory federal tax rate.

(2) Net interest spread represents the average yield earned on interest-earning assets less the average rate paid on interest-bearing liabilities.

(3) Net interest margin is computed by dividing net interest income by total average earning assets.

Distribution of Assets, Liabilities & Shareholders Equity and Yields, Rates & Interest Margin

| | Year Ended December 31, 2007 | | |
|---|---|---|---|
| (dollars in thousands) | Average Balance | Interest Income/ Expense | Rates Earned/ Paid |
| Assets | | | |
| Money market assets and funds sold | $ 671 | $ 7 | 1.04% |
| Investment securities: | | | |
| Available for sale | | | |
| Taxable | 361,851 | 15,639 | 4.32% |
| Tax-exempt (1) | 232,047 | 16,888 | 7.28% |
| Held to maturity | | | |
| Taxable | 538,089 | 23,361 | 4.34% |
| Tax-exempt (1) | 569,090 | 34,973 | 6.15% |
| Loans: | | | |
| Commercial | | | |
| Taxable | 314,428 | 26,936 | 8.57% |
| Tax-exempt (1) | 225,320 | 14,469 | 6.42% |
| Commercial real estate | 879,952 | 62,833 | 7.14% |
| Real estate construction | 81,093 | 7,878 | 9.71% |
| Real estate residential | 493,126 | 23,422 | 4.75% |
| Consumer | 517,844 | 31,497 | 6.08% |
| Total Loans (1) | 2,511,763 | 167,035 | 6.65% |
| Earning assets (1) | 4,213,511 | 257,903 | 6.12% |
| Other assets | 427,949 | | |
| Total assets | $ 4,641,460 | | |
| Liabilities and shareholders equity | | | |
| Deposits: | | | |
| Noninterest bearing demand | $ 1,262,723 | | |
| Savings and interest-bearing transaction | 1,395,622 | 8,237 | 0.59% |
| Time less than $100,000 | 210,039 | 6,956 | 3.31% |
| Time $100,000 or more | 503,469 | 22,656 | 4.50% |
| Total interest-bearing deposits | 2,109,130 | 37,849 | 1.79% |
| Short-term borrowed funds | 759,390 | 32,393 | 4.27% |
| Debt financing and notes payable | 36,850 | 2,313 | 6.28% |
| Total interest-bearing liabilities | 2,905,370 | 72,555 | 2.50% |
| Other liabilities | 67,339 | | |
| Shareholders equity | 406,028 | | |
| Total liabilities and shareholders equity | $ 4,641,460 | | |
| Net interest spread (2) | | | 3.62% |

| | | |
|---|---|---|
| Net interest income and interest margin (1)(3) | $ 185,348 | 4.40% |

(1) Amounts calculated on a fully taxable equivalent basis using the current statutory federal tax rate.

(2) Net interest spread represents the average yield earned on interest-earning assets less the average rate paid on interest-bearing liabilities.

(3) Net interest margin is computed by dividing net interest income by total average earning assets.

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The following tables set forth a summary of the changes in interest income and interest expense due to changes in average assets and liability balances (volume) and changes in average interest rates for the periods indicated. Changes not solely attributable to volume or rates have been allocated in proportion to the respective volume and rate components.

Summary of Changes in Interest Income and Expense

| Years Ended December 31, | 2009 Compared with 2008 | | |
|---|---|---|---|
| (dollars in thousands) | Volume | Rate | Total |
| Increase (decrease) in interest and fee income: | | | |
| Money market assets and funds sold | $ | $ | $ |
| Investment securities: | | | |
| Available for sale Taxable | 1,412 | (1,264) | 148 |
| Tax-exempt (1) | (2,063) | (515) | (2,578) |
| Held to maturity Taxable | (5,812) | 546 | (5,266) |
| Tax-exempt (1) | (1,370) | 376 | (994) |
| Loans: | | | |
| Commercial: | | | |
| Taxable | 18,549 | (4,530) | 14,019 |
| Tax-exempt (1) | (1,452) | 239 | (1,213) |
| Commercial real estate | 29,641 | (4,081) | 25,560 |
| Real estate construction | 197 | (1,847) | (1,650) |
| Real estate residential | (1,742) | (301) | (2,043) |
| Consumer | 5,435 | 680 | 6,115 |
| Total loans (1) | 50,628 | (9,840) | 40,788 |
| Total increase (decrease) in interest and fee income (1) | 42,795 | (10,697) | 32,098 |
| Increase (decrease) in interest expense: | | | |
| Deposits: | | | |
| Savings/ interest-bearing | 1,268 | (2,233) | (965) |
| Time less than $100,000 | 4,022 | (4,725) | (703) |
| Time $100,000 or more | 2,059 | (7,024) | (4,965) |
| Total interest-bearing | 7,349 | (13,982) | (6,633) |
| Short-term borrowed funds | (2,270) | (4,546) | (6,816) |
| Notes and mortgages payable | (460) | 46 | (414) |
| Total increase (decrease) in interest expense | 4,619 | (18,482) | (13,863) |
| Increase in net interest income (1) | $ 38,176 | $ 7,785 | $ 45,961 |

(1) Amounts calculated on a fully taxable equivalent basis using the current statutory federal tax rate.

Summary of Changes in Interest Income and Expense

| Years Ended December 31, | 2008 Compared with 2007 | | |
|---|---|---|---|
| (dollars in thousands) | Volume | Rate | Total |
| Increase (decrease) in interest and fee income: | | | |
| Money market assets and funds sold | $ 1 | $ (5) | $ (4) |
| Investment securities: | | | |
| Available for sale Taxable | (6,764) | (21) | (6,785) |
| Tax-exempt (1) | (2,466) | (627) | (3,093) |
| Held to maturity Taxable | (4,492) | 368 | (4,124) |
| Tax-exempt (1) | (1,088) | 443 | (645) |
| Loans: | | | |
| Commercial: | | | |
| Taxable | 365 | (4,960) | (4,595) |
| Tax-exempt (1) | (1,110) | 216 | (894) |
| Commercial real estate | (3,079) | (841) | (3,920) |
| Real estate construction | (449) | (2,566) | (3,015) |
| Real estate residential | (1,187) | 448 | (739) |
| Consumer | 555 | (1,144) | (589) |
| Total loans (1) | (4,905) | (8,847) | (13,752) |
| Total decrease in interest and fee income (1) | (19,714) | (8,689) | (28,403) |
| Decrease in interest expense: | | | |
| Deposits: | | | |
| Savings/ interest-bearing | (512) | (2,083) | (2,595) |
| Time less than $100,000 | (495) | (1,252) | (1,747) |
| Time $100,000 or more | (592) | (11,733) | (12,325) |
| Total interest-bearing | (1,599) | (15,068) | (16,667) |
| Short-term borrowed funds | (7,262) | (15,173) | (22,435) |
| Notes and mortgages payable | (189) | (21) | (210) |
| Total decrease in interest expense | (9,050) | (30,262) | (39,312) |
| (Decrease) increase in net interest income (1) | $ (10,664) | $ 21,573 | $ 10,909 |

(1) Amounts calculated on a fully taxable equivalent basis using the current statutory federal tax rate.

**Provision for Loan Losses**

The Company manages credit costs by consistently enforcing conservative underwriting and administration procedures and aggressively pursuing collection efforts with troubled debtors. County loans purchased from the FDIC are covered by loss-sharing agreements the Company entered into with the FDIC. Further, the Company recorded the purchased County loans at estimated fair value upon acquisition as of February 6, 2009. Due to the loss-sharing agreements and February 6, 2009 fair value recognition, the Company did not record a provision for loan losses during 2009 related to covered loans. In 2009, the provision for loan losses was $10.5 million, compared to $2.7 million for 2008, and $700 thousand for 2007. The provision reflects Management s assessment of credit risk in the loan portfolio for each of the periods presented. For further information regarding credit risk, the FDIC loss-sharing agreements, net credit losses and the allowance for loan losses, see the Loan Portfolio Credit Risk and Allowance for Credit Losses sections of this report.

**Noninterest Income**

Components of Noninterest Income

| Years Ended December 31, (dollars in thousands) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Service charges on deposit accounts | $ 36,392 | $ 29,762 | $ 30,235 |
| Merchant credit card fees | 9,068 | 10,525 | 10,841 |
| Debit card fees | 4,875 | 3,769 | 3,797 |
| ATM fees and interchange | 3,693 | 2,923 | 2,824 |
| Other service charges | 2,200 | 2,025 | 2,065 |
| Trust fees | 1,429 | 1,227 | 1,281 |
| Check sale income | 887 | 736 | 818 |
| Safe deposit rental | 697 | 593 | 624 |
| Financial services commissions | 583 | 830 | 1,321 |
| Official check sale income | 89 | 163 | 1,113 |
| Gain on acquisition | 48,844 | | |
| Life insurance proceeds | | | 822 |
| Gain on sales of real property | | | 230 |
| Securities losses and impairment | | (62,653) | |
| Gain on sale of Visa common stock | | 5,698 | |
| Other noninterest income | 3,254 | 2,346 | 3,307 |
| Total | $ 112,011 | $ (2,056) | $ 59,278 |

In 2009, noninterest income was $112.0 million compared with a noninterest loss of $2.1 million in 2008 primarily due to a $48.8 million gain on acquisition and a $6.6 million or 22.3% increase in service charges on deposit accounts in 2009 and because noninterest income in 2008 was reduced by $59.4 million in losses on sale and other than temporary impairment charges on FHLMC and FNMA preferred stock. Higher service charges on deposit accounts were attributable to growth in deposit accounts through the County acquisition in February 2009. Debit card fees and ATM fees and interchange income increased $1.1 million or 29.3% and $770 thousand or 26.3%, respectively, mainly due to an increased customer base through the County acquisition. Other noninterest income increased $908 thousand largely due to $938 thousand in miscellaneous income from County operations. Merchant credit card income declined $1.5 million or 13.8% primarily due to lower transaction volume and the impact of prevailing economic conditions on consumer spending. The County acquisition was accounted for under the acquisition method of accounting. The purchased assets and assumed liabilities were recorded at their acquisition date fair values, and identifiable intangible assets were recorded at fair value. The gain on acquisition totaling $48.8 million resulted from the amount by which the fair value of assets purchased exceeded the fair value of liabilities assumed. Offsetting the increase was a $5.7 million gain on sale of Visa common stock in 2008 and a $247 thousand decrease in financial services commissions.

In 2008, a $2.1 million loss was recorded from all sources of noninterest income compared with $59.3 million in noninterest income for 2007. The 2008 period included the $62.7 million in losses on sale and impairment charge of FHLMC and FNMA preferred stock and other common stock and $5.7 million in securities gains from the redemption of VISA Class B common stock as part of Visa s initial public offering. Noninterest income in 2007 included an $822 thousand gain on company-owned life insurance and a $230 thousand gain on sale of real property. During the second quarter of 2008, the Company began issuing its own official checks rather than use a vendor which paid the Company fees based on the availability of funds while the official checks remained outstanding ( float ). By issuing its own official checks, the Company uses the related float as a source of funding and reduces its interest expense. Such vendor fees were $950 thousand lower in 2008 compared with 2007. Financial services commissions fell $491 thousand or 37.2%. Service charges on deposits declined $473 thousand or 1.6%, due to declines in overdraft fees and returned item charges (down $492 thousand) and fees charged on business and retail checking and savings accounts (down $542 thousand), partially offset by a $562 thousand increase in deficit fees charged on analyzed accounts. Deficit fees are service charges collected from business customers that typically pay for such services with compensating balances. Merchant credit card fees declined $316 thousand or 2.9%. Other noninterest income decreased $1.1 million or 23.2% primarily due to a $292 thousand decline in interest recoveries on charged-off loans and lower customer check sales income and gains on sale of other assets in 2007.

**Noninterest Expense**

Components of Noninterest Expense

| Years Ended December 31, (dollars in thousands) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Salaries and related benefits | $ 65,391 | $ 51,492 | $ 50,142 |
| Occupancy | 18,748 | 13,703 | 13,346 |
| Outsourced data processing | 9,000 | 8,440 | 7,069 |
| Amortization of intangible assets | 6,697 | 3,221 | 3,653 |
| FDIC insurance assessments | 6,260 | 518 | 401 |
| Equipment | 5,859 | 3,801 | 4,302 |
| Courier Service | 3,808 | 3,322 | 3,404 |
| Professional fees | 3,583 | 2,624 | 1,889 |
| Postage | 2,110 | 1,487 | 1,602 |
| Loan expenses | 2,031 | 911 | 750 |
| Telephone | 1,977 | 1,368 | 1,398 |
| Stationery and supplies | 1,555 | 1,170 | 1,271 |
| In-house meetings | 1,177 | 837 | 749 |
| Correspondent service charges | 1,072 | 634 | 869 |
| Advertising and public relations | 995 | 843 | 834 |
| Operational losses | 953 | 845 | 793 |
| Customer checks | 749 | 920 | 939 |
| Visa litigation | | (2,338) | 2,338 |
| Other | 8,811 | 6,963 | 5,679 |
| Total | $ 140,776 | $ 100,761 | $ 101,428 |
| Noninterest expense to revenues ( efficiency ratio )(FTE) | 39.7% | 51.9% | 41.5% |
| Average full-time equivalent staff | 1,115 | 891 | 887 |
| Total average assets per full-time staff | $ 4,562 | $ 4,736 | $ 5,233 |

Noninterest expense increased $40.0 million or 39.7% in 2009 compared with 2008 mainly due to acquisition related incremental costs, higher FDIC insurance assessments costs and the reversal of a $2.3 million accrual for Visa related litigation in 2008. Branch consolidations and system integrations in August 2009 contributed to lowering acquisition related costs. Salaries and related benefits increased $13.9 million or 27.0% primarily due to personnel costs related to the County acquisition. Occupancy expense increased $5.0 million or 36.8% mainly due to rent and maintenance costs for County s branches. Equipment expense increased $2.1 million primarily due to additional expenses for former County branches. FDIC insurance assessments increased from $517 thousand in 2008 to $6.3 million in 2009. Amortization of deposit intangibles increased $3.5 million due to amortization of the core deposit intangible asset recognized for the assumed County deposit base. Professional fees increased $959 thousand generally due to higher legal and other professional fees. Postage increased $623 thousand mainly due to mailings of welcome packages and branch consolidation notices to former County customers. Stationary and supplies expense increased $385 thousand mostly due to printing welcome packages and branch consolidation notices to customers and supplying former County branches with Westamerica forms. Loan expense increased $1.1 million due to the County acquisition. Other categories of expenses increased due to the acquisition including outsourced data processing services expense (up $560 thousand), courier services (up $486 thousand), telephone expense (up $609 thousand), correspondent service charges (up $438 thousand), in-house meeting expense (up $340 thousand), operational losses (up $108 thousand) and advertising and public relations expenses (up $152 thousand). Other miscellaneous noninterest expense also increased $1.8 million mainly due to a $682 thousand increase in low income housing investment amortization, a $495 thousand increase in ATM and debit card network fees and insurance costs (up $176 thousand), partially offset by a $200 thousand lower provision for unfunded loan commitments. Under the terms of the FDIC loss-sharing agreements related to County, the Bank receives reimbursement from the FDIC for collection and operating costs related to covered assets on which a loss has been recognized. FDIC expense reimbursements reduce the Bank s overall cost of collection of covered assets.

In 2008, noninterest expense decreased $667 thousand or 0.7% compared with 2007. The 2008 results included reversal of the $2.3 million accrual for known Visa related litigation, which was reversed with the funding of a litigation escrow as a part of the Visa IPO. Data processing service costs were higher by $1.4 million or 19.4% due to conversion of the Company s item processing function to an outside vendor. Salaries and related benefits increased $1.4 million or 2.7% mainly due to annual merit increases granted to continuing staff and increases in incentives, payroll taxes and workers compensation. Professional fees increased $735 thousand or 38.9% primarily due to higher legal fees, partially offset by lower audit fees. Occupancy costs increased $357 thousand or 2.7% primarily due to increases in net rent and miscellaneous occupancy expense, partially offset by lower depreciation costs. Loan expenses increased $161 thousand or 21.5%. FDIC insurance assessments increased $117 thousand or 29.2%. Other noninterest expense rose by $1.4 million or 21.3% due to writedown of foreclosed property, higher insurance costs and amortization of low-income housing investments as tax benefits are realized. Other categories of expense decreased from 2007, offsetting the increases outlined above. Equipment expense declined $501 thousand or 11.6% mostly due to reduced depreciation costs and lower maintenance expenses. Amortization of intangible assets decreased $432 thousand or 11.8%. Correspondent service charges were lower by $235 thousand or 27.0%. Postage declined $115 thousand or 7.2%. Stationery and supplies expenses were lower by $101 thousand or 7.9%.

**Provision for Income Tax**

The income tax provision (FTE) was $77.5 million in 2009 compared with $30.9 million in 2008. The increase in pretax earnings was greater than the increase in the preference items. As such, the 2009 effective tax rate was 38.2% compared with 34.1% in 2008. The tax provision in 2009 included a $587 thousand reduction in income tax provision as the Company reversed tax reserves for uncertain tax positions upon the expiration of the statute of limitations for the 2005 federal return. In 2008, the Company filed its 2007 federal income tax return. Amounts included in that filed return were reconciled to estimates of such amounts used to recognize the 2007 federal income tax provision. As a result, a reduction in the tax provision in the amount of $877 thousand was recognized in 2008 to adjust the 2007 tax estimates to amounts included in the filed tax return. The adjustment primarily resulted from higher than anticipated tax credits earned on limited partnership investments providing low-income housing and housing for the elderly in our Northern and Central California communities. In 2008, the Company further reduced its tax provision by $114 thousand to reflect a reduction in its unrecognized tax benefits due to a lapse in the statute of limitations.

The income tax provision (FTE) was $30.9 million for 2008 compared with $52.7 million for 2007. The effective tax rate (FTE) of 34.1% for 2008 compared with 37.0% for 2007. The tax provision for 2007 reflected the tax-free nature of $822 thousand in life insurance proceeds, higher dividend received deductions and lower non-deductible life insurance premiums.

The Emergency Economic Stabilization Act, signed into law on October 3, 2008, provided ordinary tax treatment to losses on FHLMC and FNMA preferred stock held on September 6, 2008 or sold on or after January 1, 2008. As a result, the Company s losses on FNMA and FHLMC preferred stock receive ordinary tax treatment for federal tax purposes. The State of California categorizes these losses as capital losses.

**Investment Portfolio**

The Company maintains a securities portfolio consisting of securities issued by U.S. Government sponsored entities, state and political subdivisions, and asset-backed and other securities. Investment securities are held in safekeeping by an independent custodian.

Investment securities assigned to the available for sale portfolio are generally used to supplement the Company s liquidity, provide a prudent yield, and provide collateral for public deposits and other borrowing facilities. Unrealized net gains and losses on available for sale securities are recorded as an adjustment to equity, net of taxes, but are not reflected in the current earnings of the Company. If Management determines depreciation in any available for sale security is other than temporary, a securities loss will be recognized as a charge to earnings. If a security is sold, any gain or loss is recorded as a credit or charge to earnings and the equity adjustment is reversed. At December 31, 2009, the Company held $384.2 million in securities classified as investments available for sale with a duration of 2.9 years. At December 31, 2009, an unrealized gain of $6.9 million, net of taxes of $4.0 million, related to these securities, was included in shareholders equity.

Securities assigned to the held to maturity portfolio earn a prudent yield, provide liquidity from maturities and paydowns, and provide collateral to pledge for federal, state and local government deposits and other borrowing facilities. The held to maturity investment portfolio had a duration of 3.0 years at December 31, 2009 and, on the same date, those investments included $704.9 million in fixed-rate and $22.0 million in adjustable-rate securities. If Management determines depreciation in any held to maturity security is other than temporary, a securities loss will be recognized as a charge to earnings.

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The Company had no trading securities at December 31, 2009, 2008 and 2007.
For more information on investment securities, see the notes accompanying the consolidated financial statements.
The following table shows the fair value carrying amount of the Company s investment securities available for sale as of the dates indicated:

**Available for Sale Portfolio**

| At December 31, (dollars in thousands) | 2009 | 2008 | 2007 |
|---|---|---|---|
| U.S. Treasury securities | $ 2,987 | $ 3,082 | $ |
| Securities of U.S. Government sponsored entities | 21,041 | 11,077 | 123,062 |
| Mortgage backed securities | 146,005 | 41,240 | 68,393 |
| Obligations of States and political subdivisions | 158,193 | 161,046 | 183,307 |
| Collateralized mortgage obligations | 41,410 | 59,851 | 90,986 |
| Asset-backed securities | 8,339 | 6,447 | 9,700 |
| FHLMC and FNMA stock | 1,573 | 821 | 49,671 |
| Other | 4,660 | 4,890 | 7,702 |
| Total | $ 384,208 | $ 288,454 | $ 532,821 |

The increase in mortgage backed securities from 2008 to 2009 was primarily due to $130 million in County mortgage backed securities purchased from the FDIC, partially reduced by paydowns.
The following table sets forth the relative maturities and contractual yields of the Company s available for sale securities (stated at fair value) at December 31, 2009. Yields on state and political subdivision securities have been calculated on a fully taxable equivalent basis using the current federal statutory rate.
Available for Sale Maturity Distribution

| At December 31, 2009, (Dollars in thousands) | Within one year | After one but within five years | After five but within ten years | After ten years | Mortgage-backed | Other | Total |
|---|---|---|---|---|---|---|---|
| U.S. Treasury securities | $ 2,987 | $ | $ | $ | $ | $ | $ 2,987 |
| Interest rate | 0.44% | % | % | % | % | % | 0.44% |
| U.S. Government sponsored entities | | 19,980 | 1,061 | | | | 21,041 |
| Interest rate | | 1.85% | 5.28% | | | | 2.02% |
| States and political subdivisions | 9,865 | 68,780 | 61,871 | 17,677 | | | 158,193 |
| Interest rate (FTE) | 7.11% | 7.06% | 6.88% | 6.46% | | | 6.98% |
| Asset-backed securities | | | | 8,339 | | | 8,339 |
| Interest rate | | | | 0.49% | | | 0.49% |
| Subtotal | 12,852 | 88,760 | 62,932 | 26,016 | | | 190,560 |
| Interest rate | 5.56% | 5.89% | 6.85% | 4.55% | | | 6.05% |
| Mortgage backed securities and collateralized mortgage obligations | | | | | 187,415 | | 187,415 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Interest rate | | | | | 4.28% | | 4.28% |
| Other without set maturities | | | | | | 6,233 | 6,233 |
| Interest rate | | | | | | 5.58% | 5.58% |
| Total | $ 12,852 | $ 88,760 | $ 62,932 | $ 26,016 | $ 187,415 | $ 6,233 | $ 384,208 |
| Interest rate | 5.56% | 5.89% | 6.85% | 4.55% | 4.28% | 5.58% | 5.15% |

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The following table shows the carrying amount (amortized cost) and fair value of the Company s investment securities held to maturity as of the dates indicated:

**Held to Maturity Portfolio**

| At December 31, (Dollars in thousands) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Securities of U.S. Government sponsored entities | $ | $ 110,000 | $ 130,000 |
| Mortgage backed securities | 61,893 | 85,676 | 107,162 |
| Obligations of States and political subdivisions | 516,596 | 545,237 | 566,351 |
| Collateralized mortgage obligations | 148,446 | 208,412 | 241,775 |
| Total | $ 726,935 | $ 949,325 | $ 1,045,288 |
| Fair value | $ 736,270 | $ 950,210 | $ 1,049,442 |

The following table sets forth the relative maturities and contractual yields of the Company s held to maturity securities at December 31, 2009. Yields on state and political subdivision securities have been calculated on a fully taxable equivalent basis using the current federal statutory rate.

Held to Maturity Maturity Distribution

| At December 31, 2009, (Dollars in thousands) | Within One year | After one but within five years | After five but within ten years | After ten years | Mortgage-backed | Total |
|---|---|---|---|---|---|---|
| States and political subdivisions | $ 8,303 | $ 58,111 | $ 413,720 | $ 36,462 | $ | $ 516,596 |
| Interest rate (FTE) | 6.40% | 6.31% | 6.09% | 5.83% | | 6.15% |
| Mortgage backed securities and collateralized mortgage obligations | | | | | 210,339 | 210,339 |
| Interest rate | | | | | 4.54% | 4.54% |
| Total | $ 8,303 | $ 58,111 | $ 413,720 | $ 36,462 | $ 210,339 | $ 726,935 |
| Interest rate | 6.40% | 6.31% | 6.09% | 5.83% | 4.54% | 5.68% |

**Loan Portfolio**

The following table shows the composition of the loan portfolio of the Company by type of loan and type of borrower, on the dates indicated:

Non-covered Loan Portfolio Distribution

| At December 31, (dollars in thousands) | 2009 | 2008 | 2007 | 2006 | 2005 |
|---|---|---|---|---|---|
| Commercial and commercial real estate | $ 1,299,602 | $ 1,342,209 | $ 1,389,213 | $ 1,463,823 | $ 1,594,925 |
| Real estate construction | 32,156 | 52,664 | 97,464 | 70,650 | 72,095 |
| Real estate residential | 371,197 | 458,447 | 484,549 | 507,553 | 508,174 |
| Consumer | 498,133 | 529,106 | 531,732 | 489,708 | 497,027 |

| | | | | | |
|---|---|---|---|---|---|
| Total loans | $ 2,201,088 | $ 2,382,426 | $ 2,502,976 | $ 2,531,734 | $ 2,672,221 |

Covered Loan Portfolio Distribution

| At December 31, (dollars in thousands) | 2009 |
|---|---|
| Commercial and commercial real estate | $ 698,789 |
| Real estate construction | 40,460 |
| Real estate residential | 18,521 |
| Consumer | 97,531 |
| Total loans | $ 855,301 |

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The following table shows the maturity distribution and interest rate sensitivity of commercial, commercial real estate, and construction loans at December 31, 2009. Balances exclude residential real estate loans and consumer loans totaling $985.4 million. These types of loans are typically paid in monthly installments over a number of years.

Loan Maturity Distribution

| At December 31, 2009 (dollars in thousands) | Within One Year | One to Five Years | After Five Years | Total |
|---|---|---|---|---|
| Commercial and commercial real estate * | $ 735,378 | $ 983,331 | $ 279,682 | $ 1,998,391 |
| Real estate construction | 72,616 | | | 72,616 |
| Total | $ 807,994 | $ 983,331 | $ 279,682 | $ 2,071,007 |
| Loans with fixed interest rates | $ 202,334 | $ 274,034 | $ 198,053 | $ 674,421 |
| Loans with floating or adjustable interest rates | 605,660 | 709,297 | 81,629 | 1,396,586 |
| Total | $ 807,994 | $ 983,331 | $ 279,682 | $ 2,071,007 |

* Includes demand loans

**Commitments and Letters of Credit**

The Company issues formal commitments on lines of credit to well-established and financially responsible commercial enterprises. Such commitments can be either secured or unsecured and are typically in the form of revolving lines of credit for seasonal working capital needs. Occasionally, such commitments are in the form of letters of credit to facilitate the customers particular business transactions. Commitment fees are generally charged for commitments and letters of credit. Commitments on lines of credit and letters of credit typically mature within one year. For further information, see the notes accompanying the consolidated financial statements.

**Loan Portfolio Credit Risk**

The risk that loan customers do not repay loans granted by the Bank is the most significant risk to the Company. The Company closely monitors the markets in which it conducts its lending operations and follows a strategy to control exposure to loans with high credit risk. The Bank s organization structure separates the functions of business development and loan underwriting; Management believes this segregation of duties avoids inherent conflicts of combining the business development and loan approval functions. In managing and measuring credit risk, Management follows practices customary in the commercial banking industry.

The Bank maintains a Loan Review Department which reports directly to the Board of Directors. The Loan Review Department performs independent evaluations of loans and assigns credit risk grades to evaluated loans using grading standards employed by bank regulatory agencies. Those loans judged to carry higher risk attributes are referred to as classified loans. Classified loans receive elevated Management s attention to maximize collection.

The Bank maintains two loan administration offices whose sole responsibility is to manage and collect classified loans.

Classified loans with higher levels of credit risk are further designated as nonaccrual loans. Management places loans on nonaccrual status when full collection of contractual interest and principal payments is in doubt. Interest previously accrued on loans placed on nonaccrual status is charged against interest income. The Company does not accrue interest income on nonaccrual loans. Interest payments received on nonaccrual loans are applied to reduce the carrying amount of the loan unless the carrying amount is well secured by loan collateral or covered by FDIC loss-sharing agreements. Nonperforming assets include nonaccrual loans, loans 90 or more days past due and still accruing, and repossessed loan collateral.

On February 6, 2009, the Bank purchased loans and repossessed loan collateral of the former County from the FDIC. This purchase transaction included loss-sharing agreements with the FDIC wherein the FDIC and the Bank share losses on the purchased assets. The loss-sharing agreements significantly reduce the credit risk of these purchased assets. In evaluating credit risk, Management bifurcates the Bank s total loan portfolio between those loans qualifying under the FDIC loss-sharing agreements (referred to as covered loans ) and loans not qualifying under the FDIC loss-sharing agreements (referred to as non-covered loans ). At December 31, 2009, covered loans totaled $855 million, or 28 percent of total loans, and non-covered loans totaled $2.2 billion, or 72 percent of total loans.

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***Covered Loans and Repossessed Loan Collateral (Covered Assets)***

Covered loans and repossessed loan collateral qualify under loss-sharing agreements with the FDIC. Under the terms of the loss- sharing agreements, the FDIC absorbs 80 percent of losses and is entitled to 80 percent of loss recoveries on the first $269 million in losses on covered assets ( First Tier ), and absorbs 95 percent of losses and is entitled to 95 percent of loss recoveries exceeding $269 million ( Second Tier ). The term of the loss-sharing agreement on residential real estate assets is ten years, while the term for loss-sharing on non-residential real estate assets is five years in respect to losses and eight years in respect to loss recoveries.

The covered assets are primarily located in the California Central Valley, including Merced County. This geographic area currently has some of the weakest economic conditions within California and has experienced significant declines in real estate values. Management expects higher loss rates on covered assets than on non-covered assets.

The Bank recorded acquired covered assets at estimated fair value on the February 6, 2009 acquisition date. The credit risk discount ascribed to the $1.2 billion acquired loan and repossessed loan collateral portfolio was $161 million representing estimated losses inherent in the assets at the acquisition date. The Bank also recorded a related receivable from the FDIC in the amount of $129 million representing estimated FDIC reimbursements under the loss-sharing agreements.

In Management s judgment, the fair value discount recognized for the acquired assets remains adequate as an estimate of credit risk in covered assets as of December 31, 2009. In the event credit risk deteriorates beyond that estimated by Management, losses in excess of the fair value credit discount would be recognized, net of related FDIC loss indemnification.

The maximum risk to future earnings if First Tier losses exceed Management s estimated $161 million in recognized losses under the FDIC loss-sharing agreements is estimated to be $12 million as follows (in thousands):

| | | |
|---|---|---|
| First Tier Loss Coverage | $ | 269,000 |
| Less: Recognized credit risk discount | | 161,203 |
| Exposure to under-estimated risk within FirstTier | | 107,797 |
| Bank loss-sharing percentage | | 20 percent |
| First Tier risk to Bank, pre-tax | $ | 21,559 |
| First Tier risk to Bank, after-tax | $ | 12,494 |

Of the estimated $161 million in recognized credit risk at February 6, 2009, the Company has realized losses of $79 million during the period February 6, 2009 through December 31, 2009. Management has judged the likelihood of experiencing losses of a magnitude to trigger Second Tier FDIC reimbursement as remote. The Bank s maximum after-tax exposure to Second Tier losses is $22 million as of December 31, 2009, which would be realized only if all covered assets at December 31, 2009 generated no future cash flows.

The following is a summary of covered classified loans and repossessed loan collateral:

| | | At December 31, 2009 (In thousands) |
|---|---|---|
| Covered Classified Assets | | |
| Classified loans | $ | 181,516 |
| Repossessed loan collateral | | 23,297 |
| Total | $ | 204,813 |

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The following is a summary of covered nonperforming assets which are included in covered classified assets:

| | At December 31, 2009 (In thousands) | |
|---|---|---|
| Covered nonperforming assets | | |
| Nonperforming, nonaccrual loans | $ | 66,965 |
| Performing, nonaccrual loans | | 18,183 |
| Total nonaccrual loans | | 85,148 |
| Loans 90 days past due and still accruing | | 210 |
| Total nonperforming loans | | 85,358 |
| Covered repossessed loan collateral | | 23,297 |
| Total | $ | 108,655 |
| As a percentage of total covered loans and OREO | | 12.37% |

The amount of gross interest income that would have been recorded if all nonaccrual loans had been current in accordance with their original terms while outstanding was $3.9 million in 2009. The amount of interest income that was recognized on nonaccrual loans from cash payments made in 2009 was $1.7 million. The yield on these cash payments was 2.90% for the year ended December 31, 2009. Cash payments received, which were applied against the book balance of performing and nonperforming nonaccrual loans outstanding at December 31, 2009, totaled $-0-.

***Non-covered Classified Loans and Repossessed Loan Collateral (Non-covered Assets)***

The following is a summary of non-covered classified loans and repossessed loan collateral:

| | At December 31, | | | |
|---|---|---|---|---|
| | 2009 | | 2008 | |
| | (In thousands) | | | |
| Non-covered Classified Assets | | | | |
| Classified loans | $ | 57,241 | $ | 34,028 |
| Repossessed loan collateral | | 12,642 | | 3,505 |
| Total | $ | 69,883 | $ | 37,533 |
| Allowance for loan losses / non-covered classified loans | | 72% | | 131% |

Non-covered classified assets have increased due to weak economic conditions.

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The following is a summary of non-covered nonperforming assets which are included in non-covered classified assets on the dates indicated:

| | At December 31, 2009 | 2008 |
|---|---|---|
| | (In thousands) | |
| Non-covered nonperforming assets | | |
| Nonperforming, nonaccrual loans | $ 19,837 | $ 8,883 |
| Performing, nonaccrual loans | 25 | 1,143 |
| Total nonaccrual loans | 19,862 | 10,026 |
| Loans 90 days past due and still accruing | 800 | 755 |
| Total nonperforming loans | 20,662 | 10,781 |
| Repossessed loan collateral | 12,642 | 3,505 |
| Total | $ 33,304 | $ 14,286 |
| As a percentage of total non-covered loans and repossessed loan collateral | 1.50% | 0.60% |

Non-covered nonaccrual loans increased $9.8 million during the twelve months ended December 31, 2009 as weak economic conditions reduced some borrowers ability to repay loans and reduced collateral values, particularly real estate values. Fifty five loans comprised the $19.8 million in nonaccrual loans as of December 31, 2009. The increase in non-covered nonperforming loans is primarily due to four construction loan relationships ($3.1 million), twelve consumer mortgages ($6.2 million), and three commercial real estate relationships ($3.4 million) placed on nonaccrual status during the twelve months ended December 31, 2009. The Company actively pursues full collection of nonaccrual loans.

The Company had no restructured loans as of December 31, 2009 and December 31, 2008.

Delinquent non-covered commercial loans, non-covered construction loans and non-covered commercial real estate loans on accrual status were as follows:

| | At December 31, 2009 | 2008 |
|---|---|---|
| | (Dollars In thousands) | |
| Non-covered commercial loans: | | |
| 30-89 days delinquent: | | |
| Dollar amount | $ 10,677 | $ 3,559 |
| Percentage of total non-covered commercial loans | 2.14% | 0.70% |
| 90 or more days delinquent: | | |
| Dollar amount | $ | $ |
| Percentage of total non-covered commercial loans | % | % |
| Non-covered construction loans: | | |
| 30-89 days delinquent: | | |
| Dollar amount | $ 149 | $ 3,393 |
| Percentage of total non-covered construction loans | 0.46% | 6.44% |
| 90 or more days delinquent: | | |
| Dollar amount | $ | $ |

| | | | | |
|---|---|---|---|---|
| Percentage of total non-covered construction loans | | % | | % |
| | | | | |
| Non-covered commercial real estate loans: | | | | |
| 30-89 days delinquent: | | | | |
| Dollar amount | $ | 12,158 | $ | 5,993 |
| Percentage of total non-covered commercial real estate loans | | 1.52% | | 0.73% |
| 90 or more days delinquent: | | | | |
| Dollar amount | $ | | $ | |
| Percentage of total non-covered commercial real estate loans | | % | | % |

The Company s residential real estate loan underwriting standards for first mortgages limit the loan amount to no more than 80 percent of the appraised value of the property serving as collateral for the loan at the time of origination, and require verification of income of the borrower(s). The Company had no sub-prime non-covered loans as of December 31, 2009 and December 31, 2008. At December 31, 2009, $6.2 million non-covered residential real estate loans were on nonaccrual status.

Delinquent non-covered residential real estate loans, non-covered automobile loans and non-covered other consumer loans on accrual status were as follows:

| | At December 31, | |
|---|---|---|
| | **2009** | **2008** |
| | (Dollars In thousands) | |
| Non-covered residential real estate loans: | | |
| 30-89 days delinquent: | | |
| Dollar amount | $ 3,064 | $ 3,273 |
| Percentage of total non-covered residential real estate loans | 0.83% | 0.71% |
| 90 or more days delinquent: | | |
| Dollar amount | $ | $ |
| Percentage of total non-covered residential real estate loans | % | % |
| Non-covered automobile loans: | | |
| 30-89 days delinquent: | | |
| Dollar amount | $ 6,506 | $ 5,241 |
| Percentage of total automobile loans | 1.49% | 1.12% |
| 90 or more days delinquent: | | |
| Dollar amount | $ 723 | $ 569 |
| Percentage of total automobile loans | 0.17% | 0.12% |
| Non-covered other consumer loans: | | |
| 30-89 days delinquent: | | |
| Dollar amount | $ 762 | $ 896 |
| Percentage of total non-covered other consumer loans | 1.25% | 1.49% |
| 90 or more days delinquent: | | |
| Dollar amount | $ 77 | $ 186 |
| Percentage of total non-covered other consumer loans | 0.13% | 0.31% |

The amount of gross interest income that would have been recorded if all nonaccrual loans had been current in accordance with their original terms while outstanding during the period was $1.3 million in 2009, $665 thousand in 2008 and $428 thousand in 2007. The amount of interest income that was recognized on nonaccrual loans from cash payments made in 2009, 2008 and 2007 was $407 thousand, $511 thousand and $474 thousand, respectively. Yields on these cash payments were 1.72%, 4.72% and 9.80%, respectively, for the year ended December 31, 2009, December 31, 2008 and December 31, 2007. Cash payments received in 2009, which were applied against the book balance of performing and nonperforming nonaccrual loans outstanding at December 31, 2009, totaled $1 thousand, compared with approximately $-0- and $14 thousand for the years ended December 31, 2008 and 2007, respectively.

Non-covered nonperforming assets could fluctuate from period to period. The performance of any individual loan can be affected by external factors such as the interest rate environment, economic conditions, collateral values or factors particular to the borrower. No assurance can be given that additional increases in non-covered nonaccrual loans will not occur in the future.

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**Allowance for Credit Losses**

The Company s allowance for credit losses represents Management s estimate of credit losses inherent in the loan portfolio. In evaluating credit risk for loans, Management measures loss potential of the carrying value of loans. As described in the Nonperforming Loans section above, payments on nonaccrual loans may be applied against the principal balance of the loans until such time as full collection of the remaining recorded balance is expected. Further, the carrying value of covered loans includes fair value credit risk discounts assigned at the time of purchase under the provisions of FASB ASC 805, Business Combinations, and FASB ASC 310-30, Loans or Debt Securities with Deteriorated Credit Quality. The allowance for credit losses represents Management s estimate of credit losses in excess of these reductions in carrying value.

Management determined the fair value credit risk discounts assigned to covered loans purchased on February 6, 2009 remained adequate as an estimate of credit losses inherent in covered loans as of December 31, 2009.

The following table summarizes the allowance for credit losses, chargeoffs and recoveries of the Company for the periods indicated:

| Year ended December 31, (dollars in thousands) | 2009 | 2008 | 2007 | 2006 | 2005 |
|---|---|---|---|---|---|
| Total non-covered loans outstanding | $ 2,201,088 | $ 2,382,426 | $ 2,502,976 | $ 2,531,734 | $ 2,672,221 |
| Average non-covered loans outstanding during the period | 2,329,019 | 2,432,556 | 2,511,763 | 2,576,791 | 2,576,363 |
| Analysis of the Allowance | | | | | |
| Balance, beginning of period | $ 47,563 | $ 55,799 | $ 59,023 | $ 59,537 | $ 54,152 |
| Provision for loan losses | 10,500 | 2,700 | 700 | 445 | 900 |
| Provision for unfunded credit commitments | (400) | (200) | (400) | 5 | |
| Allowance acquired through merger | | | | | 5,213 |
| Loans charged off: | | | | | |
| Commercial and commercial real estate | (6,066) | (1,296) | (1,648) | (1,176) | (673) |
| Real estate construction | (1,333) | (5,348) | | | |
| Real estate residential | (506) | (131) | | | |
| Consumer | (9,362) | (5,638) | (4,033) | (2,446) | (2,065) |
| Total chargeoffs | (17,267) | (12,413) | (5,681) | (3,622) | (2,738) |
| Recoveries of loans previously charged off: | | | | | |
| Commercial and commercial real estate | 490 | 331 | 1,060 | 1,149 | 864 |
| Real estate construction | 664 | | | | |
| Real estate residential | | | | | |
| Consumer | 2,186 | 1,346 | 1,097 | 1,509 | 1,146 |
| Total recoveries | 3,340 | 1,677 | 2,157 | 2,658 | 2,010 |
| Net loan losses | (13,927) | (10,736) | (3,524) | (964) | (728) |
| Balance, end of period | $ 43,736 | $ 47,563 | $ 55,799 | $ 59,023 | $ 59,537 |

| | | | | | |
|---|---|---|---|---|---|
| Components: | | | | | |
| Allowance for loan losses | $ 41,043 | $ 44,470 | $ 52,506 | $ 55,330 | $ 55,849 |
| Reserve for unfunded credit commitments | 2,693 | 3,093 | 3,293 | 3,693 | 3,688 |
| Allowance for credit losses | $ 43,736 | $ 47,563 | $ 55,799 | $ 59,023 | $ 59,537 |
| Net loan losses to average non-covered loans | 0.60% | 0.44% | 0.14% | 0.04% | 0.03% |
| Allowance for loan losses as a percentage of non-covered loans outstanding | 1.86% | 1.87% | 2.10% | 2.19% | 2.09% |

The Company s non-covered loans outstanding declined over the five years presented in the above table. During 2005, 2006 and 2007, in Management s opinion, competitive loan underwriting terms were too liberal to ensure high-quality loan originations, and loan pricing was not sufficient to ensure adequate profitability over the expected loan durations. The Company s competitive posture during this period resulted in declining loan volumes. A severe recession and weak economic conditions impacted loan volumes throughout 2008 and 2009.

During 2008 and 2009, net loan losses increased due to weak economic conditions and declines in the value of real estate collateral. Accordingly, Management increased the provision for loan losses. The allowance for loan losses as a percentage of non-covered loans outstanding has gradually declined from 2006 through 2009. The decline is generally due to the realization of losses in 2008 and 2009 which were inherent in the loan portfolio in earlier years, and a reduction in the Company s exposure to higher-risk non-covered real estate construction loans.

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The Company s allowance for credit losses is maintained at a level considered adequate to provide for losses that can be estimated based upon specific and general conditions. These include conditions unique to individual borrowers, as well as overall credit loss experience, the amount of past due, nonperforming loans and classified loans, FDIC loss sharing coverage relative to covered loan carrying amounts, recommendations of regulatory authorities, prevailing economic conditions and other factors. A portion of the allowance is specifically allocated to impaired loans whose full collectibility is uncertain. Such allocations are determined by Management based on loan-by-loan analyses. A second allocation is based in part on quantitative analyses of historical credit loss experience, in which criticized and classified credit balances identified through an independent internal credit review process are analyzed using a linear regression model to determine standard loss rates. The results of this analysis are applied to current criticized and classified loan balances to allocate the allowance to the respective segments of the loan portfolio. In addition, small loans with similar characteristics not usually criticized using regulatory guidelines are analyzed based on the historical loss rates and delinquency trends, grouped by the number of days the payments on these loans are delinquent. Given currently weak economic conditions, Management is applying further analysis to consumer loans. Current levels of automobile loan losses are compared to initial allowance allocations and, based on Management judgment, additional allocations are applied, if needed, to estimate losses. For residential real estate loans, Management is comparing ultimate loss rates on foreclosed residential real estate properties and applying such loss rates to nonaccrual residential real estate loans. Based on this analysis, Management exercises judgment in allocating additional allowance if deemed appropriate to estimate losses on residential real estate loans. Last, allocations are made to non-criticized and non-classified commercial loans based on historical loss rates and other statistical data.

The remainder of the allowance is considered to be unallocated. The unallocated allowance is established to provide for probable losses that have been incurred as of the reporting date but not reflected in the allocated allowance. It addresses additional qualitative factors consistent with Management s analysis of the level of risks inherent in the loan portfolio, which are related to the risks of the Company s general lending activity. Included in the unallocated allowance is the risk of losses that are attributable to national or local economic or industry trends which have occurred but have not yet been recognized in past loan charge-off history (external factors). The external factors evaluated by the Company include: economic and business conditions, external competitive issues, and other factors. Also included in the unallocated allowance is the risk of losses attributable to general attributes of the Company s loan portfolio and credit administration (internal factors). The internal factors evaluated by the Company include: loan review system, adequacy of lending Management and staff, loan policies and procedures, problem loan trends, concentrations of credit, and other factors. By their nature, these risks are not readily allocable to any specific loan category in a statistically meaningful manner and are difficult to quantify with a specific number. Management assigns a range of estimated risk to the qualitative risk factors described above based on Management s judgment as to the level of risk, and assigns a quantitative risk factor from the range of loss estimates to determine the appropriate level of the unallocated portion of the allowance. Management considers the $43.7 million allowance for credit losses to be adequate as a reserve against non-covered credit losses as of December 31, 2009.

The following table presents the allocation of the allowance for credit losses as of December 31 for the years indicated:

Allocation of the Allowance for Credit Losses

| | 2009 | | 2008 | | 2007 | | 2006 | | 2005 | |
|---|---|---|---|---|---|---|---|---|---|---|
| At December 31, (dollars in thousands) | Allocation of the Allowance Balance | Loans as Percent of Total Non-covered Loans | Allocation of the Allowance Balance | Loans as Percent of Total Non-covered Loans | Allocation of the Allowance Balance | Loans as Percent of Total Non-covered Loans | Allocation of the Allowance Balance | Loans as Percent of Total Non-covered Loans | Allocation of the Allowance Balance | Loans as Percent of Total Non-covered Loans |
| Commercial | $ 19,108 | 59% | $ 23,774 | 57% | $ 27,233 | 56% | $ 23,217 | 58% | $ 30,438 | 60% |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Real estate construction | 2,968 | 1% | 4,725 | 2% | 5,403 | 4% | 3,942 | 3% | 3,346 | 3% |
| Real estate residential | 1,529 | 17% | 367 | 19% | 388 | 19% | 1,219 | 20% | 1,230 | 19% |
| Consumer | 8,424 | 23% | 6,331 | 22% | 4,626 | 21% | 4,132 | 19% | 5,291 | 18% |
| Unallocated portion | 11,707 | | 12,366 | | 18,149 | | 26,513 | | 19,232 | |
| Total | $ 43,736 | 100% | $ 47,563 | 100% | $ 55,799 | 100% | $ 59,023 | 100% | $ 59,537 | 100% |

The allocation to loan portfolio segments changed from December 31, 2008 to December 31, 2009. The decrease in allocation for commercial loans reflects Management s evaluation of loss rates against commercial loan performance metrics. The decrease in allocation to real estate construction loans reflects a decrease in criticized construction loans outstanding. The elevated allocation for residential real estate loans is attributable to Management s judgment regarding the appropriate allocation based on recent foreclosure losses and increased levels of nonaccrual mortgages. The higher allocation for consumer loans was primarily due to Management s judgment regarding the appropriate allocation based on current levels of auto loan chargeoffs.

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The allocation to loan portfolio segments changed from December 31, 2007 to December 31, 2008. The decrease in allocation to commercial loans was primarily due to a reduction in allocations to agricultural and municipal loans based on re-evaluation and measurement of risk attributes. The decline in the allocation to real estate construction loans reflects a decrease in criticized real estate construction loans and the increase in allocation to consumer loans reflects delinquency trends.

The unallocated portion of the allowance for credit losses declined $659 thousand from December 31, 2008 to December 31, 2009. The unallocated allowance is established to provide for probable losses that have been incurred, but not reflected in the allocated allowance. At December 31, 2009 and December 31, 2008, Management s evaluations of the unallocated portion of the allowance for credit losses attributed significant risk levels to developing economic and business conditions ($2.3 million and $3.4 million, respectively), external competitive issues ($0.8 million and $1.2 million, respectively), internal credit administration considerations ($2.0 million and $1.4 million), and delinquency and problem loan trends ($3.5 million and $3.5 million, respectively). The change in the amounts allocated to the above qualitative risk factors was based upon Management s judgment, review of trends in its loan portfolio, levels of the allowance allocated to portfolio segments, and current economic conditions in its marketplace. Based on Management s analysis and judgment, the amount of the unallocated portion of the allowance for credit losses was $11.7 million at December 31, 2009, compared to $12.4 million at December 31, 2008.

The unallocated portion of the allowance for credit losses declined $5.7 million from December 31, 2007 to December 31, 2008. During 2008, classified loans, nonperforming loans and consumer loan delinquencies increased; as a result, the allocated allowance reflects probable losses related to these loans and the unallocated allowance declined. At December 31, 2007 and December 31, 2008, Management s evaluations of the unallocated portion of the allowance for credit losses attributed significant risk levels to developing economic and business conditions ($4.0 million and $3.4 million, respectively), external competitive issues ($2.0 million and $1.2 million, respectively), internal credit administration considerations ($4.2 million and $1.4 million, respectively), and delinquency and problem loan trends ($4.2 million and $3.5 million, respectively). The change in the amounts allocated to the above qualitative risk factors was based upon Management s judgment, review of trends in its loan portfolio which includes a decline in loan balances and reduced real estate construction exposure, levels of the allowance allocated to portfolio segments, internal staffing considerations and current economic conditions in its marketplace including loan underwriting and pricing practices of competitors. Based on Management s analysis and judgment, the amount of the unallocated portion of the allowance for credit losses was $18.1 million at December 31, 2007, compared with $12.4 million at December 31, 2008.

*Impaired Loans*

The Company considers a loan to be impaired when, based on current information and events, it is probable that it will be unable to collect all amounts due (principal and interest) according to the contractual terms of the loan agreement. The measurement of impairment may be based on (i) the present value of the expected cash flows of the impaired loan discounted at the loan s original effective interest rate, (ii) the observable market price of the impaired loan or (iii) the fair value of the collateral of a collateral-dependent loan. The Company does not apply this definition to smaller-balance loans that are collectively evaluated for credit risk. In assessing impairment, the Company reviews all nonaccrual commercial and construction loans with outstanding principal balances in excess of $1 million. Nonaccrual commercial and construction loans with outstanding principal balances less than $1 million, and large groups of smaller-balance homogeneous loans such as installment, personal revolving credit, residential real estate and student loans, are evaluated collectively for impairment under the Company s standard loan loss reserve methodology.

Impaired purchased loans covered by FDIC loss-sharing agreements were recorded at fair value on the February 6, 2009 acquisition date.

The following summarizes the Company s recorded investment in non-covered impaired loans for the dates indicated:

| At December 31, | | |
|---|---|---|
| (dollars in thousands) | 2009 | 2008 |
| Total impaired loans | $ 2,447 | $ 6,849 |

| | | | | |
|---|---|---|---|---|
| Specific reserves | $ | 617 | $ | 1,936 |

At December 31, 2009 and 2008, the Company measured impairment using the fair value of loan collateral. The average balance of the Company s non-covered impaired loans for the year ended December 31, 2009 was $5.3 million compared with $7.0 million in 2008. All impaired loans are on nonaccrual status.

**Asset/Liability and Market Risk Management**

Asset/liability management involves the evaluation, monitoring and management of interest rate risk, market risk, liquidity and funding. The fundamental objective of the Company s management of assets and liabilities is to maximize its economic value while maintaining adequate liquidity and a conservative level of interest rate risk.

**Interest Rate Risk**

Interest rate risk is a significant market risk affecting the Company. Interest rate risk results from many factors. Assets and liabilities may mature or reprice at different times. Assets and liabilities may reprice at the same time but by different amounts. Short-term and long-term market interest rates may change by different amounts. The remaining maturity of various assets or liabilities may shorten or lengthen as interest rates change. In addition, interest rates may have an impact on loan demand, credit losses, and other sources of earnings such as account analysis fees on commercial deposit accounts and correspondent bank service charges.

In adjusting the Company s asset/liability position, Management attempts to manage interest rate risk while enhancing the net interest margin and net interest income. At times, depending on expected increases or decreases in general interest rates, the relationship between long and short term interest rates, market conditions and competitive factors, Management may adjust the Company s interest rate risk position in order to manage its net interest margin and net interest income. The Company s results of operations and net portfolio values remain subject to changes in interest rates and to fluctuations in the difference between long and short term interest rates.

The Company s asset and liability position was neutral at December 31, 2009; the simulation model employed by Management measured similar amounts of increased interest income and interest expense in the most likely scenarios with rising interest rates. Management continues to monitor the interest rate environment as well as economic conditions and other factors it deems relevant in managing the Company s exposure to interest rate risk.

Management assesses interest rate risk by comparing the Company s most likely earnings plan with various earnings models using many interest rate scenarios that differ in the direction of interest rate changes, the degree of change over time, the speed of change and the projected shape of the yield curve. For example, using the current composition of the Company s balance sheet and assuming no change in the federal funds rate and no change in the 10 year Constant Maturity Treasury Bond yield during the same period, earnings are not estimated to change by a meaningful amount compared to the Company s most likely net income plan for the twelve months ending December 31, 2010. Conversely, using the current composition of the Company s balance sheet and assuming an increase of 100 bp in the federal funds rate and an increase of 10 bp in the 10 year Constant Maturity Treasury Bond yield during the same period, earnings are not estimated to change by a meaningful amount compared to the Company s most likely net income plan for the twelve months ending December 31, 2010. Simulation estimates depend on, and will change with, the size and mix of the actual and projected balance sheet at the time of each simulation. The Company does not currently engage in trading activities or use derivative instruments to control interest rate risk, even though such activities may be permitted with the approval of the Company s Board of Directors.

**Market Risk Equity Markets**

Equity price risk can affect the Company. As an example, any preferred or common stock holdings, as permitted by banking regulations, can fluctuate in value. Management regularly assesses the extent and duration of any declines in market value, the causes of such declines, the likelihood of a recovery in market value, and its intent to hold securities until a recovery in value occurs. Declines in value of preferred or common stock holdings that are deemed other than temporary could result in loss recognition in the Company s income statement.

Fluctuations in the Company s common stock price can impact the Company s financial results in several ways. First, the Company has regularly repurchased and retired its common stock; the market price paid to retire the Company s common stock can affect the level of the Company s shareholders equity, cash flows and shares outstanding for purposes of computing earnings per share. Second, the Company s common stock price impacts the number of dilutive equivalent shares used to compute diluted earnings per share. Third, fluctuations in the Company s common stock price can motivate holders of options to purchase Company common stock through the exercise of such options thereby increasing the number of shares outstanding. Finally, the amount of compensation expense associated with share based compensation fluctuates with changes in and the volatility of the Company s common stock price.

**Market Risk Other**
Market values of loan collateral can directly impact the level of loan chargeoffs and the provision for loan losses. Other types of market risk, such as foreign currency exchange risk and commodity price risk, are not significant in the normal course of the Company s business activities.
**Liquidity and Funding**
The Company s routine operating sources of liquidity are operating earnings, investment securities, consumer and other loans, deposits, and other borrowed funds. During 2009, the Company s operating activities generated $149 million in liquidity providing adequate funds to pay common shareholders $41 million in dividends. Further, investment securities provided $332.5 million in liquidity from paydowns and maturities, and loans provided $447.3 million in liquidity from scheduled payments and maturities, net of loan fundings. During 2009, a portion of the liquidity from investment securities and loans provided funds to reduce short term borrowings by $472 million and to meet a net reduction in deposits totaling $262.0 million. The Company also raised $83.7 million from the issuance of preferred stock to the United States Treasury in the first quarter of 2009 and redeemed $83.7 million of the same preferred stock in the third and fourth quarters of 2009. The Company projects $153 million in additional liquidity from investment security paydowns and maturities in the twelve months ending December 31, 2010. At December 31, 2009, indirect automobile loans totaled $436.9 million, which were experiencing stable monthly principal payments of approximately $16.4 million during the last three months of 2009.
During 2008, the Company s operating activities generated $93 million in liquidity providing adequate funds to pay $40 million in common dividends and retire $36 million in common stock. During 2008, investment securities provided $305.4 million in liquidity from paydowns and maturities, and loans provided $106.3 million in liquidity from scheduled payments and maturities, net of loan fundings. A portion of the liquidity provided by investment securities and loans provided funds to meet a net reduction in deposits totaling $169.7 million. The remaining liquidity was used to reduce higher-cost borrowed funds, primarily subordinated debt which decreased $10 million and federal funds purchased which declined $286.0 million.
The Company held $1.11 billion in total investment securities at December 31, 2009. Under certain deposit, borrowing and other arrangements, the Company must pledge investment securities as collateral. At December 31, 2009, such collateral requirements totaled approximately $1.03 billion. At December 31, 2009, $384.2 million of the Company s investment securities were classified as available-for-sale , and as such, could provide additional liquidity if sold, subject to the Company s ability to meet continuing collateral requirements.
At December 31, 2009, $397.8 million in collateralized mortgage obligations ( CMOs ) and mortgage backed securities ( MBSs ) were held in the Company s investment portfolios. None of the CMOs or MBSs are backed by sub-prime mortgages. Other than nominal amounts of FHLMC and FNMA MBSs purchased for Community Reinvestment Act investment purposes, the Company has not purchased a CMO or MBS since November 2005. The CMOs and MBSs have been experiencing stable principal paydowns of approximately $10.1 million per month during the last three months. In addition, at December 31, 2009, the Company had customary lines for overnight borrowings from other financial institutions in excess of $700 million, under which $-0- was outstanding. Additionally, the Company has access to borrowing from the Federal Reserve. The Company s short-term debt rating from Fitch Ratings is F1. The Company s long-term debt rating from Fitch Ratings is A with a stable outlook. Management expects the Company could access additional long-term debt financing if desired. In Management s judgment, the Company s liquidity position is strong and asset liquidations or additional long-term debt are considered unnecessary to meet the ongoing liquidity needs of the Company.
Management anticipates that loan demand will be weak during 2010, although such demand will be dictated by economic and competitive conditions. The Company aggressively solicits non-interest bearing demand deposits and money market checking deposits, which are the least sensitive to changes in interest rates. The growth of deposit balances is subject to heightened competition, the success of the Company s sales efforts, delivery of superior customer service and market conditions. The recent low level of short-term interest rates could impact deposit volumes in the future. Depending on economic conditions, interest rate levels, and a variety of other conditions, deposit growth may be used to fund loans, to reduce short-term borrowings or purchase investment securities. However, due to concerns such as uncertainty in the general economic environment, competition and political

uncertainty, loan demand and levels of customer deposits are not certain. Shareholder dividends are expected to continue subject to the Board s discretion and continuing evaluation of capital levels, earnings, asset quality and other factors.

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The Parent Company s primary source of liquidity is dividends from the Bank. Dividends from the Bank are subject to certain regulatory limitations. During 2009, 2008 and 2007, the Bank declared dividends to the Company of $93 million, $100 million and $109 million, respectively.

The following table sets forth the known contractual obligations, except short-term borrowing arrangements and post retirement benefit plans, of the Company at December 31, 2009:

Contractual Obligations

| At December 31, 2009 (dollars in thousands) | Within One Year | Over One to Three Years | Over Three to Five Years | After Five Years | Total |
|---|---|---|---|---|---|
| Long-Term Debt Obligations | $ | $ | $ 15,000 | $ 10,000 | $ 25,000 |
| Federal Home Loan Bank advances | 75,080 | 10,390 | | | 85,470 |
| Operating Lease Obligations | 6,756 | 11,051 | 6,060 | 499 | 24,366 |
| Purchase Obligations | 8,472 | 8,472 | | | 16,944 |
| Total | $ 90,308 | $ 29,913 | $ 21,060 | $ 10,499 | $ 151,780 |

Long-term debt obligations and operating lease obligations may be retired prior to the contractual maturity as discussed in the notes to the consolidated financial statements. The purchase obligation consists of the Company s minimum liability under a contract with a third-party automation services provider.

**Capital Resources**

The Company has historically generated high levels of earnings, which provides a means of raising capital. The Company s net income as a percentage of average shareholders equity ( return on equity or ROE ) has been 22.1% in 2007, 14.8% in 2008 and 25.8% in 2009. The Company also raises capital as employees exercise stock options, which are awarded as a part of the Company s executive compensation programs to reinforce shareholders interests in the Management of the Company. Capital raised through the exercise of stock options totaled $11.9 million in 2007, $22.8 million in 2008 and $9.6 million in 2009.

The Company paid common dividends totaling $40.6 million in 2007, $40.2 million in 2008, and $41.1 million in 2009, which represent dividends per common share of $1.36, $1.39, and $1.41, respectively. In 2009, the Company was not able to, without the consent of the Treasury, increase the cash dividend on the Company s common stock above $0.35 per share, the amount of the last quarterly cash dividend per share declared prior to October 14, 2008 while the Treasury Preferred Stock was outstanding. This restriction was removed upon full redemption of the Treasury Preferred Stock on November 18, 2009. The Company s earnings have historically exceeded dividends paid to shareholders. The amount of earnings in excess of dividends gives the Company resources to finance growth and maintain appropriate levels of shareholders equity. In the absence of profitable growth opportunities, the Company has repurchased and retired its common stock as another means to return earnings to shareholders. The Company repurchased and retired 1.9 million shares valued at $87.1 million in 2007, 719 thousand shares valued at $35.9 million in 2008, and 42 thousand shares valued at $2.0 million in 2009. Share repurchases were restricted to amounts conducted in coordination with employee benefit programs under the terms of the February 13, 2009 issuance of Treasury Preferred Stock until complete redemption of the same preferred stock on November 18, 2009.

The Company s primary capital resource is shareholders equity, which increased $95.6 million or 23.3% in 2009 from the previous year, primarily the net result of $125.4 million in profits earned during the year, and $9.6 million in issuance of stock in connection with exercises of employee stock options, offset by $41.1 million in common dividends paid, and $2.0 million in stock repurchases.

The Company s ratio of equity to total assets was 10.16% at December 31, 2009 and December 31, 2008.

***Capital to Risk-Adjusted Assets***

The following summarizes the ratios of regulatory capital to risk-adjusted assets for the Company on the dates indicated:

| At December 31, | 2009 | 2008 | Minimum Regulatory Requirement | Well Capitalized |
|---|---|---|---|---|
| Tier I Capital | 13.20% | 10.47% | 4.00% | 6.00% |
| Total Capital | 14.50% | 11.76% | 8.00% | 10.00% |
| Leverage ratio | 7.60% | 7.36% | 4.00% | 5.00% |

The Company s risk-based capital ratios increased at December 31, 2009, compared with December 31, 2008, primarily due to equity capital increasing relatively faster than risk-weighted assets. FDIC-covered assets are included in the 20% risk-weighted category due to the loss sharing agreements.

The following summarizes the ratios of capital to risk-adjusted assets for the Bank on the dates indicated:

| At December 31, | 2009 | 2008 | Minimum Regulatory Requirement | Well Capitalized |
|---|---|---|---|---|
| Tier I Capital | 13.39% | 9.31% | 4.00% | 6.00% |
| Total Capital | 14.88% | 10.78% | 8.00% | 10.00% |
| Leverage ratio | 7.67% | 6.52% | 4.00% | 5.00% |

The Company contributed $93.7 million in capital to the Bank during 2009 to maintain the Bank s well capitalized condition following the February 6, 2009 County Bank acquisition. The risk-based capital ratios increased at December 31, 2009, compared with December 31, 2008, due to increased Tier I Capital resulting from the capital contribution from the Company and the retention of earnings, partially offset by an increase in risk-weighted assets. FDIC-covered assets are included in the 20% risk-weighted category due to the loss sharing agreements.

The Company and the Bank intend to maintain regulatory capital in excess of the highest regulatory standard, referred to as well capitalized . The Company and the Bank routinely project capital levels by analyzing forecasted earnings, credit quality, securities valuations, shareholder dividends, asset volumes, share repurchase activity, stock option exercise proceeds, and other factors. Based on current capital projections the Company and the Bank expect to maintain regulatory capital levels exceeding the well capitalized standard and pay quarterly dividends to shareholders. No assurance can be given that changes in capital management plans will not occur.

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***Deposit categories***

The Company primarily attracts deposits from local businesses and professionals, as well as through retail savings and checking accounts, and, to a more limited extent, certificates of deposit.

The following table summarizes the Company s average daily amount of deposits and the rates paid for the periods indicated:

Deposit Distribution and Average Rates Paid

| Years Ended December 31, (Dollars in thousands) | 2009 Average Balance | 2009 Percentage of Total Deposits | 2009 Rate | 2008 Average Balance | 2008 Percentage of Total Deposits | 2008 Rate | 2007 Average Balance | 2007 Percentage of Total Deposits | 2007 Rate |
|---|---|---|---|---|---|---|---|---|---|
| Noninterest bearing demand | $ 1,354,534 | 33.3% | % | $ 1,181,679 | 37.3% | % | $ 1,262,723 | 37.5% | % |
| Interest bearing: | | | | | | | | | |
| Transaction | 696,638 | 17.1% | 0.14% | 541,727 | 17.1% | 0.26% | 569,286 | 16.9% | 0.37% |
| Savings | 951,457 | 23.4% | 0.39% | 759,829 | 24.0% | 0.56% | 826,336 | 24.5% | 0.74% |
| Time less than $100 thousand | 458,117 | 11.3% | 0.98% | 193,889 | 6.1% | 2.69% | 210,039 | 6.2% | 3.31% |
| Time $100 thousand or more | 607,642 | 14.9% | 0.88% | 489,326 | 15.5% | 2.11% | 503,469 | 14.9% | 4.50% |
| Total | $ 4,068,388 | 100.0% | 0.54% | $ 3,166,450 | 100.0% | 1.07% | $ 3,371,853 | 100.0% | 1.79% |

During 2009, total average deposits increased by $901.9 million or 28.5% from 2008 due to growth in deposit accounts assumed from the County acquisition on February 6, 2009, including increases in noninterest bearing demand deposits (up $172.9 million), interest-bearing transaction accounts (up $154.9 million), savings deposits (up $191.6 million), time deposits less than $100 thousand (up $264.2 million) and time deposits $100 thousand or more (up $118.3 million).

Deposit competition was elevated during 2008. The Company modified its deposit pricing practices to retain its profitable customers. During 2008, total average deposits declined by $205.4 million or 6.1% from 2007 due to an $81.0 million decrease in noninterest bearing demand deposits, a $66.5 million decrease in savings deposits, a $27.6 million decrease in interest bearing transaction deposits, a $16.2 million decrease in time deposits less than $100 thousand and a $14.1 million decrease in time deposits $100 thousand or more.

Total time deposits were $991.4 million and $665.8 million at December 31, 2009 and 2008, respectively. The following table sets forth, by time remaining to maturity, the Company s total domestic time deposits. The Company has no foreign time deposits.

| (In thousands) | December 31, 2009 |
|---|---|
| 2010 | $ 920,827 |
| 2011 | 28,522 |
| 2012 | 18,096 |
| 2013 | 5,286 |
| 2014 | 13,358 |
| Thereafter | 5,299 |
| Total | $ 991,388 |

The following sets forth, by time remaining to maturity, the Company s domestic time deposits in amounts of $100 thousand or more:

| Deposits Over $100,000 Maturity Distribution (In thousands) | December 31, 2009 |
| --- | --- |
| Three months or less | $ 349,046 |
| Over three through six months | 160,675 |
| Over six through twelve months | 45,716 |
| Over twelve months | 18,716 |
| Total | $ 574,153 |

**Short-term Borrowings**

The following table sets forth the short-term borrowings of the Company:

Short-Term Borrowings Distribution

| At December 31, (In thousands) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Federal funds purchased | $ | $ 335,000 | $ 621,000 |
| Other borrowed funds: | | | |
| Sweep accounts | 109,332 | 119,015 | 150,097 |
| Term repurchase agreements | 99,044 | | |
| Securities sold under repurchase agreements | 3,102 | 3,260 | 7,969 |
| Line of credit | 15,700 | | 19,533 |
| Total short term borrowings | $ 227,178 | $ 457,275 | $ 798,599 |

The term repurchase agreement matures December 15, 2010.

Further detail of federal funds purchased and other borrowed funds is as follows:

| Years Ended December 31, (dollars in thousands) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Federal funds purchased balances and rates paid on outstanding amount: | | | |
| Average balance for the year | $ 107,732 | $ 411,488 | $ 596,711 |
| Maximum month-end balance during the year | 365,000 | 665,000 | 705,000 |
| Average interest rate for the year | 0.18% | 2.17% | 5.13% |
| Average interest rate at period end | % | 0.16% | 4.33% |
| Sweep accounts and rates paid on outstanding amount: | | | |
| Average balance for the year | $ 113,167 | $ 126,394 | $ 132,146 |
| Maximum month-end balance during the year | 124,557 | 134,610 | 185,449 |
| Average interest rate for the year | 0.41% | 0.57% | 0.31% |
| Average interest rate at period end | 0.35% | 0.53% | 0.41% |
| Term repurchase agreements balances and rates paid outstanding amount: | | | |
| Average balance for the year | $ 90,344 | $ | $ |
| Maximum month-end balance during the year | 99,044 | | |
| Average interest rate for the year | 1.53% | % | % |
| Average interest rate at period end | 1.55% | % | % |

**Financial Ratios**

The following table shows key financial ratios for the periods indicated:

| At and for the years ended December 31, | 2009 | 2008 | 2007 |
|---|---|---|---|
| Return on average total assets | 2.39% | 1.42% | 1.93% |
| Return on average common shareholders equity | 25.84% | 14.77% | 22.11% |
| Average shareholders equity as a percentage of: | | | |
| Average total assets | 10.31% | 9.60% | 8.75% |
| Average total loans | 16.25% | 16.65% | 16.17% |
| Average total deposits | 12.89% | 12.79% | 12.04% |
| Common dividend payout ratio | 34% | 68% | 46% |

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**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company does not currently engage in trading activities or use derivative instruments to control interest rate risk, even though such activities may be permitted with the approval of the Company s Board of Directors.

Credit risk and interest rate risk are the most significant market risks affecting the Company, and equity price risk can also affect the Company s financial results. These risks are described in the preceding sections regarding Loan Portfolio Credit Risk, and Asset/Liability and Market Risk Management. Other types of market risk, such as foreign currency exchange risk and commodity price risk, are not significant in the normal course of the Company s business activities.

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

INDEX TO FINANCIAL STATEMENTS

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## MANAGEMENT S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of Westamerica Bancorporation and subsidiaries (the Company ) is responsible for establishing and maintaining adequate internal control over financial reporting, and for performing an assessment of the effectiveness of internal control over financial reporting as of December 31, 2009. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. The Company s system of internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of Management and Directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company s assets that could have a material effect on the financial statements.

Management performed an assessment of the effectiveness of the Company s internal control over financial reporting as of December 31, 2009 based upon criteria in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ( COSO ). Based on this assessment, Management determined that the Company s internal control over financial reporting was effective as of December 31, 2009 based on the criteria in Internal Control - Integrated Framework issued by COSO.

The Company s independent registered public accounting firm has issued an attestation report on Management s assessment of the Company s internal control over financial reporting. This report is included below.

Dated February 26, 2010

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## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Westamerica Bancorporation:

We have audited Westamerica Bancorporation and subsidiaries (the Company) internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management s Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Company as of December 31, 2009 and 2008, and the related consolidated statements of income, changes in shareholders equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2009, and our report dated February 26, 2010 expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG LLP
KPMG LLP
San Francisco, California
February 26, 2010

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**CONSOLIDATED BALANCE SHEETS**
*(In thousands)*

| *December 31,* | *2009* | *2008* |
|---|---|---|
| **Assets** | | |
| Cash and cash equivalents | $ 361,135 | $ 138,883 |
| Money market assets | 442 | 341 |
| Investment securities available for sale | 384,208 | 288,454 |
| Investment securities held to maturity (fair values of $736,270 at December 31, 2009 and $950,210 at December 31, 2008) | 726,935 | 949,325 |
| Non-covered loans | 2,201,088 | 2,382,426 |
| Allowance for loan losses | (41,043) | (44,470) |
| Non-covered loans, net of allowance for loan losses | 2,160,045 | 2,337,956 |
| Covered loans | 855,301 | |
| Total loans | 3,015,346 | 2,337,956 |
| Non-covered other real estate owned | 12,642 | 3,505 |
| Covered other real estate owned | 23,297 | |
| Premises and equipment, net | 38,098 | 27,351 |
| Identifiable intangibles | 35,667 | 15,208 |
| Goodwill | 121,699 | 121,699 |
| Interest receivable and other assets | 256,032 | 150,212 |
| **Total Assets** | $ 4,975,501 | $ 4,032,934 |
| **Liabilities** | | |
| Deposits: | | |
| Noninterest bearing | $ 1,428,432 | $ 1,158,632 |
| Interest bearing: | | |
| Transaction | 669,004 | 525,153 |
| Savings | 971,384 | 745,496 |
| Time | 991,388 | 665,773 |
| Total deposits | 4,060,208 | 3,095,054 |
| Short-term borrowed funds | 227,178 | 457,275 |
| Federal Home Loan Bank advances | 85,470 | |
| Debt financing and notes payable | 26,497 | 26,631 |
| Liability for interest, taxes and other expenses | 70,700 | 44,122 |
| **Total Liabilities** | 4,470,053 | 3,623,082 |
| **Shareholders Equity** | | |
| Common Stock (no par value) | | |
| Authorized - 150,000 shares | | |
| | 366,247 | 352,265 |

| | | |
|---|---|---|
| Issued and outstanding - 29,208 at December 31, 2009 and 28,880 at December 31, 2008 | | |
| Deferred compensation | 2,485 | 2,409 |
| Accumulated Other Comprehensive Income | 3,714 | 1,040 |
| Retained earnings | 133,002 | 54,138 |
| **Total Shareholders Equity** | 505,448 | 409,852 |
| **Total Liabilities and Shareholders Equity** | $ 4,975,501 | $ 4,032,934 |

See accompanying notes to the consolidated financial statements.

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**CONSOLIDATED STATEMENTS OF INCOME**
*(In thousands, except per share data)*

| *For the years ended December 31,* | ***2009*** | ***2008*** | ***2007*** |
|---|---|---|---|
| **Interest and Fee Income** | | | |
| Loans | $ 189,801 | $ 148,659 | $ 162,242 |
| Money market assets and funds sold | 3 | 3 | 7 |
| Investment securities: | | | |
| Available for sale | | | |
| Taxable | 9,002 | 8,854 | 15,639 |
| Tax-exempt | 7,545 | 9,357 | 11,566 |
| Held to maturity | | | |
| Taxable | 13,971 | 19,237 | 23,361 |
| Tax-exempt | 21,627 | 22,359 | 23,057 |
| **Total Interest and Fee Income** | 241,949 | 208,469 | 235,872 |
| **Interest Expense** | | | |
| Transaction deposits | 999 | 1,397 | 2,093 |
| Savings deposits | 3,678 | 4,245 | 6,144 |
| Time deposits | 9,872 | 15,540 | 29,612 |
| Short-term borrowed funds | 2,132 | 9,958 | 32,393 |
| Federal Home Loan Bank advances | 1,010 | | |
| Debt financing and notes payable | 1,689 | 2,103 | 2,313 |
| **Total Interest Expense** | 19,380 | 33,243 | 72,555 |
| **Net Interest Income** | 222,569 | 175,226 | 163,317 |
| **Provision for Loan Losses** | 10,500 | 2,700 | 700 |
| **Net Interest Income After Provision for Loan Losses** | 212,069 | 172,526 | 162,617 |
| **Noninterest Income** | | | |
| Service charges on deposit accounts | 36,392 | 29,762 | 30,235 |
| Merchant credit card income | 9,068 | 10,525 | 10,841 |
| Debit card income | 4,875 | 3,769 | 3,797 |
| ATM fees and interchange | 3,693 | 2,923 | 2,824 |
| Trust fees | 1,429 | 1,227 | 1,281 |
| Financial services commissions | 583 | 830 | 1,321 |
| Gain on acquisition | 48,844 | | |
| Net losses from equity securities | | (56,955) | |
| Other | 7,127 | 5,863 | 8,979 |
| **Total Noninterest Income (Loss)** | 112,011 | (2,056) | 59,278 |
| **Noninterest Expense** | | | |
| Salaries and related benefits | 65,391 | 51,492 | 50,142 |
| Occupancy | 18,748 | 13,703 | 13,346 |
| Outsourced data processing services | 9,000 | 8,440 | 7,069 |

| | | | |
|---|---|---|---|
| Amortization of intangibles | 6,697 | 3,221 | 3,653 |
| FDIC insurance assessments | 6,260 | 518 | 401 |
| Furniture and equipment | 5,859 | 3,801 | 4,302 |
| Courier Service | 3,808 | 3,322 | 3,404 |
| Professional fees | 3,583 | 2,624 | 1,889 |
| Visa litigation | | (2,338) | 2,338 |
| Other | 21,430 | 15,978 | 14,884 |
| **Total Noninterest Expense** | 140,776 | 100,761 | 101,428 |
| **Income Before Income Taxes** | 183,304 | 69,709 | 120,467 |
| Provision for income taxes | 57,878 | 9,874 | 30,691 |
| **Net Income** | 125,426 | 59,835 | 89,776 |
| Preferred stock dividends and discount accretion | 3,963 | | |
| **Net Income Applicable to Common Equity** | $ 121,463 | $ 59,835 | $ 89,776 |
| **Average Common Shares Outstanding** | 29,105 | 28,892 | 29,753 |
| **Diluted Average Common Shares Outstanding** | 29,353 | 29,273 | 30,165 |
| **Per Common Share Data** | | | |
| Basic earnings | $ 4.17 | $ 2.07 | $ 3.02 |
| Diluted earnings | 4.14 | 2.04 | 2.98 |
| Dividends paid | 1.41 | 1.39 | 1.36 |

See accompanying notes to the consolidated financial statements.

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**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY AND COMPREHENSIVE INCOME**
*(In thousands)*

| | *Shares* | *Preferred Stock* | *Common Stock* | *Deferred Compensation* | *Accumulated Other Comprehensive Income (Loss)* | *Retained Earnings* | *Total* |
|---|---|---|---|---|---|---|---|
| **December 31, 2006** | 30,547 | $ | $ 341,529 | $ 2,734 | $ 1,850 | $ 78,122 | $ 424,235 |
| Comprehensive income | | | | | | | |
| Net income for the year 2007 | | | | | | 89,776 | 89,776 |
| Other comprehensive income, net of tax: | | | | | | | |
| Increase in net unrealized losses on securities available for sale | | | | | (6,406) | | (6,406) |
| Post-retirement benefit transition obligation amortization | | | | | 36 | | 36 |
| Total comprehensive income | | | | | | | 83,406 |
| Exercise of stock options | 342 | | 11,908 | | | | 11,908 |
| Stock option tax benefits | | | 306 | | | | 306 |
| Restricted stock activity | 12 | | 302 | 256 | | | 558 |
| Stock based compensation | | | 1,779 | | | | 1,779 |
| Stock awarded to employees | 3 | | 161 | | | | 161 |
| Purchase and retirement of stock | (1,886) | | (21,774) | | | (65,329) | (87,103) |
| Dividends | | | | | | (40,647) | (40,647) |
| **December 31, 2007** | 29,018 | | 334,211 | 2,990 | (4,520) | 61,922 | 394,603 |
| Comprehensive income | | | | | | | |
| Net income for the year 2008 | | | | | | 59,835 | 59,835 |
| Other comprehensive income, net of tax: | | | | | | | |
| Increase in net unrealized gains on securities available for sale | | | | | 5,524 | | 5,524 |
| Post-retirement benefit transition obligation amortization | | | | | 36 | | 36 |
| Total comprehensive income | | | | | | | 65,395 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Exercise of stock options | 567 | | 22,830 | | | | 22,830 |
| Stock option tax benefits | | | 1,130 | | | | 1,130 |
| Restricted stock activity | 11 | | 1,261 | (581) | | | 680 |
| Stock based compensation | | | 1,193 | | | | 1,193 |
| Stock awarded to employees | 3 | | 171 | | | | 171 |
| Purchase and retirement of stock | (719) | | (8,531) | | | (27,383) | (35,914) |
| Dividends | | | | | | (40,236) | (40,236) |
| **December 31, 2008** | 28,880 | | 352,265 | 2,409 | 1,040 | 54,138 | 409,852 |
| Comprehensive income | | | | | | | |
| Net income for the year 2009 | | | | | | 125,426 | 125,426 |
| Other comprehensive income, net of tax: | | | | | | | |
| Increase in net unrealized gains on securities available for sale | | | | | 2,638 | | 2,638 |
| Post-retirement benefit transition obligation amortization | | | | | 36 | | 36 |
| Total comprehensive income | | | | | | | 128,100 |
| Issuance of preferred stock and related warrants | | 82,519 | 1,207 | | | | 83,726 |
| Redemption of preferred stock | | (83,726) | | | | | (83,726) |
| Preferred stock dividends and discount accretion | | 1,207 | | | | (3,963) | (2,756) |
| Exercise of stock options | 361 | | 9,610 | | | | 9,610 |
| Stock option tax benefits | | | 2,188 | | | | 2,188 |
| Restricted stock activity | 7 | | 251 | 76 | | | 327 |
| Stock based compensation | | | 1,132 | | | | 1,132 |
| Stock awarded to employees | 2 | | 102 | | | | 102 |
| Purchase and retirement of stock | (42) | | (508) | | | (1,538) | (2,046) |
| Dividends | | | | | | (41,061) | (41,061) |
| **December 31, 2009** | 29,208 | $ | $ 366,247 | $ 2,485 | $ 3,714 | $ 133,002 | $ 505,448 |

See accompanying notes to the consolidated financial statements.

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## CONSOLIDATED STATEMENTS OF CASH FLOWS
*(In thousands)*

| *For the years ended December 31,* | *2009* | *2008* | *2007* |
|---|---|---|---|
| **Operating Activities:** | | | |
| Net income | $ 125,426 | $ 59,835 | $ 89,776 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization/accretion | 10,429 | 9,438 | 9,342 |
| Loan loss provision | 10,500 | 2,700 | 700 |
| Net amortization of deferred loan cost (fees) | 470 | 124 | (955) |
| (Increase) decrease in interest income receivable | (1,900) | 3,480 | 2,870 |
| Decrease (increase) in other assets | 29,880 | (17,633) | (7,073) |
| Stock option compensation expense | 1,132 | 1,193 | 1,779 |
| Excess tax benefits from stock-based compensation | (2,188) | (1,130) | (306) |
| Increase in income taxes payable | 2,316 | 141 | 586 |
| Decrease in interest expense payable | (439) | (3,527) | (901) |
| Increase (decrease) increase in other liabilities | 21,830 | (18,677) | 12,534 |
| Gain on acquisition | (48,844) | | |
| Loss on sale and impairment of investment securities | | 62,653 | |
| Gain on sale of Visa common stock | | (5,698) | |
| Gain on sale of real estate and other assets | | | (232) |
| Gain on sale of branch | 79 | | |
| Net loss on sales/write-down of fixed assets | 40 | 12 | 51 |
| Originations of loans for resale | (68) | (1,269) | (516) |
| Net proceeds from sale of loans originated for resale | 70 | 1,283 | 521 |
| Net write-down/loss on sale of property acquired in satisfaction of debt | 375 | 195 | 34 |
| **Net Cash Provided By Operating Activities** | 149,108 | 93,120 | 108,210 |
| **Investing Activities** | | | |
| Net repayments of loans | 447,277 | 106,279 | 26,184 |
| Proceeds from FDIC loss-sharing agreement | 43,176 | | |
| Net cash acquired from acquisition | 44,397 | | |
| Purchases of investment securities available for sale | (22,992) | (6,430) | (30,571) |
| Proceeds from maturity/calls of securities available for sale | 105,097 | 197,594 | 103,914 |
| Purchases of securities held to maturity | (522) | | |
| Proceeds from maturity/calls of securities held to maturity | 225,913 | 95,962 | 119,805 |
| Purchases of property, plant and equipment | (14,179) | (1,905) | (1,562) |
| Proceeds from sale of property and equipment | | | 237 |
| Purchases of FRB/FHLB* securities | | (147) | (145) |
| Proceeds from sale of FRB/FHLB/FHLMC* securities | 1,502 | 11,887 | 108 |
| Proceeds from sale of Visa common stock | | 5,698 | |
| Proceeds from sale of property acquired in satisfaction of debt | 11,082 | 311 | |
| **Net Cash Provided By Investing Activities** | 840,751 | 409,249 | 217,970 |
| **Financing Activities** | | | |

| | | | |
|---|---|---|---|
| Net decrease in deposits | (261,968) | (169,736) | (251,944) |
| Net (decrease) increase in short-term borrowings | (471,574) | (341,324) | 66,622 |
| Repayments of notes payable | | (10,000) | |
| Proceeds from issuance of preferred stock and warrants | 83,726 | | |
| Redemption of preferred stock | (83,726) | | |
| Preferred stock dividends | (2,756) | | |
| Exercise of stock options/issuance of shares | 9,610 | 22,830 | 11,908 |
| Excess tax benefits from stock-based compensation | 2,188 | 1,130 | 306 |
| Retirement of common stock including repurchases | (2,046) | (35,914) | (87,103) |
| Common stock dividends paid | (41,061) | (40,236) | (40,647) |
| **Net Cash Used In Financing Activities** | (767,607) | (573,250) | (300,858) |
| **Net Increase (Decrease) In Cash and Cash Equivalents** | 222,252 | (70,881) | 25,322 |
| **Cash and Cash Equivalents at Beginning of Year** | 138,883 | 209,764 | 184,442 |
| **Cash and Cash Equivalents at End of Year** | $ 361,135 | $ 138,883 | $ 209,764 |
| **Supplemental Disclosures:** | | | |
| Supplemental disclosure of noncash activities: | | | |
| Loans transferred to other real estate owned | $ 38,185 | $ 3,432 | $ |
| Unrealized gain (loss) on securities available for sale, net of tax | 2,638 | 5,524 | (6,406) |
| Supplemental disclosure of cash flow activity: | | | |
| Interest paid for the period | 27,558 | 36,770 | 73,456 |
| Income tax payments for the period | 36,852 | 24,056 | 30,791 |

See accompanying notes to the consolidated financial statements.

* Federal Reserve Bank ( FRB ), Federal Home Loan Bank ( FHLB ) and Federal Home Loan Mortgage Corp. ( FHLMC )

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# WESTAMERICA BANCORPORATION
# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## Note 1: Business and Accounting Policies

Westamerica Bancorporation, a registered bank holding company (the Company ), provides a full range of banking services to corporate and individual customers in Northern and Central California through its subsidiary bank, Westamerica Bank (the Bank ). The Bank is subject to competition from both financial and nonfinancial institutions and to the regulations of certain agencies and undergoes periodic examinations by those regulatory authorities.

**Summary of Significant Accounting Policies**

The consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States of America. The following is a summary of significant policies used in the preparation of the accompanying financial statements.

Accounting Estimates. Certain accounting policies underlying the preparation of these financial statements require Management to make estimates and judgments. These estimates and judgments may affect reported amounts of assets and liabilities, revenues and expenses, and disclosures of contingent assets and liabilities. The most significant of these involve the Allowance for Credit Losses, as discussed below under Allowance for Credit Losses, estimated fair values of purchased loans, as discussed below under Purchased Loans, and the evaluation of other than temporary impairment, as discussed below under Securities.

Principles of Consolidation. The consolidated financial statements include the accounts of the Company and all the Company s subsidiaries. Significant intercompany transactions have been eliminated in consolidation. The Company does not maintain or conduct transactions with any unconsolidated special purpose entities other than limited partnerships sponsored by third parties.

Cash Equivalents. Cash equivalents include Due From Banks balances and Federal Funds Sold which are both readily convertible to known amounts of cash and are generally 90 days or less from maturity at the time of purchase, presenting insignificant risk of changes in value due to interest rate changes.

Securities. Investment securities consist of debt securities of the U.S. Treasury, government sponsored entities, states, counties, municipalities, corporations, mortgage-backed securities, and equity securities. Securities transactions are recorded on a trade date basis. The Company classifies its debt and marketable equity securities in one of three categories: trading, available for sale or held to maturity. Trading securities are bought and held principally for the purpose of selling them in the near term. Held to maturity securities are those debt securities which the Company has the ability and intent to hold until maturity. Securities not included in trading or held to maturity are classified as available for sale. Trading and available for sale securities are recorded at fair value. Held to maturity securities are recorded at cost, adjusted for the amortization of premiums or accretion of discounts. Unrealized gains and losses on trading securities are included in earnings. Unrealized gains and losses, net of the related tax effect, on available for sale securities are reported as a separate component of shareholders equity until realized.

A decline in the market value of any available for sale or held to maturity security below cost that is deemed other than temporary results in a charge to earnings and the establishment of a new cost basis for the security. Unrealized investment securities losses are evaluated at least quarterly to determine whether such declines in value should be considered other than temporary and therefore be subject to immediate loss recognition in income. Although these evaluations involve significant judgment, an unrealized loss in the fair value of a debt security is generally deemed to be temporary when the fair value of the security is below the carrying value primarily due to changes in risk-free interest rates, there has not been significant deterioration in the financial condition of the issuer, and the Company does not intend to sell or be required to sell the securities before recovery of its amortized cost. An unrealized loss in the value of an equity security is generally considered temporary when the fair value of the security declined primarily due to current market conditions and not deterioration in the financial condition of the issuer, the Company expects the fair value of the security to recover in the near term and the Company does not intend to sell or be required to sell the securities before recovery of its amortized cost. Other factors that may be considered in determining whether a decline in the value of either a debt or an equity security is other than temporary include ratings by recognized rating agencies, actions of commercial banks or other lenders relative to the continued extension of credit facilities to the issuer of the security, the financial condition, capital strength and near-term prospects of the issuer, and recommendations of investment advisors or market analysts.

Purchase premiums are amortized and purchase discounts are accreted over the estimated life of the related investment security as an adjustment to yield using the effective interest method. Unamortized premiums, unaccreted discounts, and early payment premiums are recognized in interest income upon disposition of the related security. Interest and dividend income are recognized when earned. Realized gains and losses from the sale of available for sale securities are included in earnings using the specific identification method.

Loans. Loans are stated at the principal amount outstanding, net of unearned discount and unamortized deferred fees and costs. Interest is accrued daily on the outstanding principal balances. Loans which are more than 90 days delinquent with respect to interest or principal, unless they are well secured and in the process of collection, and other loans on which full recovery of principal or interest is in doubt, are placed on nonaccrual status. Interest previously accrued on loans placed on nonaccrual status is charged against interest income. In addition, some loans secured by real estate with temporarily impaired values and commercial loans to borrowers experiencing financial difficulties are placed on nonaccrual status ( performing nonaccrual loans ) even though the borrowers continue to repay the loans as scheduled. When the ability to fully collect nonaccrual loan principal is in doubt, payments received are applied against the principal balance of the loans until such time as full collection of the remaining recorded balance is expected. Any additional interest payments received after that time are recorded as interest income on a cash basis. Performing nonaccrual loans are reinstated to accrual status when improvements in credit quality eliminate the doubt as to the full collectibility of both interest and principal. Certain consumer loans or auto receivables are charged to the allowance for credit losses when they become 120 days past due. The Company recognizes a loan as impaired when, based on current information and events, it is probable that it will be unable to collect both the contractual interest and principal payments as scheduled in the loan agreement. Income recognition on impaired loans conforms to that used on nonaccrual loans.

Nonrefundable fees and certain costs associated with originating or acquiring loans are deferred and amortized as an adjustment to interest income over the contractual loan lives. Upon prepayment, unamortized loan fees, net of costs, are immediately recognized in interest income. Other fees, including those collected upon principal prepayments, are included in interest income when received. Loans held for sale are identified upon origination and are reported at the lower of cost or market value on an aggregate loan basis.

Purchased loans. Purchased loans acquired in a business combination, which include loans purchased in the County Bank ( County ) acquisition, are recorded at estimated fair value on their purchase date; the purchaser cannot carryover the related allowance for loan losses. Purchased loans are accounted for under Financial Accounting Standards Board Accounting Standard Codification ( FASB ASC ) 310-30, Loans and Debt Securities with Deteriorated Credit Quality (formerly American Institute of Certified Public Accountants ( AICPA ) Statement of Position 03-3), when the loans have evidence of credit deterioration since origination and it is probable at the date of acquisition that the Company will not collect all contractually required principal and interest payments. Evidence of credit quality deterioration as of the purchase date may include statistics such as past due and nonaccural status. Generally, acquired loans that meet the Company s definition for nonaccrual status fall within the scope of FASB ASC 310-30. The difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition is referred to as the nonaccretable difference which is included in the carrying amount of the loans. Subsequent decreases to the expected cash flows will generally result in a provision for loan losses. Subsequent increases in cash flows result in a reversal of the provision for loan losses to the extent of prior charges, or a reclassification of the difference from nonaccretable to accretable with a positive impact on interest income. Any excess of cash flows expected at acquisition over the estimated fair value is referred to as the accretable yield and is recognized into interest income over the remaining life of the loan when there is a reasonable expectation about the amount and timing of such cash flows. Further, the Company elected to analogize to ASC 310-30 and account for all other acquired loans not within the scope of ASC 310-30 using the same methodology.

Covered loans. Loans covered under loss-sharing or similar credit protection agreements with the FDIC are reported in loans exclusive of the expected reimbursement cash flows from the FDIC. Covered loans are initially recorded at fair value at the acquisition date. Subsequent decreases in the amount expected to be collected results in a provision for loan losses and a corresponding increase in the estimated FDIC reimbursement, with the estimated net loss impacting earnings. Interest is accrued daily on the outstanding principal balances. Covered loans which are more than

90 days delinquent with respect to interest or principal, unless they are well secured and in the process of collection, and other covered loans on which full recovery of principal or interest is in doubt, are placed on nonaccrual status. Interest previously accrued on covered loans placed on nonaccrual status is charged against interest income, net of estimated FDIC reimbursements of such accrued interest. In addition, some covered loans secured by real estate with temporarily impaired values and covered commercial loans to borrowers experiencing financial difficulties are placed on nonaccrual status even though the borrowers continue to repay the loans as scheduled ( covered performing nonaccrual loans ). When the ability to fully collect nonaccrual loan principal is in doubt, interest payments received are applied against the principal balance of the loans until such time as full collection of the remaining recorded balance is expected taking into consideration FDIC loss-sharing reimbursements. Any additional interest payments received after that time are recorded as interest income on a cash basis. Covered performing nonaccrual loans are reinstated to accrual status when improvements in credit quality eliminate the doubt as to the full collectibility of both interest and principal.

Allowance for Credit Losses. The allowance for credit losses is established through provisions for credit losses charged to income. Losses on loans, including impaired loans, are charged to the allowance for credit losses when all or a portion of the recorded amount of a loan is deemed to be uncollectible. Recoveries of loans previously charged off are credited to the allowance when realized. The Company s allowance for credit losses is maintained at a level considered adequate to provide for losses that can be estimated based upon specific and general conditions. These include conditions unique to individual borrowers, as well as overall credit loss experience, the amount of past due, nonperforming and classified loans, recommendations of regulatory authorities, prevailing economic conditions and other factors. A portion of the allowance is specifically allocated to impaired loans whose full collectibility is uncertain. Such allocations are determined by Management based on loan-by-loan analyses. A second allocation is based in part on quantitative analyses of historical credit loss experience, in which criticized and classified loan balances identified through an internal loan review process are analyzed using a linear regression model to determine standard loss rates. The results of this analysis are applied to current criticized and classified loan balances to allocate the reserve to the respective segments of the loan portfolio. In addition, loans with similar characteristics not usually criticized using regulatory guidelines are analyzed and reserves established based on the historical loss rates and delinquency trends, grouped by the number of days the payments on these loans are delinquent. Last, allocations are made to non-criticized and non-classified commercial loans and residential real estate loans based on historical loss rates. The remainder of the reserve is considered to be unallocated. The unallocated allowance is established to provide for probable losses that have been incurred as of the reporting date but not reflected in the allocated allowance. It addresses additional qualitative factors consistent with Management s analysis of the level of risks inherent in the loan portfolio, which are related to the risks of the Company s general lending activity. Included in the unallocated allowance is the risk of losses that are attributable to national or local economic or industry trends which have occurred but have yet been recognized in past loan charge-off history (external factors). The external factors evaluated by the Company include: economic and business conditions, external competitive issues, and other factors. Also included in the unallocated allowance is the risk of losses that are attributable to general attributes of the Company s loan portfolio and credit administration (internal factors). The internal factors evaluated by the Company include: loan review system, adequacy of lending Management and staff, loan policies and procedures, problem loan trends, concentrations of credit, and other factors. By their nature, these risks are not readily allocable to any specific category in a statistically meaningful manner and are difficult to quantify with a specific number.

Other Real Estate Owned. Other real estate owned is comprised of property acquired through foreclosure proceedings, acceptances of deeds-in-lieu of foreclosure and some vacated bank properties. Losses recognized at the time of acquiring property in full or partial satisfaction of debt are charged against the allowance for credit losses. Other real estate owned is recorded at the lower of the related loan balance or fair value of the collateral, generally based upon an independent property appraisal, less estimated disposition costs. Subsequently, other real estate owned is valued at the lower of the amount recorded at the date acquired or the then current fair value less estimated disposition costs. Subsequent losses incurred due to any decline in annual independent property appraisals are recognized as noninterest expense. Routine holding costs, such as property taxes, insurance and maintenance, and losses from sales and dispositions, are recognized as noninterest expense.

Covered Other Real Estate Owned. Other real estate owned covered under loss-sharing agreements with the FDIC is reported exclusive of expected reimbursement cash flows from the FDIC. Upon transferring covered loan collateral to covered other real estate owned status, acquisition date fair value discounts on the related loan is also transferred to covered other real estate owned. Fair value adjustments on covered other real estate owned result in a reduction of the covered other real estate carrying amount and a corresponding increase in the estimated FDIC reimbursement, with the estimated net loss charged against earnings.

Premises and Equipment. Premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation is computed substantially on the straight-line method over the estimated useful life of each type of asset. Estimated useful lives of premises and equipment range from 20 to 50 years and from 3 to 20 years, respectively. Leasehold improvements are amortized over the terms of the lease or their estimated useful life, whichever is shorter.

Intangible assets. Intangible assets are comprised of goodwill, core deposit intangibles and other identifiable intangibles acquired in business combinations. Intangible assets with definite useful lives are amortized on an accelerated basis over their respective estimated useful lives. If an event occurs that indicates the carrying amount of an intangible asset may not be recoverable, Management reviews the asset for impairment. Any goodwill and any intangible asset acquired in a purchase business combination determined to have an indefinite useful life is not amortized, but is annually evaluated for impairment.

Impairment of Long-Lived Assets. The Company reviews its long-lived and certain intangible assets for impairment whenever events or changes indicate that the carrying amount of an asset may not be recoverable. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Income taxes. The Company and its subsidiaries file consolidated tax returns. The Company accounts for income taxes in accordance with FASB ASC 740, Income Taxes, resulting in two components of income tax expense: current and deferred. Current income tax expense approximates taxes to be paid or refunded for the current period. The Company determines deferred income taxes using the balance sheet method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax bases of assets and liabilities, and recognizes enacted changes in tax rates and laws in the period in which they occur. Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. Deferred tax assets are recognized subject to Management s judgment that realization is more likely than not. A tax position that meets the more likely than not recognition threshold is measured to determine the amount of benefit to recognize. The tax position is measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon settlement. Interest and penalties are recognized as a component of income tax expense.

Derivative Instruments and Hedging Activities. The Company s accounting policy for derivative instruments requires the Company to recognize those items as assets or liabilities in the statement of financial position and measure them at fair value. Hybrid financial instruments are single financial instruments that contain an embedded derivative. The Company s accounting policy is to record certain hybrid financial instruments at fair value without separating the embedded derivative.

Stock Options. The Company applies FASB ASC 718 Compensation Stock Compensation, to account for stock based awards granted to employees using the fair value method. The Company recognizes compensation expense for restricted performance share grants over the relevant attribution period. Restricted performance share grants have no exercise price, therefore, the intrinsic value is measured using an estimated per share price at the vesting date for each restricted performance share. The estimated per share price is adjusted during the attribution period to reflect actual stock price performance. The Company s obligation for unvested outstanding restricted performance share grants is classified as a liability until the vesting date due to a cash settlement feature, at which time the issued shares become classified as shareholders equity.

Extinguishment of Debt. Gains and losses, including fees, incurred in connection with the early extinguishment of debt are charged to current earnings as reductions in noninterest income.

Postretirement Benefits. The Company uses an actuarial-based accrual method of accounting for post-retirement benefits.

Other. Securities and other property held by the Bank in a fiduciary or agency capacity are not included in the financial statements since such items are not assets of the Company or its subsidiaries.

As described in Note 2 below, the Bank acquired assets and assumed liabilities of the former County on February 6, 2009 from the Federal Deposit Insurance Corporation ( FDIC ). The acquired assets and assumed liabilities of County were measured at estimated fair values, as required by the acquisition method of accounting for business combinations (FASB ASC 805, Business Combinations, formerly FASB Statement No. 141 (revised 2007)). Management made significant estimates and exercised significant judgment in accounting for the acquisition of County. Management judgmentally assigned risk ratings to loans. The assigned risk ratings, appraised collateral values, expected cash flows, current interest rates, and statistically derived loss factors were used to measure fair values for loans. Repossessed loan collateral was primarily valued based upon appraised collateral values. Due to the loss-sharing agreements with the FDIC, the Bank recorded a receivable from the FDIC equal to 80 percent of the loss estimates embedded in the fair values of loans and repossessed loan collateral. The Bank also recorded an identifiable intangible asset representing the value of the core deposit customer base of County based on an appraisal performed by an independent third party. In determining the value of the identifiable intangible asset, the third-party appraiser used significant estimates including average lives of depository accounts, future interest rate levels, the cost of servicing various depository products, and other significant estimates. Management used quoted market prices to determine the fair value of investment securities, FHLB advances and other borrowings.

*Recently Adopted Accounting Pronouncements*

FASB ASC 805, *Business Combinations*, requires an acquirer in a business combination to recognize the assets acquired (including loan receivables), the liabilities assumed, and any noncontrolling interest in the acquiree at the acquisition date, at their fair values as of that date, with limited exceptions. The acquirer is not permitted to recognize a separate valuation allowance as of the acquisition date for loans and other assets acquired in a business combination. The revised statement requires acquisition-related costs to be expensed separately from the acquisition. It also requires restructuring costs that the acquirer expected but was not obligated to incur, to be expensed separately from the business combination. The Company applied these revised provisions in accounting for the acquisition of County.

FASB ASC 815-10, *Derivatives and Hedging,* changes the disclosure requirements for derivative instruments and hedging activities. It requires enhanced disclosures about how and why an entity uses derivatives, how derivatives and related hedged items are accounted for, and how derivatives and hedged items affect an entity s financial position, performance and cash flows. The Company had no derivative instruments designated as hedges as of December 31, 2009.

FASB ASC 820-10-55-23B, *Fair Value Measurements and Disclosures- Overall Implementation Guidance*, relates to the requirements that pertain to nonfinancial assets and nonfinancial liabilities covered by accounting guidance for Fair Value Measurements. The adoption of this guidance did not have any effect on the Company s financial statements at the date of adoption.

FASB ASC 320-10-65-1, *Investments Debt and Equity Securities Guidance related to Recognition and Presentation of Other-Than-Temporary Impairments* states that an other-than-temporary impairment (OTTI) write-down of debt securities, where fair value is below amortized cost, is triggered in circumstances where (1) an entity has the intent to sell a security, (2) it is more likely than not that the entity will be required to sell the security before recovery of its amortized cost basis, or (3) the entity does not expect to recover the entire amortized cost basis of the security. If an entity intends to sell a security or if it is more likely than not the entity will be required to sell the security before recovery, an OTTI write-down is recognized in earnings equal to the entire difference between the security s amortized cost basis and its fair value. If an entity does not intend to sell the security or it is more likely than not that it will not be required to sell the security before recovery, the OTTI write-down is separated into an amount representing the credit loss, which is recognized in earnings, and the amount related to all other factors, which is recognized in other comprehensive income. The adoption of these provisions did not have any effect on the Company s financial statements at the date of adoption.

FASB ASC 820-10-65-4, *Fair Value Measurements and Disclosures- Overall Transition Guidance related to Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly,* addresses measuring fair value in situations where markets are inactive and transactions are not orderly. In these circumstances quoted prices may not be determinative of fair value. Even if there has been a significant decrease in the volume and level of activity for an asset or liability and regardless of the valuation technique(s) used, the objective of a fair value measurement has not changed. Under these provisions price quotes for assets or liabilities in inactive markets may require adjustment due to uncertainty as to whether the underlying transactions are orderly. The adoption of these provisions did not have any effect on the Company s financial statements at the date of adoption.

FASB ASC 825-10-65-1, *Financial Instruments Overall Transition Guidance related to Interim Disclosures about Fair Value of Financial Instruments*, states that entities must disclose the fair value of financial instruments in interim reporting periods as well as in annual financial statements. The methods and assumptions used to estimate fair value as well as any changes in methods and assumptions that occurred during the reporting period must also be disclosed. The adoption of these provisions did not have any effect on the Company s financial statements at the date of adoption.

FASB ASC 855, *Subsequent Events,* establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. The accounting guidance defines: (1) the period after the balance sheet date during which Management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements, (2) the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements, and (3) the disclosures that an entity should make about events or transactions that occurred after the balance sheet date. Management has reviewed events occurring through February 26, 2010, the date the financial statements were issued and no subsequent events occurred requiring accrual or disclosure.

FASB Update 2009-05, *Measuring Liabilities at Fair Value.*
This Update provides amendments to Subtopic 820-10, Fair Value Measurements and Disclosures - Overall, for the fair value measurement of liabilities.
This Update clarifies:

In circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity is required to measure fair value by using one or more following: a) the quoted price for the identical liability when traded as an asset; b) the quoted prices for similar liabilities or similar liabilities when traded as assets; c) the income approach, such as present value technique; and/or d) the market approach, such as a technique that is based on the amount at the measurement date that the reporting entity would pay to transfer the identical liability or would receive to enter into the identical liability.

When estimating the fair value of a liability, a reporting entity is not required to include a separate input or adjustment to other inputs relating to the existence of a restriction that prevents the transfer of the liability.

Both a quoted price in an active market for the identical liability at the measurement date and the quoted price for the identical liability when traded as an asset in an active market when no adjustments to the quoted price of the asset are required are Level 1 fair value measurements.

The Company does not report liabilities at fair value on a recurring basis. The adoption of the Update did not have a material effect on the Company s financial statements at the date of adoption.

*Recently Issued Accounting Pronouncements*

In June 2009, the FASB issued FASB Statement No. 166, Accounting for Transfers of Financial Assets an amendment of the provisions contained in FASB ASC 860, Transfer and Servicing and FASB Statement No. 167, Amendments to FASB ASC 810, Consolidation. ASC 860, Transfers and Servicing, has been amended to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor s continuing involvement, if any, in transferred financial assets. Specifically to address: (1) practices that have developed since initial issuance, that are not consistent with the original intent and key requirements of that Standard and (2) concerns of financial statement users that many of the financial assets (and related obligations) that have been derecognized should continue to be reported in the financial statements of transferors. This Standard must be applied to transfers occurring on or after the effective date. Additionally, on and after the effective date, the concept of a qualifying special-purpose entity is no longer relevant for accounting purposes.

ASC 810 Consolidation, has been amended to improve financial reporting by enterprises involved with variable interest entities. Specifically to address: (1) the effects on certain provisions as a result of the elimination of the qualifying special-purpose entity concept in ASC 860, Transfers and Servicing, and (2) constituent concerns about the application of certain key provisions of the Standard, including those in which the accounting and disclosures do not always provide timely and useful information about an enterprise s involvement in a variable interest entity.

The provisions of both Standards must be applied as of the beginning of each reporting entity s first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter with early application prohibited. Management does not expect the adoption of these Standards to have a material effect on the Company s financial statement at the date of adoption, January 1, 2010.

**Note 2: Federally Assisted Acquisition of County Bank**

On February 6, 2009, the Bank purchased substantially all the assets and assumed substantially all the liabilities of County from the FDIC as Receiver of County. County operated 39 commercial banking branches primarily within California s central valley region between Sacramento and Fresno. The FDIC took County under receivership upon County s closure by the California Department of Financial Institutions at the close of business February 6, 2009. The Bank submitted a bid for the acquisition of County with the FDIC on February 3, 2009. The FDIC approved the Bank s bid upon reviewing three competing bids and determining the Bank s bid would be the least costly to the Deposit Insurance Fund. The Bank s bid included the purchase of substantially all County assets at a cost of assuming all County deposits and certain other liabilities. No cash or other consideration was paid by the Bank. Further, the Bank and the FDIC entered loss-sharing agreements regarding future losses incurred on loans and foreclosed loan collateral existing at February 6, 2009. Under the terms of the loss-sharing agreements, the FDIC absorbs 80 percent of losses and is entitled to 80 percent of loss recoveries on the first $269 million of losses, and absorbs 95 percent of losses and is entitled to 95 percent of loss recoveries on losses exceeding $269 million. The term for loss-sharing on residential real estate loans is ten years, while the term for loss-sharing on non-residential real estate loans is five years in respect to losses and eight years in respect to loss recoveries. As a result of the loss-sharing agreements with the FDIC, the Company recorded a receivable of $129 million at the time of acquisition.

The County acquisition was accounted for under the acquisition method of accounting in accordance with FASB ASC 805, Business Combinations. The statement of net assets acquired as of February 6, 2009 and the resulting bargain purchase gain are presented in the following table. The purchased assets and assumed liabilities were recorded at their respective acquisition date fair values, and identifiable intangible assets were recorded at fair value. Fair values are preliminary and subject to refinement for up to one year after the closing date of a merger as information relative to closing date fair values becomes available. A bargain purchase gain totaling $48.8 million resulted from the acquisition and is included as a component of noninterest income on the statement of income. The amount of the gain is equal to the amount by which the fair value of assets purchased exceeded the fair value of liabilities assumed. The acquisition resulted in a gain due to County s impaired capital condition at the time of the acquisition. The operations of County provided revenue of $60.7 million and net income of $10.5 million for the period of February 6, 2009 to December 31, 2009, and is included in the consolidated financial statements. County s results of operations prior to the acquisition are not included in Westamerica s statement of income.

Statement of Net Assets Acquired (at fair value)

| | At February 6, 2009 (In thousands) | |
|---|---|---|
| Assets | | |
| Cash and cash equivalents | $ | 44,668 |
| Federal funds sold | | 12,760 |
| Securities | | 173,839 |
| Loans | | 1,174,353 |
| Core deposit intangible | | 28,107 |
| Other real estate owned | | 9,332 |
| Other assets | | 181,405 |
| Total Assets | $ | 1,624,464 |
| Liabilities | | |
| Deposits | | 1,234,123 |
| Federal funds purchased and securities sold under repurchase agreements | | 153,169 |
| Other borrowed funds | | 187,252 |
| Liabilities for interest and other expenses | | 1,076 |
| Total Liabilities | | 1,575,620 |
| Net assets acquired | $ | 48,844 |

| | At February 6, 2009 (In thousands) | |
|---|---|---|
| County Bank tangible stockholder s equity | $ | 58,623 |
| Adjustments to reflect assets acquired and liabilities assumed at fair value: | | |
| Loans and leases, net | | (150,326) |
| Other real estate owned | | (5,470) |
| FDIC loss-sharing receivable (included in other assets) | | 128,962 |

| | | |
|---|---|---|
| Core deposit intangible | | 28,107 |
| Deposits | | (10,823) |
| Securities sold under repurchase agreements | | (2,061) |
| Other borrowed funds | | 1,832 |
| Bargain Purchase gain | $ | 48,844 |

The pro forma consolidated condensed statements of income for the Company and County for the years ended December 31, 2009 and 2008 are presented below. The unaudited pro forma information presented does not necessarily reflect the results of operations that would have resulted had the acquisition been completed at the beginning of the applicable periods presented, nor does it indicate the results of operations in future periods.

The pro forma purchase accounting adjustments related to loans and leases, deposits, securities sold under repurchase agreements and other borrowed funds are being accreted or amortized into income using methods that approximate a level yield over their respective estimated lives. Purchase accounting adjustments related to identifiable intangibles are being amortized and recorded as noninterest expense over their respective estimated lives using accelerated methods. The unaudited pro forma consolidated condensed statements of income do not reflect any adjustments to County s historical provision for credit losses and goodwill impairment charges.

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| | Year ended December 31, 2009 (In thousands except per share data) | | | |
|---|---|---|---|---|
| | Westamerica | County Bank | Pro Forma Adjustments | Pro Forma Combined |
| **Interest Income** | $ 199,915 | $ 73,977 | $ (4,603) | $ 269,289 |
| **Interest Expense** | 8,751 | 18,848 | (9,042) | 18,557 |
| **Net Interest Income** | 191,164 | 55,129 | 4,439 | 250,732 |
| **Provision for Credit Losses** | 10,500 | 11,734 | | 22,234 |
| **Net Interest Income after Provision for Credit Losses** | 180,664 | 43,395 | 4,439 | 228,498 |
| **Noninterest Income** | 53,560 | 14,122 | 48,844 | 116,526 |
| **Noninterest Expense** | 99,265 | 40,926 | 4,144 | 144,335 |
| **Income Before Taxes** | 134,959 | 16,591 | 49,139 | 200,689 |
| **Income Tax Provision** | 48,585 | 6,977 | 20,663 | 76,225 |
| **Net Income** | $ 86,374 | $ 9,614 | $ 28,476 | $ 124,464 |
| **Preferred dividends and discount accretion** | | | | |
| **Net Income Applicable to Common Equity** | $ 82,411 | $ 9,614 | $ 28,476 | $ 120,501 |
| **Earnings Per Common Share** | $ 2.83 | $ 0.33 | $ 0.98 | $ 4.14 |
| **Diluted Earnings Per Common Share** | 2.81 | 0.33 | 0.97 | 4.11 |
| **Average Common Shares Outstanding** | 29,105 | | | |
| **Diluted Average Common Shares Outstanding** | 29,353 | | | |

| | Year ended December 31, 2008 (In thousands except per share data) | | | |
|---|---|---|---|---|
| | Westamerica | County Bank | Pro Forma Adjustments | Pro Forma Combined |
| **Interest Income** | $ 208,469 | $ 117,175 | $ (4,477) | $ 321,167 |
| **Interest Expense** | 33,243 | 40,462 | (9,717) | 63,988 |
| **Net Interest Income** | 175,226 | 76,713 | 5,240 | 257,179 |
| **Provision for Credit Losses** | 2,700 | 55,370 | | 58,070 |
| **Net Interest Income after Provision for Credit Losses** | 172,526 | 21,343 | 5,240 | 199,109 |
| **Noninterest (Loss) Income** | (2,056) | 5,775 | 48,844 | 52,563 |
| **Noninterest Expense** | 100,761 | 115,774 | 5,989 | 222,524 |
| **Income (Loss) Before Taxes** | 69,709 | (88,656) | 48,095 | 29,148 |

| | | | | |
|---|---|---|---|---|
| **Income Tax Provision** | 9,874 | 7,381 | 20,224 | 37,479 |
| **Net Income (Loss)** | $ 59,835 | $ (96,037) | $ 27,871 | $ (8,331) |
| **Net Income (Loss) Applicable to Common Equity** | $ 59,835 | $ (96,037) | $ 27,871 | $ (8,331) |
| **Earnings (Loss) Per Common Share** | $ 2.07 | $ (3.32) | $ 0.96 | $ (0.29) |
| **Diluted Earnings (Loss) Per Common Share** | 2.04 | (3.28) | 0.95 | (0.28) |
| **Average Common Shares Outstanding** | 28,892 | | | |
| **Diluted Average Common Shares Outstanding** | 29,273 | | | |

**Note 3: Investment Securities**

The amortized cost, unrealized gains and losses, and estimated market value of the available for sale investment securities portfolio as of December 31, 2009, follows:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Market Value |
|---|---|---|---|---|
| | (In thousands) | | | |
| U.S. Treasury securities | $ 2,987 | $ | $ | $ 2,987 |
| Securities of U.S. Government sponsored entities | 21,018 | 48 | (25) | 21,041 |
| Mortgage backed securities | 143,625 | 2,504 | (124) | 146,005 |
| Obligations of States and political subdivisions | 155,093 | 4,077 | (977) | 158,193 |
| Collateralized mortgage obligations | 40,981 | 652 | (223) | 41,410 |
| Asset-backed securities | 10,000 | | (1,661) | 8,339 |
| FHLMC and FNMA stock | 824 | 750 | (1) | 1,573 |
| Other securities | 2,778 | 1,926 | (44) | 4,660 |
| Total | $ 377,306 | $ 9,957 | $ (3,055) | $ 384,208 |

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The amortized cost, unrealized gains and losses, and estimated market value of the held to maturity investment securities portfolio as of December 31, 2009, follows:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Market Value |
|---|---|---|---|---|
| | (In thousands) | | | |
| Mortgage backed securities | $ 61,893 | $ 1,752 | $ | $ 63,645 |
| Obligations of States and political subdivisions | 516,596 | 12,528 | (2,190) | 526,934 |
| Collateralized mortgage obligations | 148,446 | 3,352 | (6,107) | 145,691 |
| Total | $ 726,935 | $ 17,632 | $ (8,297) | $ 736,270 |

The amortized cost, unrealized gains and losses, and estimated market value of the available for sale investment securities portfolio as of December 31, 2008, follows:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Market Value |
|---|---|---|---|---|
| | (In thousands) | | | |
| U.S. Treasury securities | $ 3,014 | $ 68 | $ | $ 3,082 |
| Securities of U.S. Government sponsored entities | 11,019 | 71 | (13) | 11,077 |
| Mortgage backed securities | 40,302 | 941 | (3) | 41,240 |
| Obligations of States and political subdivisions | 156,602 | 5,042 | (598) | 161,046 |
| Collateralized mortgage obligations | 61,565 | 143 | (1,857) | 59,851 |
| Asset-backed securities | 9,999 | | (3,552) | 6,447 |
| FHLMC and FNMA stock | 824 | | (3) | 821 |
| Other securities | 2,778 | 2,222 | (110) | 4,890 |
| Total | $ 286,103 | $ 8,487 | $ (6,136) | $ 288,454 |

The amortized cost, unrealized gains and losses, and estimated market value of the held to maturity investment securities portfolio as of December 31, 2008, follows:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Market Value |
|---|---|---|---|---|
| | (In thousands) | | | |
| Securities of U.S. Government sponsored entities | $ 110,000 | $ 1,731 | $ | $ 111,731 |
| Mortgage backed securities | 85,676 | 867 | (299) | 86,244 |
| Obligations of States and political subdivisions | 545,237 | 12,983 | (2,875) | 555,345 |
| Collateralized mortgage obligations | 208,412 | 1,744 | (13,266) | 196,890 |
| Total | $ 949,325 | $ 17,325 | $ (16,440) | $ 950,210 |

The amortized cost and estimated market value of securities as of December 31, 2009, by contractual maturity, are shown in the following table:

| | Securities Available | Securities Held |
|---|---|---|

| | for Sale | | to Maturity | |
|---|---|---|---|---|
| | Amortized Cost | Estimated Market Value | Amortized Cost | Estimated Market Value |
| | (In thousands) | | | |
| Maturity in years: | | | | |
| 1 year or less | $ 12,763 | $ 12,852 | $ 8,303 | $ 8,389 |
| 1 to 5 years | 86,757 | 88,759 | 58,111 | 60,075 |
| 5 to 10 years | 61,532 | 62,933 | 413,720 | 421,955 |
| Over 10 years | 28,046 | 26,016 | 36,462 | 36,515 |
| Subtotal | 189,098 | 190,560 | 516,596 | 526,934 |
| Mortgage-backed securities and collateralized mortgage obligations | 184,606 | 187,415 | 210,339 | 209,336 |
| Other securities | 3,602 | 6,233 | | |
| Total | $ 377,306 | $ 384,208 | $ 726,935 | $ 736,270 |

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The amortized cost and estimated market value of securities as of December 31, 2008, by contractual maturity, are shown in the following table:

| | Securities Available for Sale | | Securities Held to Maturity | |
|---|---|---|---|---|
| | Amortized Cost | Estimated Market Value | Amortized Cost | Estimated Market Value |
| | (In thousands) | | | |
| Maturity in years: | | | | |
| 1 year or less | $ 17,422 | $ 17,528 | $ 115,593 | $ 117,375 |
| 1 to 5 years | 69,815 | 71,664 | 39,972 | 40,674 |
| 5 to 10 years | 72,482 | 75,431 | 396,275 | 405,283 |
| Over 10 years | 20,916 | 17,029 | 103,396 | 103,743 |
| Subtotal | 180,635 | 181,652 | 655,236 | 667,075 |
| Mortgage-backed | 101,866 | 101,091 | 294,089 | 283,135 |
| Other securities | 3,602 | 5,711 | | |
| Total | $ 286,103 | $ 288,454 | $ 949,325 | $ 950,210 |

Expected maturities of mortgage-backed securities can differ from contractual maturities because borrowers have the right to call or prepay obligations with or without call or prepayment penalties. In addition, such factors as prepayments and interest rates may affect the yield on the carrying value of mortgage-backed securities. At December 31, 2009 and 2008, the Company had no high-risk collateralized mortgage obligations as defined by regulatory guidelines.

An analysis of gross unrealized losses of the available for sale investment securities portfolio as of December 31, 2009, follows:

| | Less than 12 months | | 12 months or longer | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | (In thousands) | | | | | |
| U.S. Treasury securities | $ 2,987 | $ | $ | $ | $ 2,987 | $ |
| Securities of U.S. Government sponsored entities | 19,979 | (25) | | | 19,979 | (25) |
| Mortgage backed securities | 17,885 | (124) | | | 17,885 | (124) |
| Obligations of States and political subdivisions | 25,050 | (795) | 3,866 | (182) | 28,916 | (977) |
| Collateralized mortgage obligations | 9,896 | (37) | 5,002 | (186) | 14,898 | (223) |
| Asset-backed securities | | | 8,339 | (1,661) | 8,339 | (1,661) |
| FHLMC and FNMA stock | 4 | (1) | | | 4 | (1) |
| Other securities | | | 1,956 | (44) | 1,956 | (44) |
| Total | $ 75,801 | $ (982) | $ 19,163 | $ (2,073) | $ 94,964 | $ (3,055) |

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An analysis of gross unrealized losses of the held to maturity investment securities portfolio as of December 31, 2009, follows:

| | Less than 12 months | | 12 months or longer | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | (In thousands) | | | | | |
| Obligations of States and political subdivisions | $ 46,111 | $ (995) | $ 16,964 | $ (1,195) | $ 63,075 | $ (2,190) |
| Collateralized mortgage obligations | 7,639 | (42) | 30,674 | (6,065) | 38,313 | (6,107) |
| Total | $ 53,750 | $ (1,037) | $ 47,638 | $ (7,260) | $ 101,388 | $ (8,297) |

The unrealized losses on the Company s investments in collateralized mortgage obligations ( CMOs ) and asset backed securities were caused by market conditions for these types of investments. The Company evaluates these securities on a quarterly basis including changes in security ratings issued by ratings agencies, delinquency and loss information with respect to the underlying collateral, and changes in the levels of subordination for the Company s particular position within the repayment structure and remaining credit enhancement as compared to expected credit losses of the underlying collateral. Substantially all of these securities continue to be AAA rated by one or more major rating agencies. Because the Company does not intend to sell or be required to sell these securities and we expect to recover the amortized cost basis of the securities, the Company does not consider those investments to be other-than temporarily impaired as of December 31, 2009.

The unrealized losses on the Company s investments in obligations of states and political subdivisions were caused by conditions in the municipal securities markets and certain securities being insured by one of the monoline insurance companies. The Company evaluates these securities quarterly to determine if a change in security rating has occurred or the municipality has experienced any financial difficulties. Substantially all of these securities continue to be investment grade rated. Because the Company believes that it will collect all principal and interest due and does not intend to sell or be required to sell the securities, the Company does not consider those investments to be other-than-temporarily impaired as of December 31, 2009.

The fair values of the investment securities could decline in the future if the overall general economy deteriorates or the liquidity for securities declines. As a result, it is reasonably possible that other than temporary impairments may occur in the future given the current economic environment.

As of December 31, 2009, $1.03 billion of investment securities were pledged to secure public deposits and short-term funding needs, compared to $1.13 billion at December 31, 2008.

An analysis of gross unrealized losses of the available for sale investment securities portfolio as of December 31, 2008, follows:

| | Less than 12 months | | 12 months or longer | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | (In thousands) | | | | | |
| Securities of U.S. Government sponsored entities | $ 9,988 | $ (13) | $ | $ | $ 9,988 | $ (13) |
| Mortgage backed securities | | | 1,680 | (3) | 1,680 | (3) |
| Obligations of States and political subdivisions | 8,817 | (470) | 2,171 | (128) | 10,988 | (598) |

| | | | | | | |
|---|---|---|---|---|---|---|
| Collateralized mortgage obligations | 11,527 | (595) | 25,085 | (1,262) | 36,612 | (1,857) |
| Asset-backed securities | | | 6,447 | (3,552) | 6,447 | (3,552) |
| FHLMC and FNMA stock | 3 | (3) | | | 3 | (3) |
| Other securities | | | 1,890 | (110) | 1,890 | (110) |
| Total | $ 30,335 | $ (1,081) | $ 37,273 | $ (5,055) | $ 67,608 | $ (6,136) |

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An analysis of gross unrealized losses of the held to maturity investment securities portfolio as of December 31, 2008, follows:

| | Less than 12 months | | 12 months or longer | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | (In thousands) | | | | | |
| Mortgage backed securities | $ 22,401 | $ (286) | $ 3,886 | $ (13) | $ 26,287 | $ (299) |
| Obligations of States and political subdivisions | 73,205 | (2,846) | 4,713 | (29) | 77,918 | (2,875) |
| Collateralized mortgage obligations | 40,379 | (10,925) | 24,037 | (2,341) | 64,416 | (13,266) |
| Total | $ 135,985 | $ (14,057) | $ 32,636 | $ (2,383) | $ 168,621 | $ (16,440) |

During 2008, the Company recognized $62.7 million in losses on the sale of securities and other than temporary charges on FHLMC and FNMA stock and other securities.

**Note 4: Loans and Allowance for Credit Losses**

A summary of the major categories of non-covered and covered loans outstanding is shown in the following tables:

| | At December 31, 2009 | At December 31, 2008 |
|---|---|---|
| | (In thousands) | |
| Non-covered loans: | | |
| Commercial | $ 498,594 | $ 524,786 |
| Commercial real estate | 801,008 | 817,423 |
| Construction | 32,156 | 52,664 |
| Residential real estate | 371,197 | 458,447 |
| Consumer installment & other | 498,133 | 529,106 |
| Gross Loans | 2,201,088 | 2,382,426 |
| Allowance for loan losses | (41,043) | (44,470) |
| Net Loans | $ 2,160,045 | $ 2,337,956 |

The carrying amount of the covered loans at December 31, 2009, consisted of impaired and non impaired purchased loans in the following table (refined).

| | Impaired Purchased Loans | Non Impaired Purchased Loans | Total Covered Loans |
|---|---|---|---|
| | (In thousands) | | |
| Covered loans: | | | |
| Commercial | $ 8,538 | $ 244,811 | $ 253,349 |
| Commercial real estate | 19,870 | 425,570 | 445,440 |

| | | | |
|---|---|---|---|
| Construction | 14,378 | 26,082 | 40,460 |
| Residential real estate | 138 | 18,383 | 18,521 |
| Consumer installment & other | 272 | 97,259 | 97,531 |
| Total loans | $ 43,196 | $ 812,105 | $ 855,301 |

The Company pledges loans to secure borrowings from the Federal Home Loan Bank (FHLB). At December 31, 2009, loans pledged to secure borrowing totaled $196.4 million. The FHLB does not have the right to sell or repledge such loans.

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Since the acquisition date, February 6, 2009, the Company has refined certain of its preliminary acquisition accounting adjustments based on additional information as of February 6, 2009. This additional information resulted in a refinement to the credit risk discount allocated to impaired and non impaired loans, which is reflected in the adjusted fair values of impaired and non impaired loans as detailed below.

The following table represents the non impaired purchased loans receivable at the acquisition date of February 6, 2009. The amounts include principal only and do not reflect accrued interest as of the date of acquisition or beyond (dollars in thousands):

| | |
|---|---|
| Gross contractual loan principal payment receivable | $ 1,151,972 |
| Estimate of contractual principal not expected to be collected | (72,625) |
| Fair value of non impaired purchased loans receivable | $ 1,093,809 |

The Company applied the cost recovery method to impaired purchased loans at the acquisition date of February 6, 2009 due to the uncertainty as to the timing of expected cash flows as reflected in the following table (dollars in thousands):

| | |
|---|---|
| Contractually required payments receivable (including interest) | $ 209,842 |
| Nonaccretable difference | (129,298) |
| Cash flows expected to be collected | 80,544 |
| Accretable difference | |
| Fair value of loans acquired | $ 80,544 |

Changes in the carrying amount of impaired purchased loans were as follows for the year ended December 31, 2009 (dollars in thousands):

| | |
|---|---|
| Carrying amount at the beginning of the period (refined) | $ 80,544 |
| Reductions during the period | (37,348) |
| Carrying amount at the end of the period | $ 43,196 |

Impaired purchased loans had an unpaid principal balance (less prior charge-offs) of $164 million and $70 million at February 6, 2009 and December 31, 2009, respectively.

There were no loans held for sale at December 31, 2009 and 2008.

The following summarizes the allowance for credit losses of the Company for the periods indicated:

| | 2009 | 2008 | 2007 |
|---|---|---|---|
| Balance at January 1, | $ 47,563 | $ 55,799 | $ 59,023 |
| Provision for loan losses | 10,500 | 2,700 | 700 |
| Provision for unfunded credit commitment losses | (400) | (200) | (400) |
| Loans charged off | (17,267) | (12,413) | (5,681) |
| Recoveries of loans previously charged off | 3,340 | 1,677 | 2,157 |
| Balance as of December 31, | $ 43,736 | $ 47,563 | $ 55,799 |
| Components: | | | |
| Allowance for loan losses | $ 41,043 | $ 44,470 | $ 52,506 |
| Reserve for unfunded credit commitments | 2,693 | 3,093 | 3,293 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Allowance for credit losses | $ | 43,736 | $ | 47,563 | $ | 55,799 |

At December 31, 2009, non-covered specific impaired loans were $2.4 million compared with $6.8 million at December 31, 2008. Total reserves allocated to these loans were $617 thousand at December 31, 2009 and $1.9 million at December 31, 2008. For the year ended December 31, 2009, the average recorded net investment in non-covered impaired loans was approximately $5.3 million compared with $7.0 million and $139 thousand, for the years ended December 31, 2008 and 2007, respectively. The Company had no troubled debt restructurings at December 31, 2009.

Non-covered nonaccrual loans at December 31, 2009 and 2008 were $19.9 million and $10.0 million, respectively. The following is a summary of the effect of nonaccrual loans on interest income for the years ended December 31:

| | 2009 | 2008 | 2007 |
|---|---|---|---|
| | | (In thousands) | |
| Interest income that would have been recognized had the loans performed in accordance with their original terms | $ 5,195 | $ 665 | $ 428 |
| Less: Interest income recognized on nonaccrual loans | (2,074) | (511) | (474) |
| Total reduction (addition) of interest income | $ 3,121 | $ 154 | $ (46) |

There were no commitments to lend additional funds to borrowers whose loans were on nonaccrual status at December 31, 2009.

**Note 5: Concentration of Credit Risk**

The Company s business activity is with customers in Northern and Central California. The loan portfolio is well diversified, although the Company has significant credit arrangements that are secured by real estate collateral. In addition to real estate loans outstanding as disclosed in Note 4, the Company had loan commitments and standby letters of credit related to real estate loans of $12.8 million and $14.6 million at December 31, 2009 and 2008, respectively. The Company requires collateral on all real estate loans with loan-to-value ratios generally no greater than 75% on commercial real estate loans and no greater than 80% on residential real estate loans at origination.

**Note 6: Premises and Equipment**

Premises and equipment as of December 31 consisted of the following:

| | Cost | Accumulated Depreciation and Amortization | Net Book Value |
|---|---|---|---|
| | | (In thousands) | |
| 2009 | | | |
| Land | $ 11,490 | $ | $ 11,490 |
| Buildings and improvements | 43,833 | (21,786) | 22,047 |
| Leasehold improvements | 6,140 | (5,012) | 1,128 |
| Furniture and equipment | 15,551 | (12,118) | 3,433 |
| Total | $ 77,014 | $ (38,916) | $ 38,098 |
| 2008 | | | |
| Land | $ 8,858 | $ | $ 8,858 |
| Buildings and improvements | 33,910 | (20,156) | 13,754 |
| Leasehold improvements | 5,887 | (5,002) | 885 |
| Furniture and equipment | 15,269 | (11,415) | 3,854 |
| Total | $ 63,924 | $ (36,573) | $ 27,351 |

Depreciation of premises and equipment included in noninterest expense amounted to $3.3 million in 2009, $2.9 million in 2008, and $3.3 million in 2007.

**Note 7: Goodwill and Identifiable Intangible Assets**

The Company has recorded goodwill and other identifiable intangibles associated with purchase business combinations. Goodwill is not amortized, but is periodically evaluated for impairment. The Company did not recognize impairment during the years ended December 31, 2009 and December 31, 2008. Identifiable intangibles are amortized to their estimated residual values over their expected useful lives. Such lives and residual values are also periodically reassessed to determine if any amortization period adjustments are indicated. During the year ended December 31, 2009 and December 31, 2008, no such adjustments were recorded.

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The changes in the carrying value of goodwill were ($ in thousands):

| | | |
|---|---|---|
| December 31, 2007 | $ | 121,719 |
| Recognition of stock option tax benefits for the exercise of options converted upon merger | | (20) |
| December 31, 2008 | $ | 121,699 |
| December 31, 2009 | $ | 121,699 |

The gross carrying amount of intangible assets and accumulated amortization was ($ in thousands):

| | December 31, | | | |
|---|---|---|---|---|
| | 2009 | | 2008 | |
| | Gross Carrying Amount | Accumulated Amortization | Gross Carrying Amount | Accumulated Amortization |
| Core Deposit Intangibles | $ 51,538 | $ (19,160) | $ 24,383 | $ (13,426) |
| Merchant Draft Processing Intangible | 10,300 | (7,011) | 10,300 | (6,049) |
| Total Intangible Assets | $ 61,838 | $ (26,171) | $ 34,683 | $ (19,475) |

As of December 31, 2009, the current year and estimated future amortization expense for intangible assets was ($ in thousands):

| | Core Deposit Intangibles | Merchant Draft Processing Intangible | Total |
|---|---|---|---|
| Twelve months ended December 31, 2009 (actual) | $ 5,735 | $ 962 | $ 6,697 |
| Estimate for year ended December 31, 2010 | 5,361 | 774 | 6,135 |
| 2011 | 4,817 | 624 | 5,441 |
| 2012 | 4,372 | 500 | 4,872 |
| 2013 | 3,842 | 400 | 4,242 |
| 2014 | 3,516 | 324 | 3,840 |
| 2015 | 3,193 | 262 | 3,455 |

**Note 8: Deposits and Borrowed Funds**

Debt financing and notes payable, including the unsecured obligations of the Company, as of December 31, were as follows:

| | 2009 | 2008 |
|---|---|---|
| | (In thousands) | |
| Senior fixed-rate note(1) | $ 15,000 | $ 15,000 |
| Subordinated fixed-rate note(2) | 11,497 | 11,631 |
| Total debt financing and notes payable Parent | $ 26,497 | $ 26,631 |

(1) Senior note, issued by

Westamerica Bancorporation, originated in October 2003 and maturing October 31, 2013. Interest of 5.31% per annum is payable semiannually on April 30 and October 31, with original principal payment due at maturity.

(2) Subordinated debt, assumed by Westamerica Bancorporation March 1, 2005, originated February 22, 2001. Par amount $10 million, interest of 10.2% per annum, payable semiannually. Matures February 22, 2031, redeemable February 22, 2011 at a premium and February 22, 2021 at par.

The senior note is subject to financial covenants requiring the Company to maintain, at all times, certain minimum levels of consolidated tangible net worth and maximum levels of capital debt. The Company believes it is in compliance with all of the covenants in the senior note indenture as of December 31, 2009.

Short-term borrowed funds include federal funds purchased, business customers sweep accounts, outstanding amounts under a $35 million unsecured line of credit, and securities sold with repurchase agreements which are held in the custody of independent securities brokers. Interest paid on time deposits with balances in excess of $100 thousand was $5.4 million in 2009 and $10.3 million in 2008.

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The following table summarizes deposits and borrowed funds of the Company for the periods indicated:

| | 2009 | | | 2008 | | |
|---|---|---|---|---|---|---|
| | Balance At December 31, | Average Balance | Weighted Average Rate | Balance At December 31, | Average Balance | Weighted Average Rate |
| | | (In thousands) | | | (In thousands) | |
| Federal funds purchased | $ | $ 107,732 | 0.18% | $ 335,000 | $ 411,488 | 2.17% |
| Sweep accounts | 109,332 | 113,167 | 0.41 | 119,015 | 126,394 | 0.57 |
| Term repurchase agreements | 99,044 | 90,344 | 1.53 | | | |
| Federal Home Loan Bank advances | 85,470 | 79,417 | 1.25 | | | |
| Securities sold under repurchase agreements | 3,102 | 2,991 | 0.61 | 3,260 | 6,698 | 1.87 |
| Line of credit | 15,700 | 2,071 | 3.13 | | 4,858 | 3.47 |
| Time deposits Over $100 thousand | 574,153 | 607,642 | 0.88 | 476,604 | 489,326 | 2.11 |

| | 2009 Highest Balance at Any Month-end | 2008 Highest Balance at Any Month-end |
|---|---|---|
| | (In thousands) | |
| Federal funds purchased | $ 365,000 | $ 665,000 |
| Sweep accounts | 124,557 | 134,610 |
| Term repurchase agreement | 98,964 | |
| Federal Home Loan Bank advances | 86,916 | |
| Securities sold under repurchase agreements | 3,567 | 8,644 |
| Line of credit | 17,877 | 17,808 |

**Note 9: Shareholders Equity**

On February 13, 2009, the Company issued to the United States Department of the Treasury (the Treasury ) 83,726 shares of Series A Fixed Rate Cumulative Perpetual Preferred Stock (the Series A Preferred Stock ), having a liquidation preference of $1,000 per share. The structure of the Series A Preferred Stock included cumulative dividends at a rate of 5% per year for the first five years and thereafter at a rate of 9% per year. On September 2, 2009 and November 18, 2009, the Company redeemed 41,863 shares and 41,863 shares, respectively, of its Series A Preferred Stock at $1,000 per share. Prior to redemption, under the terms of the Series A Preferred Stock, the Company could not declare or pay any dividends or make any distribution on its common stock, other than regular quarterly cash dividends not exceeding $0.35 or dividends payable only in shares of its common stock, or repurchase its common stock or other equity or capital securities, other than in connection with benefit plans consistent with past practice and certain other circumstances specified in the Securities Purchase Agreement with the Treasury. The Treasury, as part of the preferred stock issuance, received a warrant to purchase 246,640 shares of the Company s common stock at an exercise price of $50.92. The proceeds from Treasury were allocated based on the relative fair value of the warrant as compared with the fair value of the preferred stock. The fair value of the warrant was determined using a valuation model which incorporates assumptions including the Company s common stock price, dividend yield, stock price volatility, the risk-free interest rate, and other assumptions. The Company allocated $1.2 million of the proceeds from the Series A Preferred Stock to the warrant. The discount on the preferred stock was accreted to par value during the term the Series A Preferred Stock was outstanding, and reported as a reduction to net income applicable to common equity over that period.

The Company grants stock options and restricted performance shares to employees in exchange for employee services, pursuant to the shareholder-approved 1995 Stock Option Plan, which was amended and restated in 2003. Stock options are granted with an exercise price equal to the fair market value of the related common stock on the grant date and generally become exercisable in equal annual installments over a three-year period with each installment vesting on the anniversary date of the grant. Each stock option has a maximum ten-year term. A restricted performance share grant becomes vested after three years of being awarded, provided the Company has attained its performance goals for such three-year period.

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The following table summarizes information about stock options granted under the Plans as of December 31, 2009. The intrinsic value is calculated as the difference between the market value as of December 31, 2009 and the exercise price of the shares. The market value as of December 31, 2009 was $55.37 as reported by the NASDAQ Global Select Market:

| | Options Outstanding | | | | Options Exercisable | | | |
|---|---|---|---|---|---|---|---|---|
| Range of Exercise Price | Number Outstanding at 12/31/2009 (in thousands) | Aggregate Intrinsic Value (in thousands) | Weighted Average Remaining Contractual Life (yrs) | Weighted Average Exercise Price | Number Exercisable at 12/31/2009 | Aggregate Intrinsic Value (in thousands) | Weighted Average Remaining Contractual Life (yrs) | Weighted Average Exercise Price |
| 20 - 25 | 1 | $ 38 | 1.4 | $ 24 | 1 | $ 38 | 1.4 | $ 24 |
| 35 - 40 | 586 | 9,580 | 1.7 | 39 | 586 | 9,580 | 1.7 | 39 |
| 40 - 45 | 565 | 7,731 | 5.6 | 42 | 331 | 4,834 | 3.1 | 41 |
| 45 - 50 | 685 | 4,608 | 5.9 | 49 | 496 | 3,126 | 5.1 | 49 |
| 50 - 55 | 726 | 2,452 | 6.6 | 52 | 726 | 2,452 | 6.6 | 52 |
| $20 - 55 | 2,563 | $ 24,409 | 5.0 | 46 | 2,140 | $ 20,030 | 4.4 | 46 |

The Company applies the Roll-Geske option pricing model (Modified Roll) to determine grant date fair value of stock option grants. This model modifies the Black-Scholes Model to take into account dividends and American options. During the twelve months ended December 31, 2009, 2008 and 2007, the Company granted 246 thousand, 256 thousand, and 242 thousand stock options, respectively. The following weighted average assumptions were used in the option pricing to value stock options granted in the periods indicated:

| For the twelve months ended December 31, | 2009 | 2008 | 2007 |
|---|---|---|---|
| Expected volatility*1 | 18% | 15% | 14% |
| Expected life in years*2 | 4.0 | 4.0 | 4.0 |
| Risk-free interest rate*3 | 1.25% | 2.66% | 4.89% |
| Expected dividend yield | 3.41% | 2.78% | 2.82% |
| Fair value per award | $ 4.51 | $ 6.77 | $ 6.02 |

*1 Measured using daily price changes of Company s stock over respective expected term of the option and the implied volatility derived from the market prices of the Company s stock and traded options.

*2 The number of years that the Company estimates that the options will be outstanding prior to exercise.

*3 The risk-free rate over the expected life based on the US Treasury yield curve in effect at the time of the grant.

Employee stock option grants are being expensed by the Company over the grants three year vesting period. The Company issues new shares upon the exercise of options. The number of shares authorized to be issued for options is 3.4 million.

A summary of option activity during the twelve months ended December 31, 2009 is presented below:

| | Shares (In Thousands) | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (years) |
|---|---|---|---|
| Outstanding at January 1, 2009 | 2,469 | $ 42.82 | |
| Granted | 246 | 43.02 | |
| Warrants issued to U.S. Treasury | 247 | 50.92 | |
| Exercised | (361) | 26.47 | |
| Forfeited or expired | (38) | 47.34 | |
| Outstanding at December 31, 2009 | 2,563 | 45.84 | 5.0 |
| Exercisable at December 31, 2009 | 2,140 | 46.01 | 4.4 |

A summary of the Company s nonvested option activity during the twelve months ended December 31, 2009 is presented below:

| | Shares (In Thousands) | Weighted Average Grant Date Fair Value |
|---|---|---|
| Nonvested at January 1, 2009 | 391 | |
| Granted | 246 | |
| Vested | (184) | |
| Forfeited | (30) | |
| Nonvested at December 31, 2009 | 423 | $ 5.42 |

The weighted average estimated grant date fair value for options granted under the Company s stock option plan during the twelve months ended December 31, 2009, 2008 and 2007 was $4.51, $6.77 and $6.02 per share, respectively. The total remaining unrecognized compensation cost related to nonvested awards as of December 31, 2009 is $1.2 million and the weighted average period over which the cost is expected to be recognized is 1.6 years.
The total intrinsic value of options exercised during the twelve months ended December 31, 2009, 2008 and 2007 was $8.9 million, $7.7 million and $3.7 million, respectively. The total fair value of RPSs that vested during the twelve months ended December 31, 2009, 2008 and 2007 was $443 thousand, $705 thousand and $607 thousand, respectively. The total fair value of options vested during the twelve months ended December 31, 2009, 2008 and 2007 was $1.2 million, $1.8 million and $2.6 million, respectively. The actual tax benefit recognized for the tax deductions from the exercise of options totaled $2.2 million, $1.1 million and $306 thousand, respectively, for the twelve months ended December 31, 2009, 2008 and 2007.
A summary of the status of the Company s restricted performance shares as of December 31, 2009 and 2008 and changes during the twelve months ended on those dates, follows (in thousands):

| | 2009 | 2008 |
|---|---|---|
| Outstanding at January 1, | 44 | 38 |
| Granted | 19 | 28 |
| Issued upon vesting | (9) | (14) |
| Forfeited | (5) | (8) |
| Outstanding at December 31, | 49 | 44 |

As of December 31, 2009 and 2008, the restricted performance shares had a weighted-average contractual life of 1.4 years and 1.6 years, respectively. The compensation cost that was charged against income for the Company s restricted performance shares granted was $960 thousand and $785 thousand for the twelve months ended December 31, 2009 and 2008, respectively. There were no stock appreciation rights or incentive stock options granted in the twelve months ended December 31, 2009 and 2008.
The Company repurchases and retires its common stock in accordance with Board of Directors approved share repurchase programs. At December 31, 2009, approximately 2.0 million shares remained available to repurchase under such plans.
Shareholders have authorized two additional classes of stock of one million shares each, to be denominated Class B Common Stock and Preferred Stock, respectively, in addition to the 150 million shares of common stock presently authorized. At December 31, 2009, no shares of Class B Common Stock or Preferred Stock were outstanding.

In December 1986, the Company declared a dividend distribution of one common share purchase right (the Right ) for each outstanding share of common stock. The Rights expired on December 31, 2009.

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**Note 10: Risk-Based Capital**

The Company and the Bank are subject to various regulatory capital adequacy requirements administered by federal and state agencies. The Federal Deposit Insurance Corporation Improvement Act of 1991 ( FDICIA ) required that regulatory agencies adopt regulations defining five capital tiers for banks: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. Failure to meet minimum capital requirements can initiate discretionary actions by regulators that, if undertaken, could have a direct, material effect on the Company s financial statements. Quantitative measures, established by the regulators to ensure capital adequacy, require that the Company and the Bank maintain minimum ratios of capital to risk-weighted assets. There are two categories of capital under the guidelines. Tier 1 capital includes common shareholders equity and qualifying preferred stock less goodwill, identifiable intangible assets, and other deductions including the unrealized net gains and losses, after taxes, of available for sale securities. Tier 2 capital includes preferred stock not qualifying for Tier 1 capital, mandatory convertible debt, subordinated debt, certain unsecured senior debt and the allowance for loan losses, subject to limitations within the guidelines. Under the guidelines, capital is compared to the relative risk of the balance sheet, derived from applying one of four risk weights (0%, 20%, 50% and 100%) to various categories of balance sheet assets and unfunded commitments to extend credit, primarily based on the credit risk of the counterparty. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weighting and other factors.

As of December 31, 2009, the Company and the Bank met all capital adequacy requirements to which they are subject.

The most recent notification from the Federal Reserve Board categorized the Company and the Bank as well capitalized under the FDICIA regulatory framework for prompt corrective action. To be well capitalized, the institution must maintain a total risk-based capital ratio as set forth in the following table and not be subject to a capital directive order. Since that notification, there are no conditions or events that Management believes have changed the risk-based capital category of the Company or the Bank.

The following tables show capital ratios for the Company and the Bank as of December 31, 2009 and 2008:

| | | | For Capital Adequacy Purposes | | To Be Well Capitalized Under the FDICIA Prompt Corrective Action Provisions | |
|---|---|---|---|---|---|---|
| December 31, 2009 | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| | | | (Dollars in thousands) | | | |
| Total Capital (to risk-weighted assets) | | | | | | |
| Consolidated Company | $ 406,339 | 14.50% | $ 224,241 | 8.00% | $ 280,301 | 10.00% |
| Westamerica Bank | 411,310 | 14.88% | 221,177 | 8.00% | 276,471 | 10.00% |
| Tier 1 Capital (to risk-weighted assets) | | | | | | |
| Consolidated Company | 370,011 | 13.20% | 112,120 | 4.00% | 168,180 | 6.00% |
| Westamerica Bank | 370,321 | 13.39% | 110,588 | 4.00% | 165,882 | 6.00% |
| Leverage Ratio * | | | | | | |
| Consolidated Company | 370,011 | 7.60% | 194,625 | 4.00% | 243,281 | 5.00% |
| Westamerica Bank | 370,321 | 7.67% | 193,092 | 4.00% | 241,365 | 5.00% |

| | | | For Capital | | To Be Well Capitalized Under the FDICIA Prompt Corrective | |
|---|---|---|---|---|---|---|

| December 31, 2008 | Amount | Ratio | Adequacy Purposes Amount | Ratio | Action Provisions Amount | Ratio |
|---|---|---|---|---|---|---|
| | | | (Dollars in thousands) | | | |
| Total Capital (to risk-weighted assets) | | | | | | |
| Consolidated Company | $ 324,455 | 11.76% | $ 220,709 | 8.00% | $ 275,887 | 10.00% |
| Westamerica Bank | 293,688 | 10.78% | 217,875 | 8.00% | 272,344 | 10.00% |
| Tier 1 Capital (to risk-weighted assets) | | | | | | |
| Consolidated Company | 288,859 | 10.47% | 110,355 | 4.00% | 165,532 | 6.00% |
| Westamerica Bank | 253,478 | 9.31% | 108,938 | 4.00% | 163,406 | 6.00% |
| Leverage Ratio * | | | | | | |
| Consolidated Company | 288,859 | 7.36% | 156,934 | 4.00% | 196,167 | 5.00% |
| Westamerica Bank | 253,478 | 6.52% | 155,408 | 4.00% | 194,260 | 5.00% |

* The leverage ratio consists of Tier 1 capital divided by quarterly average assets excluding certain intangible assets. The minimum leverage ratio guideline is 3.00% for banking organizations that do not anticipate significant growth and that have well-diversified risk, excellent asset quality, high liquidity, good earnings and, in general, are considered top-rated, strong banking organizations.

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**Note 11: Income Taxes**

Deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between the amounts reported in the financial statements of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Amounts for the current year are based upon estimates and assumptions as of the date of these financial statements and could vary significantly from amounts shown on the tax returns as filed.

The components of the net deferred tax asset as of December 31 are as follows:

| | 2009 | 2008 |
|---|---|---|
| | (In thousands) | |
| Deferred tax asset | | |
| Allowance for credit losses | $ 18,363 | $ 19,789 |
| State franchise taxes | 4,792 | 3,475 |
| Deferred compensation | 13,888 | 14,535 |
| Real estate owned | 97 | 97 |
| Estimated loss on acquired assets | 32,408 | |
| Post retirement benefits | 1,379 | 1,530 |
| Employee benefit accruals | 1,037 | 764 |
| Limited partnership investments | 1,161 | 377 |
| Impaired capital assets | 20,977 | 21,292 |
| Capital loss carryforward | 794 | |
| Premises and equipment | 45 | |
| Other | 2,496 | 836 |
| Subtotal deferred tax asset | 97,436 | 62,695 |
| Valuation allowance | | |
| Total deferred tax asset | 97,436 | 62,695 |
| Deferred tax liability | | |
| Net deferred loan fees | 691 | 770 |
| Premises and equipment | | 236 |
| Intangible assets | 15,643 | 6,958 |
| Securities available for sale | 2,587 | 989 |
| Leases | 994 | 439 |
| Gain on acquired net assets | 5,358 | |
| FDIC indemnification receivable | 35,693 | |
| Other | 742 | 399 |
| Total deferred tax liability | 61,708 | 9,791 |
| Net deferred tax asset | $ 35,728 | $ 52,904 |

Based on Management s judgment, a valuation allowance is not needed to reduce the gross deferred tax asset because it is more likely than not that the gross deferred tax asset will be realized through recoverable taxes or future taxable income. In making such determination, Management considered future income from FDIC indemnification payments will be realized as losses on acquired assets are realized. Net deferred tax assets are included with interest receivable and other assets in the Consolidated Balance Sheets.

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The provision for federal and state income taxes consists of amounts currently payable and amounts deferred which, for the years ended December 31, are as follows:

| | 2009 | 2008 | 2007 |
|---|---|---|---|
| | | (In thousands) | |
| Current income tax expense: | | | |
| Federal | $ 27,595 | $ 12,858 | $ 19,548 |
| State | 14,196 | 9,798 | 12,879 |
| Total current | 41,791 | 22,656 | 32,427 |
| Deferred income tax benefit: | | | |
| Federal | 11,884 | (9,397) | (1,335) |
| State | 4,203 | (3,385) | (401) |
| Total deferred | 16,087 | (12,782) | (1,736) |
| Provision for income taxes | $ 57,878 | $ 9,874 | $ 30,691 |

The provision for income taxes differs from the provision computed by applying the statutory federal income tax rate to income before taxes, as follows:

| | 2009 | 2008 | 2007 |
|---|---|---|---|
| | | (In thousands) | |
| Federal income taxes due at statutory rate | $ 64,157 | $ 24,398 | $ 42,163 |
| Reductions in income taxes resulting from: | | | |
| Interest on state and municipal securities not taxable for federal income tax purposes | (12,742) | (13,164) | (13,518) |
| State franchise taxes, net of federal income tax benefit | 11,959 | 4,168 | 8,111 |
| Limited partnerships | (3,233) | (3,100) | (2,300) |
| Dividend received deduction | (32) | (584) | (946) |
| Cash value life insurance | (715) | (783) | (955) |
| Other | (1,516) | (1,061) | (1,864) |
| Provision for income taxes | $ 57,878 | $ 9,874 | $ 30,691 |

At December 31, 2009, the company had no net operating loss and general tax credit carryforwards for tax return purposes.
During 2007, the Company did not recognize any increase or decrease for unrecognized tax benefits as a result of the implementation of the provision for accounting for uncertainty in income taxes. A reconciliation of the beginning and ending amounts of unrecognized tax benefits follow:

| | 2009 | 2008 |
|---|---|---|
| | (In thousands) | |
| Balance at January 1, | $ 803 | $ 792 |
| Additions for tax positions taken in the current period | 48 | 103 |
| Reductions for tax positions taken in the current period | | |
| Additions for tax positions taken in prior years | 29 | 22 |
| Reductions for tax positions taken in prior years | | |

| | | |
|---|---|---|
| Decreases related to settlements with taxing authorities | | |
| Decreases as a result of a lapse in statue of limitations | (639) | (114) |
| Balance at December 31, | $ 241 | $ 803 |

The Company does not anticipate any significant increase or decrease in unrecognized tax benefits during 2010. Unrecognized tax benefits at December 31, 2009 and 2008 include accrued interest and penalties of $35 thousand and $133 thousand, respectively. If recognized, the entire amount of the unrecognized tax benefits would affect the effective tax rate.

The Company classifies interest and penalties as a component of the provision for income taxes. The tax years ended December 31, 2009, 2008, 2007 and 2006 remain subject to examination by the Internal Revenue Service. The tax years ended December 31, 2009, 2008, 2007 and 2006 remain subject to examination by the California Franchise Tax Board. The Company amended its 2005 federal tax return related to one tax item. The 2005 federal tax return remains open to examination with regard to this item. The deductibility of these tax positions will be determined through examination by the appropriate tax jurisdictions or the expiration of the tax statute of limitations.

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**Note 12: Fair Value Measurements**

The Company groups its assets and liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 Valuation is based upon quoted prices for identical instruments traded in active exchange markets, such as the New York Stock Exchange. Level 1 also includes U.S. Treasury and federal agency securities, which are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market. Level 2 includes mortgage-backed securities, municipal bonds and collateralized mortgage obligations as well as other real estate owned and impaired loans collateralized by real property where the fair value is generally based upon independent market prices or appraised values of the collateral.

Level 3 Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company s estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques. Level 3 includes those impaired loans collateralized by other business assets where the expected cash flow has been used in determining the fair value.

**Assets Recorded at Fair Value on a Recurring Basis**

The table below presents assets measured at fair value on a recurring basis.

| | At December 31, 2009 | | | |
|---|---|---|---|---|
| | Fair Value | Level 1 | Level 2 | Level 3 |
| | (In thousands) | | | |
| U.S. Treasury securities | $ 2,987 | $ 2,987 | $ | $ |
| Securities of U.S. Government sponsored entities | 21,041 | 21,041 | | |
| Mortgage-backed securities | 146,005 | | 146,005 | |
| Obligations of states and political subdivisions | 158,193 | | 158,193 | |
| Collateralized mortgage obligations | 41,410 | | 41,410 | |
| Asset-backed securities | 8,339 | | 8,339 | |
| FHLMC and FNMA stock | 1,573 | 1,573 | | |
| Other securities | 4,660 | 2,703 | 1,957 | |
| Total securities available for sale | $ 384,208 | $ 28,304 | $ 355,904 | $ |

| | At December 31, 2008 | | | |
|---|---|---|---|---|
| | Fair Value | Level 1 | Level 2 | Level 3 |
| | (In thousands) | | | |
| U.S. Treasury securities | $ 3,082 | $ 3,082 | $ | $ |
| Securities of U.S. Government sponsored entities | 11,077 | 11,077 | | |
| Mortgage-backed securities | 41,240 | | 41,240 | |
| Obligations of states and political subdivisions | 161,046 | | 161,046 | |
| Collateralized mortgage obligations | 59,851 | | 59,851 | |
| Asset-backed securities | 6,447 | | 6,447 | |
| FHLMC and FNMA stock | 821 | 821 | | |
| Other securities | 4,890 | 3,000 | 1,890 | |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Total securities available for sale | $ | 288,454 | $ | 17,980 | $ | 270,474 | $ |

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**Assets Recorded at Fair Value on a Nonrecurring Basis**
The Company may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with GAAP. These adjustments to fair value usually result from application of lower-of-cost-or-market accounting or write-downs of individual assets. For assets measured at fair value on a nonrecurring basis that were still held in the balance sheet at December 31, 2009, the following table provides the level of valuation assumptions used to determine each adjustment and the carrying value of the related assets at quarter end.

| | At December 31, 2009 | | | | |
|---|---|---|---|---|---|
| | Fair Value | Level 1 | Level 2 | Level 3 | Total losses |
| | | | (In thousands) | | |
| Non-covered other real estate owned (1) | $ 413 | $ | $ 413 | $ | $ (233) |
| Non-covered impaired loans (2) | 2,447 | | 2,447 | | |
| Total assets measured at fair value on a nonrecurring basis | $ 2,860 | $ | $ 2,860 | $ | $ (233) |

(1) Represents the fair value of foreclosed real estate owned that was measured at fair value subsequent to their initial classification as foreclosed assets.

(2) Represents carrying value of loans for which adjustments are predominantly based on the appraised value of the collateral and loans considered impaired under FASB ASC 310-10-35, Subsequent Measurement of Receivables, where a specific

reserve has been established.

At December 31, 2008, loans measured at fair value on a non-recurring basis were measured for impairment by valuing the underlying collateral based on third-party appraisals, which are level 2 fair value measurements, and totaled $4.9 million, net of specific reserves.

**Disclosures about Fair Value of Financial Instruments**

The fair values presented represent the Company s best estimate of fair value using the methodologies discussed below. The fair values of financial instruments which have a relatively short period of time between their origination and their expected realization were valued using historical cost. The values assigned do not necessarily represent amounts which ultimately may be realized. In addition, these values do not give effect to discounts to fair value which may occur when financial instruments are sold in larger quantities. Such financial instruments and their estimated fair values as of December 31 were:

| | 2009 | 2008 |
|---|---|---|
| | (In thousands) | |
| Cash and cash equivalents | $ 361,135 | $ 138,883 |
| Money market assets | 442 | 341 |
| Interest and taxes receivable | 57,667 | 75,022 |
| Noninterest bearing and interest-bearing transaction and savings deposits | 3,068,820 | 2,429,281 |
| Short-term borrowed funds | 128,134 | 457,275 |
| Interest payable | 1,801 | 2,239 |

The fair values as of December 31 of the following financial instruments were estimated using quoted prices as described above for Level 1 and Level 2 valuation:

| | 2009 | | 2008 | |
|---|---|---|---|---|
| | Book Value | Fair Value | Book Value | Fair Value |
| | (In thousands) | | | |
| Investment securities available for sale | $ 384,208 | $ 384,208 | $ 288,454 | $ 288,454 |
| Investment securities held to maturity | 726,935 | 736,270 | 949,325 | 950,210 |

The fair values of FHLB advances, term repurchase agreements, and notes payable were estimated by using interpolated yields for financial instruments with similar characteristics. Such financial instruments and their estimated fair values as of December 31 were:

| | 2009 | | 2008 | |
|---|---|---|---|---|
| | Book Value | Fair Value | Book Value | Fair Value |
| | (In thousands) | | | |
| FHLB advances | $ 85,470 | $ 85,601 | $ | $ |
| Term repurchase agreements | 99,044 | 100,329 | | |
| Senior notes payable | 15,000 | 14,069 | 15,000 | 12,319 |
| Subordinated notes | 11,497 | 9,451 | 11,631 | 7,455 |

Loans were separated into two groups for valuation. Variable rate loans, except for those described below, which reprice frequently with changes in market rates were valued using historical cost. Fixed rate loans and variable rate loans that have reached their minimum contractual interest rates were valued by discounting the future cash flows expected to be received from the loans using current interest rates charged on loans with similar characteristics. Additionally, the allowance for loan losses of $41.0 million in 2009 and $44.5 million in 2008 and the fair market value discount due to credit default risk associated with purchased loans of $93.3 million at December 31, 2009 were applied against the estimated fair values to recognize estimated future defaults of contractual cash flows. The Company does not consider these values to be an exit price for the loans.

The book values and the estimated fair values of loans as of December 31 were:

| | 2009 | | 2008 | |
|---|---|---|---|---|
| | Book Value | Fair Value | Book Value | Fair Value |
| | (In thousands) | | | |
| Loans | $ 3,015,346 | $ 3,024,866 | $ 2,337,956 | $ 2,373,380 |

The fair values of FDIC receivables and time deposits were estimated by discounting estimated future cash flows related to these financial instruments using current market rates for financial instruments with similar characteristics. The book values and the estimated fair values as of December 31 were:

| | 2009 | | 2008 | |
|---|---|---|---|---|
| | Book Value | Fair Value | Book Value | Fair Value |
| | (In thousands) | | | |
| FDIC receivables | $ 85,787 | $ 83,806 | $ | $ |
| Time deposits | 991,388 | 992,560 | 665,773 | 667,065 |

The majority of the Company s standby letters of credit and other commitments to extend credit carry current market interest rates if converted to loans. No premium or discount was ascribed to these commitments because virtually all funding would be at current market rates.

**Note 13: Lease Commitments**

Thirty-five banking offices and a centralized administrative service center are owned and seventy-six facilities are leased. Substantially all the leases contain multiple renewal options and provisions for rental increases, principally for cost of living index. The Company also leases certain pieces of equipment.

Minimum future rental payments, net of sublease income, as of December 31, 2009, are as follows:

| | (In thousands) |
|---|---|
| 2010 | $ 6,756 |
| 2011 | 6,152 |
| 2012 | 4,899 |
| 2013 | 3,904 |
| 2014 | 2,156 |

| | | |
|---|---|---|
| Thereafter | | 499 |
| Total minimum lease payments | $ | 24,366 |

Total rentals for premises, net of sublease income, included in noninterest expense were $7.2 million in 2009, $6.0 million in 2008 and $5.9 million in 2007. During 2009, the Company was obligated to pay monthly lease payments on County facilities until vacated.

**Note 14: Commitments and Contingent Liabilities**

Loan commitments are agreements to lend to a customer provided there is no violation of any condition established in the agreement. Commitments generally have fixed expiration dates or other termination clauses. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future funding requirements. Loan commitments are subject to the Company s normal credit policies and collateral requirements. Unfunded loan commitments were $482.0 million and $350.8 million at December 31, 2009 and 2008, respectively. Standby letters of credit commit the Company to make payments on behalf of customers when certain specified future events occur. Standby letters of credit are primarily issued to support customers short-term financing requirements and must meet the Company s normal credit policies and collateral requirements. Standby letters of credit outstanding totaled $27.4 million and $29.0 million at December 31, 2009 and 2008, respectively. We also had commitments for commercial and similar letters of credit of $176 thousand and $1.7 million at December 31, 2009 and 2008, respectively.

During 2007, the Visa Inc. ( Visa ) organization of affiliated entities announced that it completed restructuring transactions in preparation for an initial public offering planned for early 2008, and, as part of those transactions, the Bank s membership interest in Visa U.S.A. was exchanged for an equity interest in Visa Inc. In accordance with Visa s by-laws, the Bank and other Visa U.S.A. member banks are obligated to share in Visa s litigation obligations which existed at the time of the restructuring transactions. On November 7, 2007, Visa announced that it had reached a settlement with American Express related to an antitrust lawsuit. Visa has disclosed other antitrust lawsuits which existed at the time of the restructuring transactions. In consideration of the American Express settlement and other antitrust lawsuits filed against Visa, the Company recorded in the fourth quarter of 2007 a liability and corresponding expense of $2,338 thousand. In the first quarter 2008, Visa funded a litigation settlement escrow using proceeds from its initial public offering. Upon the escrow funding, the Company relieved its liability with a corresponding expense reversal in the amount of $2,338 thousand.

On October 27, 2008, Visa announced that it had reached a settlement with Discover Financial Services related to an antitrust lawsuit that existed at the time of Visa s restructuring requiring the payment of the settlement to be funded from the litigation settlement escrow. On December 22, 2008, Visa announced that it had funded its litigation settlement escrow in an amount sufficient to meet such litigation obligation pursuant to Visa s amended and restated Certificate of Incorporation approved by Visa s shareholders on December 16, 2008. As such, the Company did not record a liability for this settlement.

Due to the nature of its business, the Company is subject to various threatened or filed legal cases. Based on the advice of legal counsel, the Company does not expect such cases will have a material, adverse effect on its financial position or results of operations. Legal costs related to covered assets are eighty percent indemnified under loss-sharing agreements with the FDIC if certain conditions are met.

**Note 15: Retirement Benefit Plans**

The Company sponsors a defined contribution Deferred Profit-Sharing Plan covering substantially all of its salaried employees with one or more years of service. Eligible employees become vested in account balances ratably over a five or six-year period, depending on years of service at January 1, 2007. Company contributions charged to noninterest expense were $1.2 million in 2009, $1.2 million in 2008 and $1.0 million in 2007.

In addition to the Deferred Profit-Sharing Plan, all salaried employees are eligible to participate in the Tax Deferred Savings/Retirement Plan (ESOP) upon completion of a 90-day introductory period. The Tax Deferred Savings/Retirement Plan (ESOP) allows employees to defer a portion of their salaries as contributions to this Plan. Participants may invest in several funds, including one fund that invests exclusively in Westamerica Bancorporation common stock. The Company makes matching contributions to employee accounts which vest immediately; such contributions charged to compensation expense were $1.4 million in 2009, $1.3 million in 2008 and $1.2 million in 2007.

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The Company offers a continuation of group insurance coverage to qualifying employees electing early retirement, for the period from the date of retirement until age 65. For eligible employees the Company pays a portion of these early retirees insurance premiums which are determined at their date of retirement. The Company reimburses a portion of Medicare Part B premiums for all qualifying retirees over age 65 and their spouses. Eligibility for post-retirement medical benefits is based on age and years of service, and restricted to employees hired prior to February 1, 2006. The Company uses an actuarial-based accrual method of accounting for post-retirement benefits. Prior to 2008, the Company used a September 30 measurement date. Effective December 31, 2008, the Company measures its benefit obligations as of the balance sheet date. The change in measurement date did not have a material impact on the Company s financial statements.

The following tables set forth the net periodic post-retirement benefit cost for the years ended December 31 and the funded status of the post-retirement benefit plan and the change in the benefit obligation as of December 31:

**Net Periodic Benefit Cost**

| (In thousands) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Service cost | $ (357) | $ (317) | $ (509) |
| Interest cost | 210 | 235 | 284 |
| Amortization of unrecognized transition obligation | 61 | 61 | 61 |
| Net periodic cost | (86) | (21) | (164) |
| **Other Changes in Benefit Obligations Recognized in Other Comprehensive Income** | | | |
| Amortization of unrecognized transition obligation, net of tax | (36) | (36) | (36) |
| Total recognized in net periodic benefit cost and accumulated other comprehensive income | $ (122) | $ (57) | $ (200) |

The remaining transition obligation cost for this post-retirement benefit plan that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year is $61 thousand.

**Obligation and Funded Status**

| (In thousands) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Change in benefit obligation | | | |
| Benefit obligation at beginning of year | $ 3,813 | $ 4,046 | $ 4,430 |
| Service cost | (357) | (317) | (509) |
| Interest cost | 210 | 235 | 284 |
| Benefits paid | (147) | (151) | (159) |
| Benefit obligation at end of year | $ 3,519 | $ 3,813 | $ 4,046 |
| Accumulated post retirement benefit obligation attributable to: | | | |
| Retirees | $ 2,241 | $ 2,724 | $ 2,929 |
| Fully eligible participants | 1,044 | 895 | 899 |
| Other | 234 | 194 | 218 |
| Total | $ 3,519 | $ 3,813 | $ 4,046 |

| | | | |
|---|---|---|---|
| Fair value of plan assets | $ | $ | $ |
| Accumulated post retirement benefit obligation in excess of plan assets | $ 3,519 | $ 3,813 | $ 4,046 |

Additional Information
Assumptions

| | 2009 | 2008 | 2007 |
|---|---|---|---|
| Weighted-average assumptions used to determine benefit obligations as of December 31 | | | |
| Discount rate | 5.50% | 5.80% | 6.50% |
| Weighted-average assumptions used to determine net periodic benefit cost as of December 31 | | | |
| Discount rate | 5.80% | 6.50% | 6.00% |

The above discount rate is based on the Corporate AA Moody s bond rate, the term of which approximates the term of the benefit obligations. The Company reserves the right to terminate or alter post-employment health benefits, which is considered in estimating the increase in the cost of providing such benefits. The assumed annual average rate of inflation used to measure the expected cost of benefits covered by the plan was 5.50% for 2010 and beyond.

Assumed benefit inflation rates have a significant effect on the amounts reported for health care plans. A one percentage point change in the assumed benefit inflation rate would have the following effect on 2009 results:

| (in thousands) | One Percentage Point Increase | One Percentage Point Decrease |
|---|---|---|
| Effect on total service and interest cost components | $ 177 | $ (149) |
| Effect on post-retirement benefit obligation | 462 | (382) |

| Estimated future benefit payments (in thousands) | |
|---|---|
| 2010 | $ 156 |
| 2011 | 162 |
| 2012 | 166 |
| 2013 | 166 |
| 2014 | 162 |
| Years 2015-2019 | 665 |

**Note 16: Related Party Transactions**

Certain of the Directors, executive officers and their associates have had banking transactions with subsidiaries of the Company in the ordinary course of business. With the exception of the Company s Employee Loan Program, all outstanding loans and commitments included in such transactions were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons, did not involve more than a normal risk of collectibility, and did not present other favorable features. As part of the Employee Loan Program, all employees, including executive officers, are eligible to receive mortgage loans at one percent below Westamerica Bank s prevailing interest rate at the time of loan origination. All loans to executive officers under the Employee Loan Program are made by Westamerica Bank in compliance with the applicable restrictions of Section 22(h) of the Federal Reserve Act.

The table below reflects information concerning loans to certain directors and executive officers and/or family members during 2009 and 2008:

| | 2009 | 2008 |
|---|---|---|
| | (In thousands) | |
| Beginning balance | $ 1,291 | $ 1,259 |
| Originations | 47 | 111 |
| Payoffs/principal payments | (142) | (79) |
| At December 31, | $ 1,196 | $ 1,291 |
| Percent of total loans outstanding | 0.04% | 0.05% |

**Note 17: Regulatory Matters**

Payment of dividends to the Company by the Bank is limited under regulations for state chartered banks. The amount that can be paid in any calendar year, without prior approval from regulatory agencies, cannot exceed the net profits (as defined) for the preceding three calendar years less dividends paid. Under this regulation, the Bank sought and obtained approval during 2009 to pay to the Company dividends of $92.8 million. The Company consistently has paid quarterly dividends to its shareholders since its formation in 1972. As of December 31, 2009, $133 million was available for payment of dividends by the Company to its shareholders.

The Bank is required to maintain reserves with the Federal Reserve Bank equal to a percentage of its reservable deposits. The Bank s daily average on deposit at the Federal Reserve Bank was $78.0 million in 2009 and

$19.7 million in 2008.

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**Note 18: Other Comprehensive Income**

The components of other comprehensive (loss) income and other related tax effects were:

| | 2007 | | |
|---|---|---|---|
| (in thousands) | Before tax | Tax effect | Net of tax |
| Securities available for sale: | | | |
| Net unrealized losses arising during the year | $ (11,054) | $ 4,648 | $ (6,406) |
| Reclassification of gains included in net income | | | |
| Net unrealized losses arising during the year | (11,054) | 4,648 | (6,406) |
| Post-retirement benefit obligation | 61 | (25) | 36 |
| Other comprehensive loss | $ (10,993) | $ 4,623 | $ (6,370) |

| | 2008 | | |
|---|---|---|---|
| | Before tax | Tax effect | Net of tax |
| Securities available for sale: | | | |
| Net unrealized losses arising during the year | $ (47,423) | $ 19,940 | $ (27,483) |
| Reclassification of losses included in net income | 56,955 | (23,948) | 33,007 |
| Net unrealized gains arising during the year | 9,532 | (4,008) | 5,524 |
| Post-retirement benefit obligation | 61 | (25) | 36 |
| Other comprehensive income | $ 9,593 | $ (4,033) | $ 5,560 |

| | 2009 | | |
|---|---|---|---|
| | Before tax | Tax effect | Net of tax |
| Securities available for sale: | | | |
| Net unrealized gains arising during the year | $ 4,552 | $ (1,914) | $ 2,638 |
| Reclassification of gains included in net income | | | |
| Net unrealized gains arising during the year | 4,552 | (1,914) | 2,638 |
| Post-retirement benefit obligation | 61 | (25) | 36 |
| Other comprehensive income | $ 4,613 | $ (1,939) | $ 2,674 |

Cumulative other comprehensive income balances were:

| (in thousands) | Post-retirement Benefit Obligation | Net Unrealized gains(losses) on securities | Cumulative Other Comprehensive Income |
|---|---|---|---|
| Balance, December 31, 2006 | $ (394) | $ 2,244 | $ 1,850 |
| Net change | 36 | (6,406) | (6,370) |
| Balance, December 31, 2007 | (358) | (4,162) | (4,520) |
| Net change | 36 | 5,524 | 5,560 |

| | | | |
|---|---|---|---|
| Balance, December 31, 2008 | (322) | 1,362 | 1,040 |
| Net change | 36 | 2,638 | 2,674 |
| Balance, December 31, 2009 | $ (286) | $ 4,000 | $ 3,714 |

**Note 19: Earnings Per Common Share**

The table below shows earnings per common share and diluted earnings per common share. Basic earnings per common share are computed by dividing net income applicable to common equity by the average number of common shares outstanding during the period. Diluted earnings per common share are computed by dividing net income applicable to common equity by the average number of common shares outstanding during the period plus the impact of common stock equivalents.

| (In thousands, except per share data) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Weighted average number of common shares outstanding basic | 29,105 | 28,892 | 29,753 |
| Add exercise of options reduced by the number of shares that could have been purchased with the proceeds of such exercise | 248 | 381 | 412 |
| Weighted average number of common shares outstanding diluted | 29,353 | 29,273 | 30,165 |
| Net income applicable to common equity | $ 121,463 | $ 59,835 | $ 89,776 |
| Basic earnings per common share | 4.17 | 2.07 | 3.02 |
| Diluted earnings per common share | 4.14 | 2.04 | 2.98 |

For the years ended December 31, 2009, 2008, and 2007, options to purchase 788 thousand, 634 thousand and 1.1 million shares of common stock, respectively, were outstanding but not included in the computation of diluted earnings per common share because the option exercise price exceeded the fair value of the stock such that their inclusion would have had an anti-dilutive effect.

**Note 20: Westamerica Bancorporation (Parent Company Only)**

Statements of Income and Comprehensive Income

| For the years ended December 31, | 2009 | 2008 | 2007 |
|---|---|---|---|
| | | (In thousands) | |
| Dividends from subsidiaries | $ 92,785 | $ 101,270 | $ 113,448 |
| Interest income | 180 | 263 | 219 |
| Other income | 6,979 | 5,543 | 8,976 |
| Total income | 99,944 | 107,076 | 122,643 |
| Interest on borrowings | 1,749 | 2,271 | 3,230 |
| Salaries and benefits | 7,182 | 6,487 | 6,785 |
| Other expense | 2,643 | 2,256 | 2,041 |
| Total expenses | 11,574 | 11,014 | 12,056 |
| Income before taxes and equity in undistributed income of subsidiaries | 88,370 | 96,062 | 110,587 |
| Income tax benefit | 2,279 | 2,074 | 2,187 |
| Earnings of subsidiaries greater (less) than subsidiary dividends | 34,777 | (38,301) | (22,998) |
| Net income | 125,426 | 59,835 | 89,776 |
| Other comprehensive income (loss), net of tax | 2,674 | 5,560 | (6,370) |
| Comprehensive income | $ 128,100 | $ 65,395 | $ 83,406 |

Balance Sheets

| Balances as of December 31, | 2009 | 2008 |
|---|---|---|
| Assets | | |
| Cash and cash equivalents | $ 1,200 | $ 18,101 |
| Money market assets and investment securities available for sale | 2,703 | 2,999 |
| Investment in subsidiaries | 521,414 | 390,066 |
| Premises and equipment, net | 11,612 | 11,862 |
| Accounts receivable from subsidiaries | 689 | 1,839 |
| Other assets | 27,134 | 26,035 |
| Total assets | $ 564,752 | $ 450,902 |
| Liabilities | | |
| Debt financing and notes payable | $ 42,507 | $ 26,941 |
| Other liabilities | 16,797 | 14,109 |
| Total liabilities | 59,304 | 41,050 |
| Shareholders equity | 505,448 | 409,852 |
| Total liabilities and shareholders equity | $ 564,752 | $ 450,902 |

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Statements of Cash Flows

| For the years ended December 31, | 2009 | 2008 | 2007 |
|---|---|---|---|
| | | (In thousands) | |
| Operating Activities | | | |
| Net income | $ 125,426 | $ 59,835 | $ 89,776 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization | 186 | 204 | 236 |
| (Decrease) increase in accounts receivable from affiliates | 1,150 | (956) | (135) |
| Increase in other assets | (1,191) | (2,484) | (942) |
| Stock option expense | 1,132 | 1,193 | 1,779 |
| Excess tax benefits from stock based compensation | (2,188) | (1,130) | (306) |
| Provision for deferred income tax | 3,758 | 2,801 | 207 |
| (Decrease) increase in other liabilities | 1,765 | (10) | 2,038 |
| Earnings of subsidiaries (greater) less than subsidiary dividends | (34,777) | 38,301 | 22,998 |
| Impairment and losses on sale of investment securities | | 1,246 | |
| Net cash provided by operating activities | 95,261 | 99,000 | 115,651 |
| Investing Activities | | | |
| Investment in subsidiary bank | (93,726) | | |
| Purchases of premises and equipment | (70) | (204) | (489) |
| Net (increase) decrease in short term investments | (1) | (10) | 234 |
| Net cash used in investing activities | (93,797) | (214) | (255) |
| Financing Activities | | | |
| Increase (decrease) in short-term debt | 15,700 | (19,532) | (980) |
| Net reductions in notes payable and long-term borrowings | | (10,000) | |
| Proceeds from issuance of preferred stock and warrants | 83,726 | | |
| Redemption of preferred stock | (83,726) | | |
| Preferred stock dividends | (2,756) | | |
| Exercise of stock options/issuance of shares | 9,610 | 22,830 | 11,908 |
| Excess tax benefits from stock based compensation | 2,188 | 1,130 | 306 |
| Retirement of common stock including repurchases | (2,046) | (35,914) | (87,103) |
| Dividends | (41,061) | (40,236) | (40,647) |
| Net cash used in financing activities | (18,365) | (81,722) | (116,516) |
| Net (decrease) increase in cash and cash equivalents | (16,901) | 17,064 | (1,120) |
| Cash and cash equivalents at beginning of year | 18,101 | 1,037 | 2,157 |
| Cash and cash equivalents at end of year | $ 1,200 | $ 18,101 | $ 1,037 |
| Supplemental disclosure: | | | |
| Unrealized gain (loss) on securities available for sale, net | $ 2,638 | $ 5,524 | $ (6,406) |

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**Note 21: Quarterly Financial Information (Unaudited)**

| | March 31, | June 30, | September 30, | December 31, |
|---|---|---|---|---|
| | (In thousands, except per share data and price range of common stock) | | | |
| 2009 | | | | |
| Interest and fee income (FTE) | $ 64,192 | $ 68,063 | $ 66,093 | $ 63,250 |
| Net interest income (FTE) | 59,359 | 62,318 | 61,593 | 58,949 |
| Provision for credit losses | 1,800 | 2,600 | 2,800 | 3,300 |
| Noninterest income | 63,968 | 16,386 | 15,961 | 15,696 |
| Noninterest expense | 34,123 | 38,666 | 35,151 | 32,836 |
| Income before taxes (FTE) | 87,404 | 37,438 | 39,603 | 38,509 |
| Net income | 52,825 | 23,183 | 25,257 | 24,161 |
| Net income applicable to common equity | 52,247 | 22,076 | 23,791 | 23,349 |
| Basic earnings per common share | 1.81 | 0.76 | 0.81 | 0.80 |
| Diluted earnings per common share | 1.80 | 0.75 | 0.81 | 0.79 |
| Dividends paid per common share | 0.36 | 0.35 | 0.35 | 0.35 |
| Price range, common stock | 33.08-51.29 | 44.13-56.79 | 45.42-54.70 | 47.08-56.80 |
| 2008 | | | | |
| Interest and fee income (FTE) | $ 60,810 | $ 58,117 | $ 56,131 | $ 54,442 |
| Net interest income (FTE) | 47,982 | 49,731 | 48,693 | 49,850 |
| Provision for credit losses | 600 | 600 | 600 | 900 |
| Noninterest income (loss) | 19,378 | (3,843) | (27,499) | 9,908 |
| Noninterest expense | 23,056 | 26,337 | 25,203 | 26,166 |
| Income (loss) before taxes (FTE) | 43,704 | 18,951 | (4,609) | 32,692 |
| Net income | 26,778 | 12,202 | 44 | 20,810 |
| Basic earnings per share | 0.93 | 0.42 | 0.00 | 0.72 |
| Diluted earnings per share | 0.92 | 0.42 | 0.00 | 0.71 |
| Dividends paid per share | | | | |