

WESTAMERICA BANCORPORATION

Form 10-Q

November 01, 2010

Table of Contents

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

(Mark One)

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

For the quarterly period ended September 30, 2010

or

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

For the transition period from _____ to _____.

**Commission file number: 001-9383
WESTAMERICA BANCORPORATION
(Exact Name of Registrant as Specified in Its Charter)**

CALIFORNIA
(State or Other Jurisdiction of
Incorporation or Organization)

94-2156203
(I.R.S. Employer
Identification No.)

1108 FIFTH AVENUE, SAN RAFAEL, CALIFORNIA 94901

(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code (707) 863-6000

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

Yes No

Indicate by check mark whether the registrant 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

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

Yes No

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date:

Title of Class	Shares outstanding as of October 22, 2010
Common Stock, No Par Value	29,111,478

TABLE OF CONTENTS

<u>Forward Looking Statements</u>	Page 3
<u>PART I FINANCIAL INFORMATION</u>	
<u>Item 1 Financial Statements</u>	4
<u>Notes to Unaudited Condensed Consolidated Financial Statements</u>	8
<u>Financial Summary</u>	24
<u>Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	25
<u>Item 3 Quantitative and Qualitative Disclosures about Market Risk</u>	48
<u>Item 4 Controls and Procedures</u>	48
<u>PART II OTHER INFORMATION</u>	
<u>Item 1 Legal Proceedings</u>	48
<u>Item 1A Risk Factors</u>	49
<u>Item 2 Unregistered Sales of Equity Securities and Use of Proceeds</u>	50
<u>Item 3 Defaults upon Senior Securities</u>	50
<u>Item 4 Reserved</u>	50
<u>Item 5 Other Information</u>	50
<u>Item 6 Exhibits</u>	51
<u>Signatures</u>	52
<u>Exhibit Index</u>	53
<u>Exhibit 31.1 - Certification of Chief Executive Officer pursuant to Securities Exchange Act Rule 13a-14(a)/15d-14(a)</u>	
<u>Exhibit 31.2 - Certification of Chief Financial Officer pursuant to Securities Exchange Act Rule 13a-14(a)/15d-14(a)</u>	
<u>Exhibit 32.1 - Certification of Chief Executive Officer Required by 18 U.S.C. Section 1350</u>	
<u>Exhibit 32.2 - Certification of Chief Financial Officer Required by 18 U.S.C. Section 1350</u>	
<u>EX-101 INSTANCE DOCUMENT</u>	
<u>EX-101 SCHEMA DOCUMENT</u>	
<u>EX-101 CALCULATION LINKBASE DOCUMENT</u>	
<u>EX-101 LABELS LINKBASE DOCUMENT</u>	
<u>EX-101 PRESENTATION LINKBASE DOCUMENT</u>	
<u>EX-101 DEFINITION LINKBASE DOCUMENT</u>	

Table of Contents

FORWARD-LOOKING STATEMENTS

This report on Form 10-Q 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 statements 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. The reader is directed to the Company's annual report on Form 10-K for the year ended December 31, 2009, for further discussion of factors which could affect the Company's business and cause actual results to differ materially from those expressed in any forward-looking statement made in this report. The Company undertakes no obligation to update any forward-looking statements in this report.

Table of Contents**PART I FINANCIAL INFORMATION****Item 1 Financial Statements**

WESTAMERICA BANCORPORATION
CONSOLIDATED BALANCE SHEETS
(unaudited)

	At September 30, 2010	At December 31, 2009
	(In thousands)	
Assets:		
Cash and due from banks	\$ 344,169	\$ 361,135
Money market assets	392	442
Investment securities available for sale	569,511	384,208
Investment securities held to maturity, with fair values of:		
\$642,882 at September 30, 2010	618,838	
\$736,270 at December 31, 2009		726,935
Purchased covered loans	718,618	855,301
Purchased non-covered loans	212,318	
Originated loans	2,077,915	2,201,088
Allowance for loan losses	(38,129)	(41,043)
Total loans	2,970,722	3,015,346
Non-covered other real estate owned	22,201	12,642
Covered other real estate owned	25,251	23,297
Premises and equipment, net	36,271	38,098
Identifiable intangibles, net	36,226	35,667
Goodwill	121,673	121,699
Interest receivable and other assets	232,617	256,032
Total Assets	\$ 4,977,871	\$ 4,975,501
Liabilities:		
Noninterest bearing deposits	\$ 1,428,882	\$ 1,428,432
Interest bearing deposits	2,643,816	2,631,776
Total deposits	4,072,698	4,060,208
Short-term borrowed funds	193,202	227,178
Federal Home Loan Bank advances	66,934	85,470
Debt financing and notes payable	26,396	26,497
Liability for interest, taxes and other expenses	77,468	70,700
Total Liabilities	4,436,698	4,470,053
Shareholders Equity:		
Common stock, authorized 150,000 shares		

Issued and outstanding:			
29,118 at September 30, 2010	376,123		
29,208 at December 31, 2009			366,247
Deferred compensation	2,724		2,485
Accumulated other comprehensive income	7,238		3,714
Retained earnings	155,088		133,002
Total Shareholders Equity	541,173		505,448
Total Liabilities and Shareholders Equity	\$ 4,977,871	\$	4,975,501

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

WESTAMERICA BANCORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
	(In thousands, except per share data)			
Interest Income:				
Loans	\$ 44,434	\$ 48,530	\$ 133,196	\$ 143,148
Money market assets and funds sold	1	1	2	3
Investment securities available for sale	4,189	4,272	12,110	12,550
Investment securities held to maturity	6,579	8,393	20,976	27,752
Total Interest Income	55,203	61,196	166,284	183,453
Interest Expense:				
Deposits	2,047	3,273	6,716	11,525
Short-term borrowed funds	511	509	1,538	1,572
Federal Home Loan Bank advances	113	295	249	714
Notes payable	425	423	1,272	1,267
Total Interest Expense	3,096	4,500	9,775	15,078
Net Interest Income	52,107	56,696	156,509	168,375
Provision for Loan Losses	2,800	2,800	8,400	7,200
Net Interest Income After Provision For Loan Losses	49,307	53,896	148,109	161,175
Noninterest Income:				
Service charges on deposit accounts	8,162	9,479	25,533	27,017
Merchant credit card	2,234	2,163	6,631	6,818
Debit card	1,259	1,267	3,678	3,656
ATM and interchange	1,004	965	2,917	2,792
Trust fees	429	319	1,257	1,056
Financial services commissions	211	129	583	420
Gain on acquisition	178		178	48,844
Other	1,594	1,639	5,534	5,712
Total Noninterest Income	15,071	15,961	46,311	96,315
Noninterest Expense:				
Salaries and related benefits	15,481	16,402	46,849	50,221
Occupancy	3,962	4,008	11,561	14,831
Outsourced data processing services	2,187	2,258	6,629	6,740
Amortization of identifiable intangibles	1,573	1,671	4,711	5,051
FDIC insurance assessments	1,268	1,442	3,848	4,820
Furniture and equipment	1,067	1,789	3,234	4,618

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Professional fees	950	913	2,480	2,580
Courier service	826	989	2,636	2,881
Other	4,194	5,679	13,687	16,198
Total Noninterest Expense	31,508	35,151	95,635	107,940
Income Before Income Taxes	32,870	34,706	98,785	149,550
Provision for income taxes	9,161	9,449	27,939	48,285
Net Income	23,709	25,257	70,846	101,265
Preferred stock dividends and discount accretion		1,466		3,151
Net Income Applicable to Common Equity	\$ 23,709	\$ 23,791	\$ 70,846	\$ 98,114
Average Common Shares Outstanding	29,127	29,210	29,187	29,072
Diluted Average Common Shares Outstanding	29,385	29,429	29,515	29,313
Per Common Share Data:				
Basic earnings	\$ 0.81	\$ 0.81	\$ 2.43	\$ 3.37
Diluted earnings	0.81	0.81	2.40	3.35
Dividends paid	0.36	0.35	1.08	1.06
See accompanying notes to unaudited condensed consolidated financial statements.				

Table of Contents**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY AND
COMPREHENSIVE INCOME**

(unaudited)

	Common Shares Outstanding	Preferred Stock	Common Stock	Accumulated Deferred Compensation	Comprehensive Income	Retained Earnings	Total
	(In thousands)						
Balance, December 31, 2008	28,880	\$	\$ 352,265	\$ 2,409	\$ 1,040	\$ 54,138	\$ 409,852
Comprehensive income							
Net income for the period						101,265	101,265
Other comprehensive income, net of tax:							
Increase in net unrealized gain on securities available for sale					4,986		4,986
Post-retirement benefit transition obligation amortization					27		27
Total comprehensive income							106,278
Issuance of preferred stock and related warrants		82,519	1,207				83,726
Redemption of preferred stock		(41,863)					(41,863)
Preferred stock dividends and discount accretion		679				(3,151)	(2,472)
Exercise of stock options	350		9,094				9,094
Stock option tax benefits			2,179				2,179
Restricted stock activity	7		251	76			327
Stock based compensation			847				847
Stock awarded to employees	2		78				78
Purchase and retirement of stock	(32)		(374)			(1,116)	(1,490)
Dividends						(30,838)	(30,838)
Balance, September 30, 2009	29,207	\$ 41,335	\$ 365,547	\$ 2,485	\$ 6,053	\$ 120,298	\$ 535,718
Balance, December 31, 2009	29,208	\$	\$ 366,247	\$ 2,485	\$ 3,714	\$ 133,002	\$ 505,448
Comprehensive income							
Net income for the period						70,846	70,846
Other comprehensive income, net of tax:							
Increase in net unrealized gain on securities available for sale					3,497		3,497
Post-retirement benefit transition obligation amortization					27		27
Total comprehensive income							74,370

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Exercise of stock options	305	12,682		12,682
Stock option tax benefits		917		917
Restricted stock activity	7	194	239	433
Stock based compensation		1,060		1,060
Stock awarded to employees	2	101		101
Purchase and retirement of stock	(404)	(5,078)		(17,171) (22,249)
Dividends				(31,589) (31,589)
Balance, September 30, 2010	29,118	\$ 376,123	\$ 2,724	\$ 7,238 \$ 155,088 \$ 541,173

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

WESTAMERICA BANCORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	For the nine months ended September 30,	
	2010	2009
	(In thousands)	
Operating Activities:		
Net income	\$ 70,846	\$ 101,265
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	11,359	7,317
Loan loss provision	8,400	7,200
Net amortization of deferred loan cost	12	358
Decrease (increase) in interest income receivable	742	(3,637)
Gain on acquisition	(178)	(48,844)
Decrease in other assets	11,751	48,191
Increase in income taxes payable	2,530	3,811
Decrease in interest expense payable	(28)	(317)
(Decrease) increase in other liabilities	(14,778)	26,398
Stock option compensation expense	1,060	847
Stock option tax benefits	(917)	(2,179)
Gain on sale of other assets	(608)	
Net (gain on sale) writedown of property and equipment	(445)	37
Originations of mortgage loans for resale	(277)	(68)
Net proceeds from sale of mortgage loans originated for resale	288	101
Net loss (gain) on sale of foreclosed assets	(561)	(166)
Writedown of foreclosed assets	793	83
Net Cash Provided by Operating Activities	89,989	140,397
Investing Activities:		
Net repayments of loans	227,056	324,315
Proceeds from FDIC loss-sharing indemnification	35,792	43,696
Purchases of investment securities available for sale	(279,827)	
Purchases of investment securities held to maturity		(522)
Proceeds from maturity/calls of securities available for sale	122,452	76,185
Proceeds from maturity/calls of securities held to maturity	108,096	172,002
Net change in FRB/FHLB* securities	3,479	1,502
Proceeds from sale of foreclosed assets	10,953	10,009
Purchases of property, plant and equipment	(657)	(14,146)
Proceeds from sale of property, plant and equipment	603	
Net cash acquired from acquisitions	57,895	44,397
Net Cash Provided by Investing Activities	285,842	657,438
Financing Activities:		

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Net change in deposits	(237,794)	(298,770)
Net change in short-term borrowings	(114,764)	(476,483)
Exercise of stock options	12,682	9,094
Proceeds from issuance of preferred stock		83,726
Redemption of preferred stock		(41,863)
Stock option tax benefits	917	2,179
Repurchases/retirement of stock	(22,249)	(1,490)
Dividends paid	(31,589)	(30,838)
Preferred dividends		(2,215)
Net Cash Used in Financing Activities	(392,797)	(756,660)
Net Change In Cash and Cash Equivalents	(16,966)	41,175
Cash and Due from Banks at Beginning of Period	361,135	138,883
Cash and Due from Banks at End of Period	\$ 344,169	\$ 180,058
Supplemental Cash Flow Disclosures:		
Supplemental disclosure of non cash activities:		
Loan collateral transferred to other real estate owned	\$ 24,188	\$ 23,804
Unrealized gain on securities available for sale, net	3,497	4,986
Supplemental disclosure of cash flow activities:		
Interest paid for the period	11,759	21,719
Income tax payments for the period	39,578	27,553
Acquisitions:		
Assets acquired	\$ 315,083	\$ 1,624,464
Liabilities assumed	314,905	1,575,620
Net	178	48,844

See accompanying notes to unaudited condensed consolidated financial statements.

* Federal Reserve
Bank/Federal
Home Loan
Bank
(FRB/FHLB)

Table of Contents**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****Note 1: Basis of Presentation**

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. The results of operations reflect interim adjustments, all of which are of a normal recurring nature and which, in the opinion of Management, are necessary for a fair presentation of the results for the interim periods presented. The interim results for the three and nine months ended September 30, 2010 and 2009 are not necessarily indicative of the results expected for the full year. These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes as well as other information included in the Company's Annual Report on Form 10-K for the year ended December 31, 2009.

The Company has evaluated events and transactions subsequent to the balance sheet date. Based on this evaluation, the Company is not aware of any events or transactions that occurred subsequent to the balance sheet date but prior to filing that would require recognition or disclosure in its consolidated financial statements.

Note 2: Accounting Policies

The Company's accounting policies are discussed in Note 1 to the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2009. Certain amounts in prior periods have been reclassified to conform to the current presentation.

Certain accounting policies underlying the preparation of these financial statements require Management to make estimates and judgments. These estimates and judgments may significantly affect reported amounts of assets and liabilities, revenues and expenses, and disclosures of contingent assets and liabilities.

Management exercises judgment to estimate the appropriate level of the allowance for credit losses and purchased impaired loans, which are discussed in the Company's accounting policies.

As described in Note 3 below, Westamerica Bank (Bank) acquired assets and assumed liabilities of the former Sonoma Valley Bank on August 20, 2010. The acquired assets and assumed liabilities were measured at estimated fair values, as required by Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 805, Business Combinations. Management made significant estimates and exercised significant judgment in accounting for the acquisition. Management judgmentally measured loan fair values based on loan file reviews (including borrower financial statements and tax returns), appraised collateral values, expected cash flows, and historical loss factors. Repossessed loan collateral was primarily valued based upon appraised collateral values. The Bank also recorded an identifiable intangible asset representing the value of the core deposit customer base of Sonoma Valley Bank based on Management's evaluation of the cost of such deposits relative to alternative funding sources. In determining the value of the identifiable intangible asset, Management 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 and FHLB advances.

The acquired assets of Sonoma Valley Bank include loans; such loans are not indemnified by the Federal Deposit Insurance Corporation (FDIC). However, on February 6, 2009, the Bank acquired loans in a business combination that are indemnified by the FDIC, as described in Note 2 to the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2009. Pursuant to acquisition accounting, the loans in each business combination were measured at their estimated fair value at the respective acquisition date. This method of measuring the carrying value of purchased loans differs from loans originated by the Company, and as such, the Company identifies purchased loans not indemnified by the FDIC as Purchased Non-covered Loans and purchased loans indemnified by the FDIC as Purchased Covered Loans.

Loans originated by the Company are measured at the principal amount outstanding, net of unearned discount and unamortized deferred fees and costs. These loans are identified as Originated Loans.

Table of Contents**Recently Adopted Accounting Standards**

In the first quarter of 2010, the Company adopted the following new accounting guidance:

FASB ASC 860, as amended, *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 January 1, 2010, 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. The adoption of this Statement did not have any effect on the Company's financial statements at the date of adoption.

FASB ASC 810, as amended, *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 adoption of this Statement did not have any effect on the Company's financial statements at the date of adoption.

FASB Accounting Standards Update (ASU) 2010-06, *Fair Value Measurements and Disclosures (Topic 820)*, issued January 2010 and effective January 1, 2010, requires new disclosures for: (1) transfers in and out of Levels 1 and 2, including separate disclosure of significant amounts and a description of the reasons for the transfers; and (2) separate presentation of information about purchases, sales, issuances, and settlements (on a gross basis rather than net) in the reconciliation for fair value measurements using significant unobservable inputs (Level 3). The Update clarifies existing disclosure requirements for: (1) Level of disaggregation, which provides measurement disclosures for each class of assets and liabilities. Emphasizing that judgment should be used in determining the appropriate classes of assets and liabilities; and (2) inputs and valuation techniques for both recurring and nonrecurring Level 2 and Level 3 fair value measurements.

This update also includes conforming amendments to the guidance on employer's disclosures about postretirement benefit plan assets changing the terminology of major categories of assets to classes of assets and providing a cross reference to the guidance in Subtopic 820-10 on how to determine appropriate classes to present fair value disclosures. The adoption of this Update did not have a significant effect on the Company's financial statements at the date of adoption.

Recently Issued Accounting Standards

FASB ASU 2010-18, *Effect of a Loan Modification When the Loan is Part of a Pool that is Accounted for as a Single Asset (Topic 310)*, was issued April 2010 and is effective for modifications of loans accounted for within pools under Subtopic 310-30 occurring in the first interim or annual period ending after July 15, 2010. As a result of the amendments in this Update, modification of loans within the pool does not result in the removal of those loans from the pool even if the modification of those loans would otherwise be considered a troubled debt restructuring. An entity will continue to be required to consider whether the pool of assets in which the loan is included is impaired if expected cash flows for the pool change. However, loans within the scope of Subtopic 310-30 that are accounted for individually will continue to be subject to the troubled debt restructuring accounting provisions.

The provisions of this Update will be applied prospectively with early application permitted. Upon initial adoption of the guidance in this Update, an entity may make a one-time election to terminate accounting for loans as a pool under Subtopic 310-30. The election may be applied on a pool-by-pool basis and does not preclude an entity from applying pool accounting to subsequent acquisitions of loans with credit deterioration.

The Company does not have any pools of loans accounted for in accordance with Subtopic 310-30, and therefore, the adoption of this Update will not have a significant effect on the Company's financial statements.

FASB ASU 2010-20, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses (Topic 310)*, was issued July 2010. The guidance will significantly expand the disclosures that the Company must make about the credit quality of financing receivables and the allowance for credit losses. The objectives of the enhanced disclosures are to provide financial statement users with additional information about the nature of credit risks inherent in the Company's financing receivables, how credit risk is analyzed and assessed when determining the allowance for credit losses, and the reasons for the change in the allowance for credit losses.

Table of Contents

The disclosures as of the end of the reporting period are effective for the Company's interim and annual periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for the Company's interim and annual periods beginning on or after December 15, 2010. The adoption of this Update requires enhanced disclosures and is not expected to have a significant effect on the Company's financial statements.

Note 3: Acquisition of Sonoma Valley Bank

On August 20, 2010, Westamerica Bank purchased substantially all the assets and assumed substantially all the liabilities of Sonoma Valley Bank (Sonoma) from the Federal Deposit Insurance Corporation (FDIC), as Receiver of Sonoma. Sonoma operated 3 commercial banking branches within Sonoma County, California. The FDIC took Sonoma under receivership upon Sonoma's closure by the California Department of Financial Institutions at the close of business August 20, 2010. Westamerica Bank purchased substantially all of Sonoma's net assets at a discount of \$43 million, and paid a \$5 million deposit premium.

The Sonoma acquisition was accounted for under the purchase method of accounting in accordance with FASB ASC 805, Business Combinations. The statement of net assets acquired as of August 20, 2010 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 \$178 thousand 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. Sonoma'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 August 20, 2010 (In thousands)
Assets	
Cash and due from banks	\$ 57,895
Money market assets	26,050
Securities	7,223
Loans	213,664
Other real estate owned	2,916
Core deposit intangible	5,270
Other assets	2,065
Total Assets	\$ 315,083
Liabilities	
Deposits	252,563
Federal Home Loan Bank advances	61,872
Liabilities for interest and other expenses	470
Total Liabilities	314,905
Net assets acquired	\$ 178

At

	August 20, 2010 (In thousands)
Sonoma Valley Bank tangible shareholder's equity	\$ 13,923
Adjustments to reflect assets acquired and liabilities assumed at fair value:	
Cash payment from FDIC	21,270
Loans and leases, net	(34,562)
Other real estate owned	(1,491)
Other assets	(811)
Core deposit intangible	5,270
Deposits	(1,233)
Federal Home Loan Bank advances	(1,872)
Other liabilities	(316)
Gain on acquisition	\$ 178

The pro forma consolidated condensed statements of income for Westamerica Bancorporation and Sonoma Valley Bank for the nine months ended September 30, 2010 and 2009, and the year ended December 31, 2009 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.

Table of Contents

The pro forma purchase accounting adjustments related to loans and leases, deposits and Federal Home Loan Bank advances 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 pro forma consolidated condensed statements of income do not reflect any adjustments to Sonoma's historical provision for credit losses. (in thousands, except per share data)

	Nine months ended September 30, 2010				Nine months ended September 30, 2009			
	Westamerica	Sonoma Valley Bank	Proforma Adjustments	Pro Forma Combined	Westamerica	Sonoma Valley Bank	Proforma Adjustments	Pro forma combined
Interest Income	\$ 178,664	\$ 11,404	\$ (872)	\$ 189,196	\$ 183,453	\$ 13,856	\$ (872)	\$ 196,437
Interest Expense	9,614	2,387	(863)	11,138	15,078	3,044	(863)	17,259
Net Interest Income	169,050	9,017	(9)	178,058	168,375	10,812	(9)	179,178
Provision for Credit Losses	8,400	4,400		12,800	7,200	29,330		36,530
Net Interest Income after Provision for Credit Losses	160,650	4,617	(9)	165,258	161,175	(18,518)	(9)	142,648
Noninterest Income	45,998	2,034	178	48,210	96,315	1,502	178	97,995
Noninterest Expense	95,064	5,143	(43)	100,164	107,940	6,885	(43)	114,782
Income (Loss) Before Taxes	111,584	1,508	212	113,304	149,550	(23,901)	212	125,861
Income Tax Provision (Benefit)	41,268	634	89	41,991	48,285	(4,629)	89	43,745
Net Income (Loss)	\$ 70,316	\$ 874	\$ 123	\$ 71,313	\$ 101,265	\$ (19,272)	\$ 123	\$ 82,116
Net Income (Loss) Applicable to Common Equity	\$ 70,316	\$ 874	\$ 123	\$ 71,313	\$ 98,114	\$ (19,272)	\$ 123	\$ 78,965
Earnings (Loss) Per Common Share	\$ 2.41	\$ 0.03	\$ 0.00	\$ 2.44	\$ 3.37	\$ (0.66)	\$ 0.00	\$ 2.72
Diluted Earnings (Loss) Per Common Share	2.38	0.03	0.00	2.42	3.35	(0.66)	0.00	2.69

Average Common Shares

Outstanding	29,187	29,072
Diluted Average Common Shares Outstanding	29,515	29,313

Year ended December 31, 2009

	Westamerica	Sonoma Valley Bank	Proforma Adjustments	Pro Forma Combined
Interest Income	\$ 241,949	\$ 18,177	\$ (1,163)	\$ 258,963
Interest Expense	19,380	3,883	(1,150)	22,113
Net Interest Income	222,569	14,294	(13)	236,850
Provision for Credit Losses	10,500	31,130		41,630
Net Interest Income after Provision for Credit Losses	212,069	(16,836)	(13)	195,220
Noninterest Income	112,011	2,029	178	114,218
Noninterest Expense	140,776	8,914	(108)	149,582
Income (Loss) Before Taxes	183,304	(23,721)	273	159,856
Income Tax Provision (Benefit)	57,878	(4,481)	115	53,512
Net Income (Loss)	\$ 125,426	\$ (19,240)	\$ 158	\$ 106,344
Net Income (Loss) Applicable to Common Equity	\$ 121,463	\$ (19,240)	\$ 158	\$ 102,381
Earnings (Loss) Per Common Share	\$ 4.17	\$ (0.66)	\$ 0.01	\$ 3.52
Diluted Earnings (Loss) Per Common Share	4.14	(0.66)	0.01	3.49
Average Common Shares Outstanding	29,105			
Diluted Average Common Shares Outstanding	29,353			

Note 4: Investment Securities

The amortized cost, unrealized gains and losses accumulated in other comprehensive income, and fair value of the available for sale investment securities portfolio as of September 30, 2010, follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(In thousands)		
U.S. Treasury securities	\$ 3,504	\$ 7	\$	\$ 3,511
Securities of U.S. Government sponsored entities	118,673	231	(71)	118,833
Residential mortgage-backed securities	112,961	5,302		118,263
Commercial mortgage-backed securities	5,204	10	(23)	5,191
Obligations of States and political subdivisions	209,178	5,507	(377)	214,308

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Residential collateralized mortgage obligations	24,228	1,110		25,338
Asset-backed securities	9,401		(981)	8,420
FHLMC and FNMA stock	824	30	(237)	617
Corporate securities	69,811	142	(170)	69,783
Other securities	2,790	2,487	(30)	5,247
Total	\$ 556,574	\$ 14,826	\$ (1,889)	\$ 569,511

Table of Contents

The amortized cost, unrealized gains and losses, and fair value of the held to maturity investment securities portfolio as of September 30, 2010, follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
(In thousands)				
Residential mortgage-backed securities	\$ 44,754	\$ 1,937	\$ (2)	\$ 46,689
Obligations of States and political subdivisions	470,638	22,426	(319)	492,745
Residential collateralized mortgage obligations	103,446	2,791	(2,789)	103,448
Total	\$ 618,838	\$ 27,154	\$ (3,110)	\$ 642,882

The amortized cost, unrealized gains and losses accumulated in other comprehensive income, and fair value of the available for sale investment securities portfolio as of December 31, 2009, follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
(In thousands)				
U.S. Treasury securities	\$ 2,987	\$	\$	\$ 2,987
Securities of U.S. Government sponsored entities	21,018	48	(25)	21,041
Residential mortgage-backed securities	143,625	2,504	(124)	146,005
Obligations of States and political subdivisions	155,093	4,077	(977)	158,193
Residential 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

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

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

The amortized cost and fair value of securities as of September 30, 2010, by contractual maturity, are shown in the following table:

Securities Available for Sale	Securities Held to Maturity
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	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)			
Maturity in years:				
1 year or less	\$ 26,089	\$ 26,214	\$ 7,850	\$ 7,924
Over 1 to 5 years	238,045	239,761	78,128	81,386
Over 5 to 10 years	73,486	75,512	373,875	392,421
Over 10 years	72,947	73,368	10,785	11,014
Subtotal	410,567	414,855	470,638	492,745
Mortgage-backed securities and residential collateralized mortgage obligations	142,393	148,792	148,200	150,137
Other securities	3,614	5,864		
Total	\$ 556,574	\$ 569,511	\$ 618,838	\$ 642,882

Table of Contents

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

	Securities Available for Sale		Securities Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
(In thousands)				
Maturity in years:				
1 year or less	\$ 12,763	\$ 12,852	\$ 8,303	\$ 8,389
Over 1 to 5 years	86,757	88,759	58,111	60,075
Over 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

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. An analysis of gross unrealized losses of the available for sale investment securities portfolio as of September 30, 2010, follows:

	Less than 12 months Unrealized		12 months or longer Unrealized		Total Unrealized	
	Fair Value	Losses	Fair Value	Losses	Fair Value	Losses
(In thousands)						
Securities of U.S. Government sponsored entities	\$ 50,812	\$ (71)	\$	\$	\$ 50,812	\$ (71)
Residential mortgage-backed securities	98				98	
Commercial mortgage-backed securities	3,071	(23)			3,071	(23)
Obligations of States and political subdivisions	14,732	(122)	10,959	(255)	25,691	(377)
Residential collateralized mortgage obligations	5				5	
Asset-backed securities			8,420	(981)	8,420	(981)
FHLMC and FNMA stock	1	(5)	472	(232)	473	(237)
Corporate securities	29,977	(170)			29,977	(170)
Other securities	5		1,970	(30)	1,975	(30)
Total	\$ 98,701	\$ (391)	\$ 21,821	\$ (1,498)	\$ 120,522	\$ (1,889)

An analysis of gross unrealized losses of the held to maturity investment securities portfolio as of September 30, 2010, follows:

	Less than 12 months Unrealized		12 months or longer Unrealized		Total Unrealized	
	Fair Value	Losses	Fair Value	Losses	Fair Value	Losses
	(In thousands)					
Residential mortgage backed securities	\$ 437	\$ (2)	\$	\$	\$ 437	\$ (2)
Obligations of States and political subdivisions	1,102	(17)	13,981	(302)	15,083	(319)
Residential collateralized mortgage obligations			26,698	(2,789)	26,698	(2,789)
Total	\$ 1,539	\$ (19)	\$ 40,679	\$ (3,091)	\$ 42,218	\$ (3,110)

The unrealized losses on the Company's investments in collateralized mortgage obligations 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, 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 security. Substantially all of these securities continue to be AAA rated by one or more major rating agencies.

Table of Contents

The unrealized losses on the Company's investments in obligations of states and political subdivisions were caused by conditions in the municipal securities market. The Company's investments in obligations of states and political subdivisions primarily finance essential community services such as school districts, water delivery systems, hospitals and fire protection services. Further, these bonds are primarily bank qualified issues whereby the issuing authority's total debt issued in any one year does not exceed \$30 million, thereby qualifying the bonds for tax-exempt status for federal income tax purposes. Therefore, bank qualified bonds are relatively small in amount providing a high degree of diversification within the Company's investment portfolio. The Company evaluates these securities quarterly to determine if a change in security rating has occurred or the municipality has experienced financial difficulties. Substantially all of these securities continue to be investment grade rated.

The Company does not intend to sell any investments and has concluded that it is more likely than not that it will not be required to sell the investments prior to recovery of the amortized cost basis. Therefore, the Company does not consider these investments to be other-than-temporarily impaired as of September 30, 2010.

The fair values of the investment securities could decline in the future if the general economy deteriorates, credit ratings decline, or the liquidity for securities is low. As a result, other than temporary impairments may occur in the future.

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

	Less than 12 months Unrealized		12 months or longer Unrealized		Total Unrealized	
	Fair Value	Losses	Fair Value	Losses	Fair Value	Losses
	(In thousands)					
U.S. Treasury securities	\$ 2,987	\$	\$	\$	\$ 2,987	\$
Securities of U.S. Government sponsored entities	19,979	(25)			19,979	(25)
Residential mortgage-backed securities	17,885	(124)			17,885	(124)
Obligations of States and political subdivisions	25,050	(795)	3,866	(182)	28,916	(977)
Residential 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)

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

	Less than 12 months Unrealized		12 months or longer Unrealized		Total Unrealized	
	Fair Value	Losses	Fair Value	Losses	Fair Value	Losses
	(In thousands)					
Obligations of States and political subdivisions	\$ 46,111	\$ (995)	\$ 16,964	\$ (1,195)	\$ 63,075	\$ (2,190)
Residential 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)
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Table of Contents**Note 5: Loans and Allowance for Credit Losses**

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

	At September 30, 2010	At December 31, 2009
	(In thousands)	
Originated loans:		
Commercial	\$ 491,043	\$ 498,594
Commercial real estate	769,545	801,008
Construction	28,987	32,156
Residential real estate	320,881	371,197
Consumer installment & other	467,459	498,133
Gross Loans	2,077,915	2,201,088
Allowance for loan losses	(38,129)	(41,043)
Net Loans	\$ 2,039,786	\$ 2,160,045

The carrying amount of the purchased covered loans at September 30, 2010, consisted of impaired and non impaired purchased covered loans in the following table.

	Impaired Purchased Covered Loans	Non Impaired Purchased Covered Loans	Total Purchased Covered Loans
	(In thousands)		
Purchased covered loans:			
Commercial	\$ 10,881	\$ 170,577	\$ 181,458
Commercial real estate	14,128	385,805	399,933
Construction	9,517	19,423	28,940
Residential real estate	138	18,551	18,689
Consumer installment & other	253	89,345	89,598
Total loans	\$ 34,917	\$ 683,701	\$ 718,618

The carrying amount of the purchased non-covered loans at September 30, 2010, consisted of impaired and non impaired purchased non-covered loans in the following table.

	Impaired Purchased Non- covered Loans	Non Impaired Purchased Non- covered Loans	Total Purchased Non-covered Loans
	(In thousands)		
Purchased non-covered loans:			

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Commercial	\$ 492	\$ 11,906	\$ 12,398
Commercial real estate	26,252	89,600	115,852
Construction	7,636	18,469	26,105
Residential real estate	2,143	20,706	22,849
Consumer installment & other	1,217	33,897	35,114
Total loans	\$ 37,740	\$ 174,578	\$ 212,318

Table of Contents

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

	Impaired Purchased Covered Loans	Non Impaired Purchased Covered Loans (In thousands)	Total Purchased Covered Loans
Purchased 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

Changes in the carrying amount of impaired purchased covered loans were as follows for the nine months ended September 30, 2010 and the period February 6, 2009 (acquisition date) through December 31, 2009:

	Nine months ended September 30, 2010	February 6, 2009 through December 31, 2009 (refined)
		(In thousands)
Carrying amount at the beginning of the period	\$ 43,196	\$ 80,544
Reductions during the period	(8,279)	(37,348)
Carrying amount at the end of the period	\$ 34,917	\$ 43,196

The following table represents the non impaired purchased non-covered loans receivable at the acquisition date of August 20, 2010. 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	\$ 188,206
Estimate of contractual principal not expected to be collected	(15,058)
Fair value of non impaired purchased loans receivable	\$ 175,922
The Company applied the cost recovery method to impaired purchased non-covered loans at the acquisition date of August 20, 2010 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)	\$ 70,882
Nonaccretable difference	(33,140)
Cash flows expected to be collected	37,742
Accretable difference	

Fair value of loans acquired \$ 37,742

Changes in the carrying amount of impaired purchased non-covered loans were as follows for the period from August 20, 2010 (acquisition date) through September 30, 2010:

	August 20, 2010 through September 30, 2010 (In thousands)
Carrying amount at the beginning of the period	\$ 37,742
Reductions during the period	(2)
Carrying amount at the end of the period	\$ 37,740

Table of Contents

Impaired purchased covered loans had an unpaid principal balance (less prior charge-offs) of \$52 million, \$70 million and \$164 million at September 30, 2010, December 31, 2009 and February 6, 2009, respectively.

Impaired purchased non-covered loans had an unpaid principal balance (less prior charge-offs) of \$60 million and \$60 million at September 30, 2010 and August 20, 2010, respectively.

The Company pledges loans to secure borrowings from the Federal Home Loan Bank (FHLB). At September 30, 2010, loans pledged to secure borrowing totaled \$170.1 million. The FHLB does not have the right to sell or repledge such loans.

There were no loans held for sale at September 30, 2010 and December 31, 2009.

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

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
	(In thousands)			
Balance, beginning of period	\$ 42,409	\$ 45,815	\$ 43,736	\$ 47,563
Provision for loan losses	2,800	2,800	8,400	7,200
Provision for unfunded commitments				(400)
Loans charged off	(5,216)	(3,870)	(13,926)	(10,735)
Recoveries of previously charged off loans	829	631	2,612	1,748
Net loan losses	(4,387)	(3,239)	(11,314)	(8,987)
Balance, end of period	\$ 40,822	\$ 45,376	\$ 40,822	\$ 45,376
Components:				
Allowance for loan losses	\$ 38,129	\$ 42,683		
Reserve for unfunded credit commitments	2,693	2,693		
Allowance for credit losses	\$ 40,822	\$ 45,376		

Allowance for loan losses / originated loans
outstanding

1.83% 1.88%

Management determined the credit default fair value discounts assigned to covered loans purchased on February 6, 2009 and non-covered loans purchased on August 20, 2010 remained adequate as an estimate of credit losses inherent in purchased covered and non-covered loans as of September 30, 2010.

Nonaccrual originated loans at September 30, 2010 and December 31, 2009 were \$19.4 million and \$19.9 million, respectively. Nonaccrual purchased covered loans at September 30, 2010 and December 31, 2009 were \$52.2 million and \$85.1 million, respectively. Nonaccrual purchased non-covered loans at September 30, 2010 were \$37.9 million.

There were no commitments to lend additional funds to borrowers whose loans were on nonaccrual status at September 30, 2010.

Note 6: Goodwill and Other 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 nine months ended September 30, 2010.

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

December 31, 2009	\$ 121,699
Recognition of stock option tax benefits for the exercise of options converted upon merger	(26)

September 30, 2010

\$ 121,673

Table of Contents

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 nine months ended September 30, 2010, no such adjustments were recorded.

The gross carrying amount of identifiable intangible assets and accumulated amortization was:

	At September 30, 2010		At December 31, 2009	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
	(In thousands)			
Core Deposit Intangibles	\$ 56,808	\$ (23,283)	\$ 51,538	\$ (19,160)
Merchant Draft Processing Intangible	10,300	(7,599)	10,300	(7,011)
Total Identifiable Intangible Assets	\$ 67,108	\$ (30,882)	\$ 61,838	\$ (26,171)

As of September 30, 2010, the current year and estimated future amortization expense for identifiable intangible assets was:

	Core Deposit Intangibles	Merchant Draft Processing Intangible	Total
	(In thousands)		
Ninemonths ended September 30, 2010 (actual)	\$ 4,123	\$ 588	\$ 4,711
Estimate for year ended December 31, 2010	5,559	774	6,333
2011	5,351	624	5,975
2012	4,868	500	5,368
2013	4,304	400	4,704
2014	3,946	324	4,270
2015	3,594	262	3,856

Note 7: Post Retirement Benefits

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. The Company also reimburses a portion of Medicare Part B premiums for all qualifying retirees over age 65 and their qualified 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.

The following table sets forth the net periodic post-retirement benefit costs:

	For the nine months ended September 30,	
	2010	2009
	(In thousands)	
Service cost (benefit)	\$ (270)	\$ (237)
Interest cost	144	165
Amortization of unrecognized transition obligation	45	45

Net periodic cost (benefit)	\$	(81)	\$	(27)
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The Company does not fund plan assets for any post-retirement benefit plans.

Table of Contents**Note 8: 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 \$409.8 million and \$482.0 million at September 30, 2010 and December 31, 2009, 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 \$25.5 million and \$27.4 million at September 30, 2010 and December 31, 2009, respectively. The Company also had commitments for commercial and similar letters of credit of \$3.3 million and \$176 thousand at September 30, 2010 and December 31, 2009, respectively.

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 80 percent indemnified under loss-sharing agreements with the FDIC if certain conditions are met.

Note 9: Fair Value Measurements

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Available for sale investment securities are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, such as certain loans held for investment and other assets. These nonrecurring fair value adjustments typically involve the lower-of-cost-or-fair value accounting or impairment or write-down of individual assets.

In accordance with the Fair Value Measurement and Disclosure topic of the Codification, the Company bases its fair values on the price that would be received to sell an asset or paid to transfer a liability in the principal market or most advantageous market for an asset or liability in an orderly transaction between market participants on the measurement date. A fair value measurement reflects all of the assumptions that market participants would use in pricing the asset or liability, including assumptions about the risk inherent in a particular valuation technique, the effect of a restriction on the sale or use of an asset, and the risk of nonperformance.

The Company groups its assets and liabilities measured at fair value into a three-level hierarchy, 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 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 residential 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.

Table of Contents**Assets Recorded at Fair Value on a Recurring Basis**

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

	Fair Value	At September 30, 2010		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(In thousands)				
U.S. Treasury securities	\$ 3,511	\$ 3,511	\$	\$
Securities of U.S. Government sponsored entities	118,833	118,833		
Municipal bonds:				
Federally Tax-exempt California	84,505		84,505	
Federally Tax-exempt 29 other states	119,591		119,591	
Taxable California	9,711		9,711	
Taxable 1 other state	501		501	
Residential mortgage-backed securities (MBS):				
Guaranteed by GNMA	47,613		47,613	
Issued by FNMA and FHLMC	70,650		70,650	
Residential collateralized mortgage obligations:				
Issued or guaranteed by FNMA, FHLMC, or GNMA	16,447		16,447	
All other	8,891		8,891	
Commercial mortgage-backed securities	5,191		5,191	
Asset-backed securities government guaranteed student loans	8,420		8,420	
FHLMC and FNMA stock	617	617		
Corporate securities	69,783	69,783		
Other securities	5,247	3,278	1,969	
Total securities available for sale	\$ 569,511	\$ 196,022	\$ 373,489	\$

There were no significant transfers in or out of Levels 1 and 2 for the nine months ended September 30, 2010.

	Fair Value	At December 31, 2009		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(In thousands)				
U.S. Treasury securities	\$ 2,987	\$ 2,987	\$	\$
Securities of U.S. Government sponsored entities	21,041	21,041		
Municipal bonds:				
Federally Tax-exempt California	56,431		56,431	

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Federally Tax-exempt 25 other states	97,094		97,094
Taxable California	4,668		4,668
Residential mortgage-backed securities (MBS):			
Guaranteed by GNMA	54,361		54,361
Issued by FNMA and FHLMC	91,644		91,644
Residential collateralized mortgage obligations:			
Issued or guaranteed by FNMA, FHLMC, or			
GNMA	29,536		29,536
All other	11,874		11,874
Asset-backed securities government guaranteed			
student loans	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

Table of Contents**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 during the first nine months ended September 30, 2010 and year ended December 31, 2009 that were still held in the balance sheet at the end of such periods, the following table provides the level of valuation assumptions used to determine each adjustment and the carrying value of the related assets at the dates indicated.

	Fair Value	At September 30, 2010			Total losses
		Level 1	Level 2	Level 3	
			(In thousands)		
Non-covered other real estate owned (1)	\$ 1,863	\$	\$ 1,863	\$	\$ (664)
Impaired originated loans (2)	4,780		4,780		
Total assets measured at fair value on a nonrecurring basis	\$ 6,643	\$	\$ 6,643	\$	\$ (664)

	Fair Value	At December 31, 2009			Total losses
		Level 1	Level 2	Level 3	
			(In thousands)		
Non-covered other real estate owned (1)	\$ 413	\$	\$ 413	\$	\$ (233)
Impaired originated 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.

Disclosures about Fair Value of Financial Instruments

The following section describes the valuation methodologies used by the Company for estimating fair value of financial instruments not recorded at fair value.

Cash and Due from Banks The carrying amount of cash and amounts due from banks approximate fair value due to the relatively short period of time between their origination and their expected realization.

Money Market Assets The carrying amount of money market assets approximate fair value due to the relatively short period of time between their origination and their expected realization.

Investment Securities Held to Maturity The fair values of investment securities were estimated using quoted prices as described above for Level 1 and Level 2 valuation.

Loans 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 \$38.1 million at September 30, 2010 and \$41.0 million at December 31, 2009 and the fair value discount due to credit default risk associated with purchased covered and non-covered loans of \$66.5 million and \$36.9 million, respectively at September 30, 2010 and \$93.3 million associated with purchased covered loans 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 a liquidation price for the loans.

FDIC Receivable The fair value of the FDIC receivable recorded in Other Assets was estimated by discounting estimated future cash flows using current market rates for financial instruments with similar characteristics.

Deposit Liabilities The carrying amount of demand deposits, savings accounts and money market accounts approximates fair value due to the relatively short period of time between their origination and their expected realization. The fair values of the 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.

Short-Term Borrowed Funds The carrying amount of securities sold under agreement to repurchase and other short-term borrowed funds approximate fair value due to the relatively short period of time between their origination and their expected realization. The fair values of term repurchase agreements were estimated by using interpolated yields for financial instruments with similar characteristics.

Table of Contents

Federal Home Loan Bank Advances The fair values of FHLB advances were estimated by using interpolated yields for financial instruments with similar characteristics.

Debt Financing and Notes Payable The fair values of debt financing and notes payable were estimated by using interpolated yields for financial instruments with similar characteristics.

Restricted Performance Share Grants The fair value of liabilities for unvested restricted performance share grants recorded in Other Liabilities were estimated using quoted prices as described above for Level 1 valuation.

The table below is a summary of fair value estimates for financial instruments, excluding financial instruments recorded at fair value on a recurring basis. 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. The carrying amounts in the following table are recorded in the balance sheet under the indicated captions.

The Company has not included assets and liabilities that are not financial instruments, such as goodwill, long-term relationships with deposit, merchant processing and trust customers, other purchased intangibles, premises and equipment, deferred taxes and other assets and liabilities. The total estimated fair values do not represent, and should not be construed to represent, the underlying value of the Company.

	At September 30, 2010		At December 31, 2009	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(In thousands)			
Financial Assets				
Cash and due from banks	\$ 344,169	\$ 344,169	\$ 361,135	\$ 361,135
Money market assets	392	392	442	442
Investment securities held to maturity	618,838	642,882	726,935	736,270
Loans	2,970,722	2,992,724	3,015,346	3,024,866
Other assets FDIC receivable	49,994	49,707	85,787	83,806
Financial Liabilities				
Deposits	4,072,698	4,073,550	4,060,208	4,061,380
Short-term borrowed funds	193,202	193,257	227,178	228,463
Federal Home Loan Bank Advances	66,934	67,138	85,470	85,601
Debt financing and notes payable	26,396	26,244	26,497	23,520
Other liabilities restricted performance share grants	2,069	2,069	1,942	1,942

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 10: 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 period the Series A Preferred Stock was outstanding, and reported as a reduction to net income applicable to common equity over that period.

Table of Contents**Note 11: 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.

	For the three months ended September 30,		For the nine months ended September 30,	
	2010	2009	2010	2009
	(In thousands, except per share data)			
Weighted average number of common shares outstanding basic	29,127	29,210	29,187	29,072
Add exercise of options reduced by the number of shares that could have been purchased with the proceeds of such exercise	258	219	328	241
Weighted average number of common shares outstanding diluted	29,385	29,429	29,515	29,313
Net income applicable to common equity	\$ 23,709	\$ 23,791	\$ 70,846	\$ 98,114
Basic earnings per common share	\$ 0.81	\$ 0.81	\$ 2.43	\$ 3.37
Diluted earnings per common share	0.81	0.81	2.40	3.35

For the three months and nine months ended September 30, 2010, options to purchase 273 thousand and 285 thousand shares of common stock, respectively, were outstanding but not included in the computation of diluted net income per share because the option exercise price exceeded the fair value of the stock such that their inclusion would have had an anti-dilutive effect. For the three and nine months ended September 30, 2009, options and warrants to purchase 726 thousand and 889 thousand shares of common stock, respectively, were outstanding but not included in the computation of diluted net income per share because the option exercise price exceeded the fair value of the stock such that their inclusion would have had an anti-dilutive effect.

Table of Contents**WESTAMERICA BANCORPORATION
FINANCIAL SUMMARY**

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
	(In thousands, except per share data)			
Net Interest Income (FTE)*	\$ 56,669	\$ 61,593	\$ 170,271	\$ 183,270
Provision for Loan Losses	(2,800)	(2,800)	(8,400)	(7,200)
Noninterest Income:				
Gain on acquisition	178		178	48,844
Deposit service charges and other	14,893	15,961	46,133	47,471
Total Noninterest Income	15,071	15,961	46,311	96,315
Noninterest Expense	31,508	35,151	95,635	107,940
Income Before Income Taxes (FTE)*	37,432	39,603	112,547	164,445
Income Tax Provision (FTE)*	13,723	14,346	41,701	63,180
Net Income	23,709	25,257	70,846	101,265
Preferred stock dividends and discount accretion		1,466		3,151
Net Income Applicable to Common Equity	\$ 23,709	\$ 23,791	\$ 70,846	\$ 98,114
Average Common Shares Outstanding	29,127	29,210	29,187	29,072
Diluted Average Common Shares Outstanding	29,385	29,429	29,515	29,313
Common Shares Outstanding at Period End	29,118	29,207	29,118	29,207
As Reported:				
Basic Earnings Per Common Share	\$ 0.81	\$ 0.81	\$ 2.43	\$ 3.37
Diluted Earnings Per Common Share	0.81	0.81	2.40	3.35
Return On Assets	1.95%	1.86%	1.98%	2.57%
Return On Common Equity	17.90%	19.68%	18.32%	28.38%
Net Interest Margin (FTE)*	5.54%	5.48%	5.59%	5.39%
Net Loan Losses to Average Originated Loans	0.83%	0.56%	0.71%	0.51%
Efficiency Ratio**	43.9%	45.3%	44.2%	38.6%
Average Balances:				
Total Assets	\$ 4,835,357	\$ 5,072,866	\$ 4,793,266	\$ 5,113,359
Total Earning Assets	4,068,561	4,470,851	4,071,089	4,541,596
Originated Loans	2,096,937	2,289,331	2,132,687	2,360,540
Purchased Covered Loans	743,126	974,057	787,142	900,922
Purchased Non-covered Loans	97,438		32,836	
Total Deposits	3,981,437	4,131,388	3,944,231	4,066,462
Shareholders Equity	525,630	549,331	517,121	527,635

Balances at Period End:

Total Assets	\$ 4,977,871	\$ 4,971,159
Total Earning Assets	4,197,592	4,372,739
Originated Loans	2,077,915	2,267,130
Purchased Covered Loans	718,618	932,656
Purchased Non-covered Loans	212,318	
Total Deposits	4,072,698	4,024,626
Shareholders' Equity	541,173	535,718

Financial Ratios at Period End:

Allowance for Loan Losses to Originated Loans	1.83%	1.88%
Book Value Per Common Share	\$ 18.59	\$ 16.93
Equity to Assets	10.87%	10.78%
Total Capital to Risk Adjusted Assets	14.88%	15.07%

Dividends Paid Per Common Share	\$ 0.36	\$ 0.35	\$ 1.08	\$ 1.06
Common Dividend Payout Ratio	44%	43%	45%	32%

The above financial summary has been derived from the Company's unaudited consolidated financial statements. This information should be read in conjunction with those statements, notes and the other information included elsewhere herein. Percentages under the heading "As Reported" are annualized with the exception of the efficiency ratio.

* 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).

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

Westamerica Bancorporation and subsidiaries (the Company) reported third quarter 2010 net income applicable to common equity of \$23.7 million or \$0.81 diluted earnings per common share. The third quarter of 2010 included a \$178 thousand gain on the acquisition of Sonoma Valley Bank. These results compare to net income applicable to common equity of \$23.8 million or \$0.81 diluted earnings per common share for the same period of 2009.

The Company reported net income applicable to common equity of \$70.8 million or \$2.40 diluted earnings per common share for the nine months ended September 30, 2010, compared with \$98.1 million or \$3.35 diluted earnings per common share for the same period of 2009. The first nine months of 2009 included a \$48.8 million gain on the acquisition of County Bank (County) which increased net income by \$28.3 million and earnings per diluted common share by \$0.97.

Acquisitions

As described in Note 3, Westamerica Bank (Bank) acquired assets and assumed liabilities of the former Sonoma Valley Bank on August 20, 2010. The acquired assets and assumed liabilities were measured at estimated fair values, as required by FASB ASC 805, Business Combinations. Management made significant estimates and exercised significant judgment in accounting for the acquisition. Management judgmentally measured loan fair values based on loan file reviews (including borrower financial statements and tax returns), appraised collateral values, expected cash flows, and historical loss factors. Repossessed loan collateral was primarily valued based upon appraised collateral values. The Bank also recorded an identifiable intangible asset representing the value of the core deposit customer base of Sonoma Valley Bank based on Management's evaluation of the cost of such deposits relative to alternative funding sources. In determining the value of the identifiable intangible asset, Management 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 which were purchased and assumed.

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.

Table of Contents**Net Income**

Following is a summary of the components of net income for the periods indicated:

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
	(In thousands, except per share data)			
Net interest income (FTE)	\$ 56,669	\$ 61,593	\$ 170,271	\$ 183,270
Provision for loan losses	(2,800)	(2,800)	(8,400)	(7,200)
Noninterest income	15,071	15,961	46,311	96,315
Noninterest expense	(31,508)	(35,151)	(95,635)	(107,940)
Income before taxes (FTE)	37,432	39,603	112,547	164,445
Income tax provision (FTE)	(13,723)	(14,346)	(41,701)	(63,180)
Net income	\$ 23,709	\$ 25,257	\$ 70,846	\$ 101,265
Net income applicable to common equity	\$ 23,709	\$ 23,791	\$ 70,846	\$ 98,114
Average diluted common shares	29,385	29,429	29,515	29,313
Diluted earnings per common share	\$ 0.81	\$ 0.81	\$ 2.40	\$ 3.35
Average total assets	\$ 4,835,357	\$ 5,072,866	\$ 4,793,266	\$ 5,113,359
Net income applicable to common equity to average total assets (annualized)	1.95%	1.86%	1.98%	2.57%
Net income applicable to common equity to average common stockholders equity (annualized)	17.90%	19.68%	18.32%	28.38%

Net income applicable to common equity for the third quarter of 2010 was \$82 thousand or 0.3% less than the same quarter of 2009, the net result of lower net interest income (FTE) and lower noninterest income, partially offset by decreases in noninterest expense and income tax provision (FTE) and the elimination of preferred stock dividends and discount accretion. A \$4.9 million or 8.0% decrease in net interest income (FTE) was mostly attributed to lower average balances of interest earning assets and lower yields on investments, partially offset by higher yields on loans, lower average balances of interest-bearing liabilities and lower rates paid on interest-bearing deposits. The provision for loan losses remained the same, reflecting Management's evaluation of losses inherent in the originated loan portfolio. Noninterest income decreased \$890 thousand mainly due to lower service charges on deposit accounts. Noninterest expense decreased \$3.6 million mostly due to lower personnel, occupancy and equipment expenses and other operating expenses. The provision for income taxes (FTE) decreased \$623 thousand. Net income applicable to common equity in the third quarter of 2009 reflected \$1.5 million in preferred stock dividends and discount accretion. Comparing the first nine months of 2010 to the first nine months of 2009, net income applicable to common equity decreased \$27.3 million, primarily due to a \$48.8 million gain on acquisition in the first nine months of 2009, lower net interest income (FTE) and higher provision for loan losses, partially offset by decreases in noninterest expense and income tax provision (FTE) and the elimination of preferred stock dividends and discount accretion. The lower net interest income (FTE) was primarily caused by a lower volume of average interest earning assets, lower yields on investments and higher rates paid on borrowings, partially offset by higher yields on loans, lower average balances of interest-bearing liabilities and lower rates paid on interest-bearing deposits. The provision for loan losses increased \$1.2 million, reflecting Management's evaluation of losses inherent in the originated loan portfolio. Noninterest income decreased \$50.0 million largely due to a \$48.8 million acquisition gain in the first nine months of 2009.

Noninterest expense declined \$12.3 million primarily due to decreases in personnel, occupancy and equipment expenses subsequent to integrating the acquired County Bank and lower FDIC insurance assessments. The income tax provision (FTE) decreased \$21.5 million. Net income applicable to common equity in the first nine months of 2009 reflected \$3.2 million in preferred stock dividends and discount accretion. The preferred stock was redeemed during the fourth quarter of 2009.

Table of Contents**Net Interest Income**

Following is a summary of the components of net interest income for the periods indicated:

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
	(In thousands)			
Interest and fee income	\$ 55,203	\$ 61,196	\$ 166,284	\$ 183,453
Interest expense	(3,096)	(4,500)	(9,775)	(15,078)
FTE adjustment	4,562	4,897	13,762	14,895
Net interest income (FTE)	\$ 56,669	\$ 61,593	\$ 170,271	\$ 183,270

Average earning assets	\$ 4,068,561	\$ 4,470,851	\$ 4,071,089	\$ 4,541,596
Net interest margin (FTE) (annualized)	5.54%	5.48%	5.59%	5.39%

Net interest income (FTE) decreased during the third quarter of 2010 by \$4.9 million or 8.0% from the same period in 2009 to \$56.7 million, mainly due to lower average balances of interest earning assets (down \$402 million), lower yields on investments (down 0.38%) and higher rates on short-term borrowings (up 0.08%), partially offset by higher yields on loans (up 0.1%), lower average balances of interest-bearing liabilities (down \$264 million) and lower rates paid on interest-bearing deposits (down 0.15%).

Comparing the first nine months of 2010 with the first nine months of 2009, net interest income (FTE) decreased \$13.0 million or 7.1%, primarily due to a lower volume of average earning assets (down \$471 million) and lower yields on investments (down 0.17%) and higher rates on short-term borrowings (up 0.37%), partially offset by higher yields on loans (up 0.16%), lower average balances of interest-bearing liabilities (down \$377 million) and lower rates paid on interest-bearing deposits (down 0.21%).

At September 30, 2010, purchased FDIC covered loans represented 24 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.

Interest and Fee Income

Interest and fee income (FTE) for the third quarter of 2010 decreased \$6.3 million or 9.6% from the same period in 2009. The decrease was caused by lower average balances of earning assets (down \$402 million) and lower yields on investments (down 0.38%), partially offset by higher yields on loans (up 0.1%). The total average balances of loans declined \$326 million or 10.0% due to decreases in the average balances of taxable commercial loans (down \$105 million), commercial real estate loans (down \$79 million), residential real estate loans (down \$69 million), indirect auto loans (down \$46 million) and tax-exempt commercial loans (down \$19 million). The average investment portfolio decreased \$76 million largely due to declines in average balances of collateralized mortgage obligations (down \$81 million), residential mortgage backed securities (down \$55 million), and municipal securities (down \$33 million), partially offset by increases in the average balances of U.S. Government sponsored entities (up \$48 million) and corporate and other securities (up \$36 million). The average yield on the Company's earning assets decreased from 5.88% in the third quarter of 2009 to 5.84% in the corresponding period of 2010. The composite yield on loans rose 0.1% to 6.13% due to increases in yields on taxable commercial loans (up 0.5%) and construction loans (up 2.03%), partially offset by decreases in yields on residential real estate loans (down 0.5%) and indirect auto loans (down 0.19%). Nonperforming loans are included in average loan volumes used to compute loan yields; fluctuations in nonaccrual loan volumes impact loan yields. The investment portfolio yield decreased 0.38% to 5.09%, mainly due to declines in yields on U.S. government sponsored entity obligations (down 2.78%), municipal securities (down 0.11%) and U.S. Treasury (down 2.25%), partially offset by a 0.12% increase in yields on corporate and other securities.

Table of Contents

Comparing the first nine months of 2010 with the first nine months of 2009, interest and fee income (FTE) was down \$18.3 million or 9.2%. The decrease resulted from a lower volume of average earning assets and lower yields on investment securities, partially offset by higher yields on loans. Average interest earning assets decreased \$471 million or 10.4% in the first nine months of 2010 compared with the same period of 2009 due to a \$309 million decrease in average loans and a \$162 million decrease in average investments. The decrease in the average balance of the loan portfolio was attributable to decreases in average balances of indirect auto loans (down \$101 million), taxable commercial loans (down \$98 million), residential real estate loans (down \$78 million), commercial real estate loans (down \$57 million), tax-exempt commercial loans (down \$19 million) and construction loans (down \$12 million), partially offset by a \$56 million increase in the average balance of direct consumer loans. The average investment portfolio decreased \$162 million largely due to declines in average balances of collateralized mortgage obligations (down \$89 million), municipal securities (down \$46 million), U.S. government sponsored entity obligations (down \$11 million) and residential mortgage backed securities (down \$41 million), partially offset by a \$19 million increase in the average balances of corporate and other securities. The average yield on earning assets for the first nine months of 2010 was 5.91% compared with 5.83% in the first nine months of 2009. The loan portfolio yield for the first nine months of 2010 compared with the corresponding 2009 period was higher by 0.16%, due to increases in yields on construction loans (up 1.73%), taxable commercial loans (up 0.56%), commercial real estate loans (up 0.07%) and a 0.57% increase in yields on indirect auto loans, partially offset by a 0.34% decrease in yields on residential real estate loans. The investment portfolio yield decreased by 0.17%, reflecting lower yields on U.S. government sponsored entity obligations (down 2.81%), municipal securities (down 0.05%), U.S. Treasury (down 2.32%) and corporate and other securities (down 0.38%).

Interest Expense

Interest expense in the third quarter of 2010 decreased \$1.4 million or 31.2% compared with the same period in 2009. The decrease was attributable to lower average balances of interest-bearing liabilities and lower rates paid on the interest-bearing deposits, partially offset by higher rates paid on short-term borrowings. The average rate paid on interest-bearing liabilities decreased from 0.58% in the third quarter of 2009 to 0.43% in the same quarter of 2010. Rates on interest-bearing deposits decreased 0.15% to 0.32% primarily due to decreases in rates paid on time deposits \$100 thousand or more (down 0.28%), time deposits less than \$100 thousand (down 0.26%) and preferred money market savings (down 0.15%). Rates on short-term borrowings increased 0.08%. Average interest-bearing liabilities declined \$264 million. Interest-bearing deposits decreased \$196 million mostly due to decreases in the average balance of time deposits less than \$100 thousand (down \$150 million), time deposits \$100 thousand or more (down \$32 million) and money market checking accounts (down \$30 million). Average FHLB advances and sweep accounts declined \$50 million and \$21 million, respectively.

Comparing the first nine months of 2010 with the first nine months of 2009, interest expense declined \$5.3 million or 35.2%, due to lower average balances of interest-bearing liabilities and lower rates on interest-bearing deposits, offset by higher rates paid on borrowings. Average interest-bearing liabilities during the first nine months of 2010 fell by \$377 million over the same period of 2009 mainly due to decreases in average balances of federal funds purchased (down \$144 million), FHLB advances (down \$54 million), time deposits less than \$100 thousand (down \$105 million), time deposits \$100 thousand or more (down \$73 million) and money market checking accounts (down \$37 million), partially offset by increases in the average balance of repurchases facilities (up \$12 million), regular savings (up \$14 million) and money market savings (up \$12 million). Rates paid on interest-bearing liabilities averaged 0.46% during the first nine months of 2010 compared with 0.63% for the first nine months of 2009. The average rate paid on interest-bearing deposits declined 0.21% to 0.35% in the first nine months of 2010 compared with the same period of 2009 mainly due to lower rates on time deposits less than \$100 thousand (down 0.52%), time deposits \$100 thousand or more (down 0.28%), preferred money market savings (down 0.14%) and regular savings (down 0.10%).

Net Interest Margin (FTE)

The following summarizes the components of the Company's net interest margin for the periods indicated:

Three months ended

Nine months ended

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	September 30,		September 30,	
	2010	2009	2010	2009
Yield on earning assets (FTE)	5.84%	5.88%	5.91%	5.83%
Rate paid on interest-bearing liabilities	0.43%	0.58%	0.46%	0.63%
Net interest spread (FTE)	5.41%	5.30%	5.45%	5.20%
Impact of all other net noninterest bearing funds	0.13%	0.18%	0.14%	0.19%
Net interest margin (FTE)	5.54%	5.48%	5.59%	5.39%

During the third quarter of 2010, the net interest margin (FTE) increased 0.06% compared with the same period in 2009. Lower rates paid on interest-bearing liabilities were partially offset by lower yields on earning assets and resulted in a 0.11% increase in net interest spread. The increase in the net interest spread was partially reduced by the lower net interest margin contribution of noninterest-bearing demand deposits. The net interest margin (FTE) in the first nine months of 2010 rose by 0.20% compared with the corresponding period of 2009. Earning asset yields increased 0.08% while the cost of interest-bearing liabilities declined by 0.17%, resulting in a 0.25% increase in the net interest spread. The 0.05% decrease in margin contribution from noninterest bearing funding sources resulted in the net interest margin of 5.59%.

Table of Contents**Summary of Average Balances, Yields/Rates and Interest Differential**

The following tables present, for the periods indicated, information regarding the Company's consolidated average assets, liabilities and shareholders' equity, the amount of interest income from average earning assets and the resulting annualized yields, and the amount of interest expense paid on average interest-bearing liabilities and the resulting annualized rate 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 which is exempt from federal income taxation at the current statutory tax rate (FTE).

	For the three months ended September 30, 2010		
	Average Balance	Interest Income/ Expense (In thousands)	Rates Earned/ Paid
Assets:			
Money market assets and funds sold	\$ 5,130	\$ 1	0.08%
Investment securities:			
Available for sale			
Taxable	302,176	2,158	2.86%
Tax-exempt (1)	187,405	3,059	6.53%
Held to maturity			
Taxable	166,634	1,798	4.32%
Tax-exempt (1)	469,715	7,367	6.27%
Loans:			
Commercial:			
Taxable	537,116	8,534	6.30%
Tax-exempt (1)	164,838	2,733	6.58%
Commercial real estate	1,234,475	20,696	6.65%
Real estate construction	71,043	998	5.57%
Real estate residential	355,103	3,744	4.22%
Consumer	574,926	8,677	5.99%
Total loans (1)	2,937,501	45,382	6.13%
Total earning assets (1)	4,068,561	\$ 59,765	5.84%
Other assets	766,796		
Total assets	\$ 4,835,357		
Liabilities and shareholders' equity			
Deposits:			
Noninterest bearing demand	\$ 1,417,638	\$	
Savings and interest-bearing transaction	1,672,458	892	0.21%
Time less than \$100,000	341,882	357	0.41%
Time \$100,000 or more	549,459	798	0.58%

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Total interest-bearing deposits	2,563,799	2,047	0.32%
Short-term borrowed funds	203,841	511	0.98%
Federal Home Loan Bank advances	36,298	113	1.22%
Debt financing and notes payable	26,417	425	6.43%
Total interest-bearing liabilities	2,830,355	\$ 3,096	0.43%
Other liabilities	61,734		
Shareholders' equity	525,630		
Total liabilities and shareholders' equity	\$ 4,835,357		
Net interest spread (1) (2)			5.41%
Net interest income and interest margin (1) (3)		\$ 56,669	5.54%

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

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

(3) Net interest margin is computed by calculating the difference between interest income and expense (annualized), divided by the average balance of earning

assets.

Table of Contents

	For the three months ended September 30, 2009		
	Average Balance	Interest Income/ Expense (In thousands)	Rates Earned/ Paid
Assets:			
Money market assets and funds sold	\$ 602	\$ 1	0.66%
Investment securities:			
Available for sale			
Taxable	237,965	2,352	3.95%
Tax-exempt (1)	167,339	2,846	6.80%
Held to maturity			
Taxable	275,553	3,025	4.39%
Tax-exempt (1)	526,004	8,290	6.30%
Loans:			
Commercial:			
Taxable	642,366	9,391	5.80%
Tax-exempt (1)	184,054	3,032	6.54%
Commercial real estate	1,313,545	21,967	6.63%
Real estate construction	74,707	667	3.54%
Real estate residential	424,189	5,004	4.72%
Consumer	624,527	9,518	6.05%
Total loans (1)	3,263,388	49,579	6.03%
Total earning assets (1)	4,470,851	\$ 66,093	5.88%
Other assets	602,015		
Total assets	\$ 5,072,866		
Liabilities and shareholders' equity			
Deposits:			
Noninterest bearing demand	\$ 1,371,124	\$	
Savings and interest-bearing transaction	1,687,028	1,178	0.28%
Time less than \$100,000	491,555	829	0.67%
Time \$100,000 or more	581,681	1,266	0.86%
Total interest-bearing deposits	2,760,264	3,273	0.47%
Short-term borrowed funds	221,100	509	0.90%
Federal Home Loan Bank advances	86,166	295	1.34%
Debt financing and notes payable	26,551	423	6.36%
Total interest-bearing liabilities	3,094,081	\$ 4,500	0.58%
Other liabilities	58,330		
Shareholders' equity	549,331		

Total liabilities and shareholders' equity	\$ 5,072,866	
Net interest spread (1) (2)		5.30%
Net interest income and interest margin (1) (3)	\$ 61,593	5.48%

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

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

(3) Net interest margin is computed by calculating the difference between interest income and expense (annualized), divided by the average balance of earning assets.

Table of Contents

	For the nine months ended September 30, 2010		
	Average Balance	Interest Income/ Expense (In thousands)	Rates Earned/ Paid
Assets:			
Money market assets and funds sold	\$ 2,174	\$ 2	0.12%
Investment securities:			
Available for sale			
Taxable	272,141	6,465	3.17%
Tax-exempt (1)	171,122	8,466	6.60%
Held to maturity			
Taxable	186,336	6,119	4.38%
Tax-exempt (1)	486,651	22,906	6.28%
Loans:			
Commercial:			
Taxable	546,269	25,660	6.28%
Tax-exempt (1)	169,314	8,344	6.59%
Commercial real estate	1,232,406	61,229	6.64%
Real estate construction	65,352	2,767	5.66%
Real estate residential	363,337	12,104	4.44%
Consumer	575,987	25,984	6.03%
Total loans (1)	2,952,665	136,088	6.16%
Total earning assets (1)	4,071,089	\$ 180,046	5.91%
Other assets	722,177		
Total assets	\$ 4,793,266		
Liabilities and shareholders' equity			
Deposits:			
Noninterest bearing demand	\$ 1,394,033	\$	
Savings and interest-bearing transaction	1,640,421	2,725	0.22%
Time less than \$100,000	360,929	1,425	0.53%
Time \$100,000 or more	548,848	2,566	0.63%
Total interest-bearing deposits	2,550,198	6,716	0.35%
Short-term borrowed funds	209,846	1,538	0.97%
Federal Home Loan Bank advances	23,767	249	1.38%
Debt financing and notes payable	26,450	1,272	6.41%
Total interest-bearing liabilities	2,810,261	\$ 9,775	0.46%
Other liabilities	71,851		
Shareholders' equity	517,121		

Total liabilities and shareholders' equity	\$ 4,793,266	
Net interest spread (1) (2)		5.45%
Net interest income and interest margin (1) (3)	\$ 170,271	5.59%

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

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

(3) Net interest margin is computed by calculating the difference between interest income and expense (annualized), divided by the average balance of earning assets.

Table of Contents

	For the nine months ended September 30, 2009		
	Average Balance	Interest Income/ Expense (In thousands)	Rates Earned/ Paid
Assets:			
Money market assets and funds sold	\$ 942	\$ 3	0.43%
Investment securities:			
Available for sale			
Taxable	242,125	6,775	3.73%
Tax-exempt (1)	170,519	8,591	6.72%
Held to maturity			
Taxable	332,416	11,384	4.57%
Tax-exempt (1)	534,132	25,219	6.30%
Loans:			
Commercial:			
Taxable	644,107	27,565	5.72%
Tax-exempt (1)	188,479	9,351	6.63%
Commercial real estate	1,289,190	63,354	6.57%
Real estate construction	77,677	2,286	3.93%
Real estate residential	440,975	15,802	4.78%
Consumer	621,034	28,018	6.03%
Total loans (1)	3,261,462	146,376	6.00%
Total earning assets (1)	4,541,596	\$ 198,348	5.83%
Other assets	571,763		
Total assets	\$ 5,113,359		
Liabilities and shareholders' equity			
Deposits:			
Noninterest bearing demand	\$ 1,330,495	\$	
Savings and interest-bearing transaction	1,647,624	3,635	0.29%
Time less than \$100,000	466,175	3,662	1.05%
Time \$100,000 or more	622,168	4,228	0.91%
Total interest-bearing deposits	2,735,967	11,525	0.56%
Short-term borrowed funds	347,072	1,572	0.60%
Federal Home Loan Bank advances	77,290	714	1.22%
Debt financing and notes payable	26,584	1,267	6.35%
Total interest-bearing liabilities	3,186,913	\$ 15,078	0.63%
Other liabilities	68,316		
Shareholders' equity	527,635		

Total liabilities and shareholders' equity	\$ 5,113,359	
Net interest spread (1) (2)		5.20%
Net interest income and interest margin (1) (3)	\$ 183,270	5.39%

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

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

(3) Net interest margin is computed by calculating the difference between interest income and expense (annualized), divided by the average balance of earning assets.

Table of Contents**Summary of Changes in Interest Income and Expense due to Changes in Average Asset & Liability Balances and Yields Earned & Rates Paid**

The following tables set forth a summary of the changes in interest income and interest expense due to changes in average asset 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.

	Three months ended September 30, 2010 compared with Three months ended September 30, 2009		
	Volume	Rate	Total
	(In thousands)		
Interest and fee income:			
Money market assets and funds sold	\$ 2	\$ (2)	\$ 0
Investment securities:			
Available for sale			
Taxable	553	(747)	(194)
Tax-exempt (1)	332	(119)	213
Held to maturity			
Taxable	(1,176)	(51)	(1,227)
Tax-exempt (1)	(883)	(40)	(923)
Loans:			
Commercial:			
Taxable	(1,626)	769	(857)
Tax-exempt (1)	(318)	19	(299)
Commercial real estate	(1,325)	54	(1,271)
Real estate construction	(34)	365	331
Real estate residential	(763)	(497)	(1,260)
Consumer	(749)	(92)	(841)
Total loans (1)	(4,815)	618	(4,197)
Total decrease in interest and fee income (1)	(5,987)	(341)	(6,328)

Interest expense:

Deposits: