
CPF 10-Q 9/30/2008

Section 1: 10-Q (FORM 10-Q)

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

FORM 10-Q

(Mark One)

T QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2008

or

£ 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 0-10777



CENTRAL PACIFIC FINANCIAL CORP.
(Exact name of registrant as specified in its charter)

Hawaii
(State or other jurisdiction of
incorporation or organization)

99-0212597
(I.R.S. Employer
Identification No.)

220 South King Street, Honolulu, Hawaii 96813
(Address of principal executive offices) (Zip Code)

(808) 544-0500
(Registrant's telephone number, including area code)

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

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

Large accelerated filer **T**

Accelerated filer **£**

Non-accelerated filer **£**

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 **T**

The number of shares outstanding of registrant's common stock, par value \$.01 per share, on November 3, 2008 was 28,728,478 shares.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

Forward-Looking Statements

This document may contain forward-looking statements concerning projections of revenues, income, earnings per share, capital expenditures, dividends, capital structure, or other financial items, concerning plans and objectives of management for future operations, concerning future economic performance, or concerning any of the assumptions underlying or relating to any of the foregoing. Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts, and may include the words “believes”, “plans”, “intends”, “expects”, “anticipates”, “forecasts” or words of similar meaning. While we believe that our forward-looking statements and the assumptions underlying them are reasonably based, such statements and assumptions are by their nature subject to risks and uncertainties, and thus could later prove to be inaccurate or incorrect. Accordingly, actual results could materially differ from projections for a variety of reasons, to include, but not limited to: the impact of local, national, and international economies and events (including natural disasters such as wildfires, tsunamis and earthquakes) on the Company’s business and operations and on tourism, the military, and other major industries operating within the Hawaii market and any other markets in which the Company does business; the impact of legislation affecting the banking industry; the impact of competitive products, services, pricing, and other competitive forces; movements in interest rates; loan delinquency rates and changes in asset quality; adverse conditions in the public debt market, the stock market or other capital markets, including any adverse changes in the price of the Company’s stock; and a general deterioration or malaise in economic conditions, including the continued destabilizing factors in the financial industry and continued deterioration of the real estate market, as well as the impact of declining levels of consumer and business confidence in the state of the economy in general and in financial institutions in particular. For further information on factors that could cause actual results to materially differ from projections, please see the Company’s publicly available Securities and Exchange Commission filings, including the Company’s Form 10-K for the last fiscal year. The Company does not update any of its forward-looking statements.

Item 1. Financial Statements

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Unaudited)

(Dollars in thousands)	September 30, 2008	December 31, 2007
Assets		
Cash and due from banks	\$ 68,293	\$ 79,088
Interest-bearing deposits in other banks	133	241
Federal funds sold	12,000	2,800
Investment securities:		
Available for sale	779,016	835,130
Held to maturity (fair value of \$23,896 at September 30, 2008 and \$46,077 at December 31, 2007)	23,968	46,124
Total investment securities	802,984	881,254
Loans held for sale	36,470	37,572
Loans and leases	4,080,266	4,141,705
Less allowance for loan and lease losses	100,227	92,049
Net loans and leases	3,980,039	4,049,656
Premises and equipment, net	81,918	82,841
Accrued interest receivable	22,591	26,041
Investment in unconsolidated subsidiaries	16,104	17,404
Other real estate	11,590	-
Goodwill	152,820	244,702
Other intangible assets	43,519	39,972
Bank-owned life insurance	134,200	131,454
Federal Home Loan Bank stock	48,797	48,797
Income tax receivable	41,608	1,488
Other assets	51,238	37,076
Total assets	\$ 5,504,304	\$ 5,680,386
Liabilities and Shareholders' Equity		
Deposits:		
Noninterest-bearing demand	\$ 596,907	\$ 665,034
Interest-bearing demand	457,906	461,175
Savings and money market	1,067,690	1,178,855
Time	1,654,569	1,697,655
Total deposits	3,777,072	4,002,719
Short-term borrowings	278,205	16,000
Long-term debt	881,534	916,019
Minority interest	10,055	13,104
Other liabilities	47,367	58,141
Total liabilities	4,994,233	5,005,983
Shareholders' equity:		
Preferred stock, no par value, authorized 1,000,000 shares, none issued	-	-
Common stock, no par value, authorized 100,000,000 shares, issued and outstanding 28,729,933 shares at September 30, 2008 and 28,756,647 shares at December 31, 2007	403,117	403,304
Surplus	55,639	54,669
Retained earnings	63,489	222,644
Accumulated other comprehensive loss	(12,174)	(6,214)
Total shareholders' equity	510,071	674,403
Total liabilities and shareholders' equity	\$ 5,504,304	\$ 5,680,386

See accompanying notes to consolidated financial statements.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
(Amounts in thousands, except per share data)				
Interest income:				
Interest and fees on loans and leases	\$ 64,224	\$ 78,325	\$ 200,195	\$ 231,561
Interest and dividends on investment securities:				
Taxable interest	8,696	8,386	27,275	25,964
Tax-exempt interest	1,351	1,343	4,156	4,071
Dividends	7	83	42	176
Interest on deposits in other banks	4	82	11	156
Interest on Federal funds sold and securities purchased under agreements to resell	33	125	76	244
Dividends on Federal Home Loan Bank stock	171	73	464	195
Total interest income	74,486	88,417	232,219	262,367
Interest expense:				
Interest on deposits:				
Demand	251	139	567	418
Savings and money market	3,171	6,321	9,936	18,773
Time	10,932	17,925	37,367	51,182
Interest on short-term borrowings	1,583	302	5,863	1,110
Interest on long-term debt	7,965	10,900	25,661	31,484
Total interest expense	23,902	35,587	79,394	102,967
Net interest income	50,584	52,830	152,825	159,400
Provision for loan and lease losses	22,900	21,200	144,972	24,800
Net interest income after provision for loan and lease losses	27,684	31,630	7,853	134,600
Other operating income:				
Service charges on deposit accounts	3,702	3,581	10,756	10,488
Other service charges and fees	3,501	3,281	10,626	10,052
Income from fiduciary activities	945	968	2,940	2,583
Equity in earnings of unconsolidated subsidiaries	103	169	517	593
Fees on foreign exchange	142	149	448	541
Investment securities gains	12	-	265	-
Loan placement fees	201	248	567	790
Net gain on sales of residential loans	1,807	1,116	5,846	3,886
Income from bank-owned life insurance	888	1,861	3,603	4,075
Other	409	379	2,352	1,434
Total other operating income	11,710	11,752	37,920	34,442
Other operating expense:				
Salaries and employee benefits	17,558	16,240	53,570	49,534
Net occupancy	3,261	2,624	9,380	7,721
Equipment	1,420	1,255	4,248	3,810
Amortization of other intangible assets	1,237	1,162	3,687	3,542
Communication expense	1,155	1,032	3,365	3,118
Legal and professional services	3,209	2,223	8,237	6,660
Computer software expense	865	869	2,537	2,561
Advertising expense	1,016	661	2,398	1,919
Goodwill impairment	-	-	94,279	-
Foreclosed asset expense	83	-	6,657	-
Loss on sales of commercial real estate loans	203	-	1,874	-
Write down of assets	100	-	22,524	-
Other	7,358	5,487	16,452	14,495
Total other operating expense	37,465	31,553	229,208	93,360
Income (loss) before income taxes	1,929	11,829	(183,435)	75,682
Income tax expense (benefit)	(1,112)	2,722	(41,876)	25,424
Net income (loss)	\$ 3,041	\$ 9,107	\$ (141,559)	\$ 50,258
Per share data:				
Basic earnings (loss) per share	\$ 0.11	\$ 0.30	\$ (4.94)	\$ 1.65
Diluted earnings (loss) per share	0.11	0.30	(4.94)	1.64
Cash dividends declared	0.10	0.25	0.60	0.73
Shares used in computation:				
Basic shares	28,665	30,192	28,668	30,480
Diluted shares	28,699	30,378	28,668	30,707

See accompanying notes to consolidated financial statements.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

Nine Months Ended September 30,

2008 **2007**

(Dollars in thousands)

	2008	2007
Cash flows from operating activities:		
Net income (loss)	\$ (141,559)	\$ 50,258
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Provision for loan and lease losses	144,972	24,800
Depreciation and amortization	5,964	5,303
Goodwill impairment	94,279	-
Write down of assets	22,524	-
Foreclosed asset expense	6,657	-
Amortization of other intangible assets	3,687	3,542
Net amortization of investment securities	1,074	1,591
Share-based compensation	1,764	2,920
Net gain on investment securities	(265)	-
Deferred income tax benefit	(11,889)	(6,521)
Net gain on sales of residential loans	(5,846)	(3,886)
Loss on sale of commercial real estate loans	1,874	-
Proceeds from sales of trading securities	4,986	-
Proceeds from sales of loans held for sale	1,147,478	688,923
Originations of loans held for sale	(973,176)	(689,756)
Tax benefits from share-based compensation	(40)	(10)
Equity in earnings of unconsolidated subsidiaries	(517)	(593)
Increase in cash surrender value of bank-owned life insurance	(3,589)	(4,124)
Increase in income tax receivable	(40,120)	(2,283)
Net change in other assets and liabilities	(9,630)	(2,178)
Net cash provided by operating activities	<u>248,628</u>	<u>67,986</u>
Cash flows from investing activities:		
Proceeds from maturities of and calls on investment securities available for sale	413,915	520,640
Proceeds from sales of investment securities available for sale	10,735	-
Purchases of investment securities available for sale	(369,131)	(485,956)
Proceeds from maturities of and calls on investment securities held to maturity	21,648	17,657
Proceeds from sales of investment securities held to maturity	454	-
Net loan originations	(435,078)	(220,098)
Purchase of loan portfolio	-	(10,496)
Proceeds from sales of loans originated for investment	111,471	-
Proceeds from sales of securitized residential mortgage loans	20,838	-
Proceeds from sale of other real estate	2,000	-
Proceeds from bank-owned life insurance	843	1,364
Purchase of bank-owned life insurance	-	(25,000)
Purchases of premises and equipment	(5,041)	(8,136)
Distributions from unconsolidated subsidiaries	656	596
Contributions to unconsolidated subsidiaries	(846)	(5,294)
Acquisition of businesses and minority interests	(6,738)	-
Net cash used in investing activities	<u>(234,274)</u>	<u>(214,723)</u>
Cash flows from financing activities:		
Net increase (decrease) in deposits	(225,647)	97,776
Proceeds from long-term debt	30,000	150,000
Repayments of long-term debt	(64,111)	(73,046)
Net increase (decrease) in short-term borrowings	262,205	(7,063)
Cash dividends paid	(17,240)	(22,274)
Tax benefits from share-based compensation	40	10
Repurchases of common stock	(1,824)	(31,075)
Proceeds from issuance of common stock and stock option exercises	520	2,261
Net cash provided by (used in) financing activities	<u>(16,057)</u>	<u>116,589</u>
Net decrease in cash and cash equivalents	(1,703)	(30,148)
Cash and cash equivalents at beginning of period	82,129	135,648
Cash and cash equivalents at end of period	<u>\$ 80,426</u>	<u>\$ 105,500</u>
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest	\$ 85,751	\$ 100,488
Income taxes	13,798	24,711
Cash received during the period for:		
Income taxes	1,820	-
Supplemental disclosure of noncash investing and financing activities:		
Net change in common stock held by directors' deferred compensation plan	\$ 73	\$ 33
Net reclassification of loans to other real estate	17,490	-
Net transfer of loans to loans held for sale	167,354	-
Securitization of residential mortgage loans into trading mortgage backed securities	4,995	-
Securitization of residential mortgage loans into available for sale mortgage backed securities	10,936	-

See accompanying notes to consolidated financial statements.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Central Pacific Financial Corp. (referred to herein as “the Company,” “we,” “us,” or “our”) have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. These interim condensed consolidated financial statements and notes should be read in conjunction with the Company’s consolidated financial statements and notes thereto filed on Form 10-K for the fiscal year ended December 31, 2007. In the opinion of management, all adjustments necessary for a fair presentation have been made and include all normal recurring adjustments. Interim results of operations are not necessarily indicative of results to be expected for the year.

Certain prior period amounts in the consolidated financial statements and the notes thereto have been reclassified to conform to the current period presentation. Such reclassifications had no effect on net income (loss) or shareholders’ equity for any periods presented.

2. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

On January 1, 2008, we adopted the following new accounting pronouncements:

- SFAS 157 – Statement of Financial Accounting Standards No. 157, “Fair Value Measurements,”
- SFAS 159 – Statement of Financial Accounting Standards No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities,”
- EITF 06-10 – Emerging Issues Task Force Issue No. 06-10, “Accounting for Deferred Compensation and Postretirement Benefit Aspects of Collateral Assignment Split-Dollar Life Insurance Arrangements,” and
- SAB 109 – Staff Accounting Bulletin No. 109, “Written Loan Commitments Recorded at Fair Value Through Earnings.”

The adoption of these pronouncements did not have a material impact on our consolidated financial statements.

In February 2008, the Financial Accounting Standards Board (“FASB”) amended SFAS 157 through the issuance of FSP FAS No. 157-2, “Effective Date of FASB Statement No. 157” (“FSP FAS 157-2”). FSP FAS 157-2 is effective upon issuance and delays the effective date of SFAS 157 to fiscal years beginning after November 15, 2008, for nonfinancial assets and nonfinancial liabilities that are not recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). As permitted under SFAS 157, we plan to adopt the provisions of SFAS 157 for nonfinancial assets and nonfinancial liabilities that are not recognized or disclosed at fair value in our financial statements on a recurring basis effective January 1, 2009. We are evaluating the impact of the adoption of SFAS 157 for nonfinancial assets and nonfinancial liabilities on our consolidated financial statements.

In October 2008, the FASB issued FSP FAS No. 157-3, “Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active” (“FSP FAS 157-3”). FSP FAS 157-3 clarifies the application of SFAS 157 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. FSP FAS 157-3 is effective upon issuance, including prior periods for which financial statements have not been issued. Revisions resulting from a change in the valuation technique or its application should be accounted for as a change in accounting estimate following the guidance in SFAS 154, “Accounting Changes and Error Corrections.” However, the disclosure provisions in SFAS 154 for a change in accounting estimate are not required for revisions resulting from a change in valuation technique or its application. We adopted the provisions of FSP FAS 157-3 and such adoption did not have a material impact on our consolidated financial statements for the three and nine months ended September 30, 2008.

In December 2007, the FASB issued SFAS No. 141(R), “Business Combinations” (“SFAS 141(R)"). SFAS 141(R) establishes principles and requirements for how the acquirer in a business combination recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest (minority interest) in the acquiree. The statement also provides guidance for recognizing and measuring the goodwill acquired in the business combination or a gain from a bargain purchase and determining what information should be disclosed to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS 141(R) is to be applied prospectively to business combinations for which the acquisition date is on or after fiscal years beginning after December 15, 2008. We do not expect the adoption of this statement to have a material impact on our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, “Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB No. 51” (“SFAS 160”). SFAS 160 establishes new accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. Specifically, this statement requires the recognition of a noncontrolling interest (minority interest) as equity in the consolidated financial statements and separate from the parent’s equity. The amount of net income attributable to the noncontrolling interest will be included in consolidated net income on the face of the income statement. SFAS 160 clarifies that changes in a parent’s ownership interest in a subsidiary that do not result in deconsolidation are equity transactions if the parent retains its controlling financial interest. In addition, this statement requires that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated. Such gain or loss will be measured using the fair value of the noncontrolling equity investment on the deconsolidation date. SFAS 160 also includes expanded disclosure requirements regarding the interests of the parent and its noncontrolling interest. SFAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited. We are evaluating the impact of this pronouncement on our consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, “Disclosures about Derivative Instruments and Hedging Activities - an amendment of FASB Statement 133” (“SFAS 161”). SFAS 161 enhances required disclosures regarding derivatives and hedging activities, including enhanced disclosures regarding how (a) an entity uses derivative instruments; (b) derivative instruments and related hedged items are accounted for under SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities; and (c) derivative instruments and related hedged items affect an entity’s financial position, financial performance, and cash flows. Specifically, SFAS 161 requires (1) disclosure of the objectives for using derivative instruments be disclosed in terms of underlying risk and accounting designation; (2) disclosure of the fair values of derivative instruments and their gains and losses in a tabular format; (3) disclosure of information about credit-risk-related contingent features; and (4) cross-reference from the derivative footnote to other footnotes in which derivative-related information is disclosed. SFAS 161 is effective for fiscal years and interim periods beginning after November 15, 2008. We are evaluating the impact of this pronouncement on our consolidated financial statements.

In May 2008, the FASB issued SFAS No. 162, “The Hierarchy of Generally Accepted Accounting Principles” (“SFAS 162”). SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles in the United States. SFAS 162 is effective 60 days following the Securities and Exchange Commission’s approval of the Public Company Accounting Oversight Board amendments to AU Section 411. We are evaluating the impact of this pronouncement on our consolidated financial statements.

In June 2008, the FASB issued FSP EITF No. 03-6-1, “Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities” (“FSP EITF 03-6-1”). FSP EITF 03-6-1 states that unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings per share pursuant to the two-class method. FSP EITF 03-6-1 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited. We are evaluating the impact of this pronouncement on our consolidated financial statements.

In June 2008, the EITF reached a consensus on EITF No. 08-3 “Accounting by Lessees for Nonrefundable Maintenance Deposits” (“EITF 08-3”). EITF 08-3 states that lessees shall account for nonrefundable maintenance deposits as a deposit asset if it is probable that the maintenance activities will occur and the deposit is realizable. EITF 08-3 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. Early adoption is prohibited. We are evaluating the impact of this pronouncement on our consolidated financial statements.

3. BUSINESS COMBINATIONS

On July 1, 2008 (the “acquisition date”), we completed the acquisition of certain assets of Pacific Islands Financial Management LLC (“PIFM”), a Hawaii based investment advisory firm that managed money for private clients, corporate accounts and various retirement plans. The acquisition is expected to enhance our asset management operations by providing access to new customers and greater resources.

At the acquisition date, we paid \$2.1 million (the “purchase price”) in cash to purchase the assets of PIFM. Additional cash consideration of up to \$2.1 million may be paid five years from the date of acquisition as a result of earnout provisions tied to revenue growth during the five year period immediately following the acquisition date.

The acquisition was accounted for using the purchase accounting method. Accordingly, the purchase price was allocated to the assets acquired based on their estimated fair values at the acquisition date. No liabilities were assumed in the acquisition. As a result of the acquisition, we recognized certain identifiable intangible assets including customer relationships of \$1.4 million and non-compete agreements of \$0.3 million, which are amortized on a straight-line basis over their estimated useful lives of 10 years and 5 years, respectively. The excess of the purchase price over the amounts assigned to the assets acquired of \$0.5 million was recognized as goodwill and was assigned to our Hawaii Market reportable segment. It is anticipated that all of the goodwill resulting from the acquisition will be deductible for income tax purposes.

Pro forma results of operations have not been presented for the acquisition of PIFM because the effects of the acquisition were not material to our consolidated financial statements.

4. INVESTMENT SECURITIES

A summary of investment securities is as follows:

	<u>Amortized cost</u>	<u>Gross unrealized gains</u>	<u>Gross unrealized losses</u>	<u>Estimated fair value</u>
(Dollars in thousands)				
September 30, 2008				
<u>Held to Maturity</u>				
U.S. Government sponsored entities debt securities	\$ 8,623	\$ 7	\$ -	\$ 8,630
U.S. Government sponsored entities mortgage-backed securities	7,261	4	(104)	7,161
States and political subdivisions	8,084	21	-	8,105
Total	<u>\$ 23,968</u>	<u>\$ 32</u>	<u>\$ (104)</u>	<u>\$ 23,896</u>
<u>Available for Sale</u>				
U.S. Government sponsored entities debt securities	\$ 99,061	\$ 315	\$ (1,378)	\$ 97,998
U.S. Government sponsored entities mortgage-backed securities	446,695	2,569	(2,627)	446,637
States and political subdivisions	129,357	602	(3,552)	126,407
Privately-issued mortgage-backed securities	113,786	-	(6,737)	107,049
Other	1,026	-	(101)	925
Total	<u>\$ 789,925</u>	<u>\$ 3,486</u>	<u>\$ (14,395)</u>	<u>\$ 779,016</u>
December 31, 2007				
<u>Held to Maturity</u>				
U.S. Government sponsored entities debt securities	\$ 26,844	\$ -	\$ (68)	\$ 26,776
U.S. Government sponsored entities mortgage-backed securities	9,637	9	(41)	9,605
States and political subdivisions	9,643	53	-	9,696
Total	<u>\$ 46,124</u>	<u>\$ 62</u>	<u>\$ (109)</u>	<u>\$ 46,077</u>
<u>Available for Sale</u>				
U.S. Government sponsored entities debt securities	\$ 79,563	\$ 539	\$ -	\$ 80,102
U.S. Government sponsored entities mortgage-backed securities	484,012	1,644	(2,229)	483,427
States and political subdivisions	147,559	1,251	(672)	148,138
Privately-issued mortgage-backed securities	123,499	401	(1,167)	122,733
Other	898	-	(168)	730
Total	<u>\$ 835,531</u>	<u>\$ 3,835</u>	<u>\$ (4,236)</u>	<u>\$ 835,130</u>

The amortized cost and estimated fair value of investment securities at September 30, 2008 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	September 30, 2008	
	Amortized cost	Estimated fair value
(Dollars in thousands)		
Held to Maturity		
Due in one year or less	\$ 11,498	\$ 11,518
Due after one year through five years	1,064	1,072
Due after five years through ten years	922	922
Due after ten years	3,223	3,223
Mortgage-backed securities	7,261	7,161
Total	\$ 23,968	\$ 23,896
Available for Sale		
Due in one year or less	\$ 5,408	\$ 5,460
Due after one year through five years	60,902	61,324
Due after five years through ten years	112,387	110,922
Due after ten years	49,721	46,699
Mortgage-backed securities	560,481	553,686
Other	1,026	925
Total	\$ 789,925	\$ 779,016

Proceeds from sales of investment securities available for sale were \$10.7 million for the nine months ended September 30, 2008, resulting in gross realized gains of \$0.1 million and gross realized losses of \$0.1 million. There were no sales of available for sale securities during the nine months ended September 30, 2007. Proceeds from sales of investment securities classified as trading were \$5.0 million for the nine months ended September 30, 2008, resulting in gross realized gains and losses of less than \$0.1 million. There were no sales of trading securities during the nine months ended September 30, 2007.

Investment securities of \$731.9 million at September 30, 2008 were pledged to secure public funds on deposit, securities sold under agreements to repurchase and other long-term and short-term borrowings.

Provided below is a summary of investment securities which were in an unrealized loss position at September 30, 2008 and December 31, 2007. There were a total of 142 securities in an unrealized loss position at September 30, 2008.

<u>Description of Securities</u>	<u>Less than 12 months</u>		<u>12 months or longer</u>		<u>Total</u>	
	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>
At September 30, 2008:						
U.S. Government sponsored entities debt securities	\$ 37,629	\$ (1,378)	\$ -	\$ -	\$ 37,629	\$ (1,378)
U.S. Government sponsored entities mortgage-backed securities	211,190	(1,848)	35,800	(883)	246,990	(2,731)
States and political subdivisions	61,234	(3,518)	2,084	(34)	63,318	(3,552)
Privately issued mortgage backed-securities	52,414	(4,988)	54,635	(1,749)	107,049	(6,737)
Other	925	(101)	-	-	925	(101)
Total temporarily impaired securities	\$ 363,392	\$ (11,833)	\$ 92,519	\$ (2,666)	\$ 455,911	\$ (14,499)
At December 31, 2007:						
U.S. Government sponsored entities debt securities	\$ -	\$ -	\$ 26,776	\$ (68)	\$ 26,776	\$ (68)
U.S. Government sponsored entities mortgage-backed securities	44,436	(93)	200,045	(2,177)	244,481	(2,270)
States and political subdivisions	21,479	(348)	25,013	(324)	46,492	(672)
Privately issued mortgage backed-securities	20	-	81,307	(1,167)	81,327	(1,167)
Other	730	(168)	-	-	730	(168)
Total temporarily impaired securities	\$ 66,665	\$ (609)	\$ 333,141	\$ (3,736)	\$ 399,806	\$ (4,345)

The declines in market value were primarily attributable to changes in interest rates and disruptions in the credit and financial markets. Because we have the ability and intent to hold all of these investments until a recovery of fair value, which may be maturity, we do not consider these investments to be other-than-temporarily impaired.

5. LOANS AND LEASES

Loans, excluding loans held for sale, consisted of the following at the dates indicated:

	<u>September 30,</u> <u>2008</u>	<u>December 31,</u> <u>2007</u>
	(Dollars in thousands)	
Commercial, financial and agricultural	\$ 375,389	\$ 385,521
Real estate:		
Construction	1,113,110	1,226,138
Mortgage - residential	1,098,849	1,036,702
Mortgage - commercial	1,250,491	1,243,383
Consumer	191,947	209,166
Leases	60,204	53,303
	4,089,990	4,154,213
Unearned income	(9,724)	(12,508)
Total loans and leases	\$ 4,080,266	\$ 4,141,705

Impaired loans requiring an allowance for loan and lease losses at September 30, 2008 and December 31, 2007 amounted to \$49.8 million and \$74.3 million, respectively, and included all nonaccrual and restructured loans greater than \$0.5 million. At September 30, 2008 impaired loans not requiring an allowance for loan and lease losses amounted to \$78.0 million. There were no impaired loans that did not require an allowance at December 31, 2007.

6. ALLOWANCE FOR LOAN AND LEASE LOSSES

The following table presents the changes in the allowance for loan and lease losses (the "Allowance") for the periods indicated:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(Dollars in thousands)			
Balance, beginning of period	\$ 86,050	\$ 51,409	\$ 92,049	\$ 52,280
Provision for loan and lease losses	22,900	21,200	144,972	24,800
	108,950	72,609	237,021	77,080
Charge-offs	(9,141)	(835)	(138,208)	(6,513)
Recoveries	418	743	1,414	1,950
Net charge-offs	(8,723)	(92)	(136,794)	(4,563)
Balance, end of period	\$ 100,227	\$ 72,517	\$ 100,227	\$ 72,517

As a result of the downturn in the California residential construction market, which began in 2007 and has continued through the third quarter of 2008, some of our borrowers are finding it increasingly difficult to repay amounts due on their outstanding balances as they primarily rely on the proceeds received from the sales of homes to repay their loans. In turn, the collateral values securing some of these loans have significantly declined in value as evidenced by appraisals received in the first three quarters of 2008. In some instances, recent appraisals reflect market values that have dropped more than 50% from the market values indicated in appraisals obtained in the latter part of 2007. Due to the deterioration in the California housing market and the downturn in the national and local economies, we have also started to see signs of weakness in a few of our mainland commercial construction and Hawaii residential construction borrowers. These factors have contributed to increases in the number of loan downgrades, nonaccrual loans, specific reserves on certain impaired loans and certain loan loss factors for specified pools of loans during the nine months ended September 30, 2008. Additionally, our methodology for determining the adequacy of the Allowance has required that we increase our reserve levels on these loans.

Net charge-offs for the nine months ended September 30, 2008 included charge-offs of loans transferred to loans held for sale of \$79.5 million and were primarily concentrated on loans with direct exposure to the California residential construction market. There were no net charge-offs of loans transferred to loans held for sale during the three months ended September 30, 2008.

In July 2008, we reduced our exposure to the California residential construction market by selling certain non-performing assets with a combined carrying amount of \$44.2 million at June 30, 2008. No gain or loss was recorded on the sale as the carrying values of these assets were written down to their sales price at June 30, 2008.

7. SECURITIZATIONS

During the nine months ended September 30, 2008, we securitized certain residential mortgage loans with an outstanding principal balance of \$36.5 million with a U.S. Government sponsored entity. After the securitizations, we continued to hold mortgage-backed securities and service the residential mortgage loans.

At September 30, 2008, \$10.9 million of unsold mortgage-backed securities that we received were categorized as available for sale securities and were therefore recorded at their fair value of \$10.9 million. The fair values of these mortgage-backed securities were based on quoted prices of similar instruments in active markets in accordance with SFAS 157. Unrealized gains and losses on these securities were recorded in other comprehensive income (loss) and were less than \$0.1 million at September 30, 2008. During the nine months ended, we recognized a gain of \$0.3 million on the sale of securitized mortgage-backed securities.

We recorded \$0.5 million of servicing assets related to the securitizations during the nine months ended September 30, 2008. The servicing assets were recorded at their respective fair values at the time of securitization. The fair value of the servicing assets were determined using a discounted cash flow model based on market value assumptions at the time of securitization and is amortized in proportion to and over the period of net servicing income in accordance with SFAS 156.

8. GOODWILL AND OTHER INTANGIBLE ASSETS

The following table presents the changes in goodwill allocated to each of our reportable segments during the nine months ended September 30, 2008:

	<u>Hawaii Market</u>	<u>Commercial Real Estate</u>	<u>Total</u>
	(Dollars in thousands)		
Balance, beginning of period	\$ 150,423	\$ 94,279	\$ 244,702
Additions	2,397	-	2,397
Impairment charge	-	(94,279)	(94,279)
Balance, end of period	<u>\$ 152,820</u>	<u>\$ -</u>	<u>\$ 152,820</u>

The additions to goodwill were the result of an earnout payment of \$1.4 million related to our acquisition of Hawaii HomeLoans in fiscal 2005, goodwill recognized from the acquisition of PIFM of \$0.5 million and adjustments related to CB Bancshares, Inc. income tax contingencies of \$0.5 million.

At the end of the second quarter of 2008, we experienced a decline in our market capitalization which we determined to be an indicator that an impairment test was required under SFAS 142. As a result of the impairment test performed, we determined that the remaining goodwill associated with our Commercial Real Estate reporting segment was impaired and we recorded an impairment charge of \$94.3 million in the second quarter of 2008. At September 30, 2008, we performed an impairment assessment and concluded that our remaining goodwill was not impaired.

Other intangible assets include a core deposit premium, mortgage servicing rights, customer relationships and non-compete agreements. The following table presents changes in other intangible assets for the nine months ended September 30, 2008:

	<u>Core Deposit Premium</u>	<u>Mortgage Servicing Rights</u>	<u>Customer Relationships</u>	<u>Non-Compete Agreements</u>	<u>Total</u>
	(Dollars in thousands)				
Balance, beginning of period	\$ 28,750	\$ 11,222	\$ -	\$ -	\$ 39,972
Additions	-	5,534	1,400	300	7,234
Amortization	(2,006)	(1,631)	(35)	(15)	(3,687)
Balance, end of period	<u>\$ 26,744</u>	<u>\$ 15,125</u>	<u>\$ 1,365</u>	<u>\$ 285</u>	<u>\$ 43,519</u>

Income generated as the result of new mortgage servicing rights is reported as gains on sales of loans and totaled \$2.0 million and \$5.5 million for the three and nine months ended September 30, 2008, respectively, compared to \$0.3 million and \$1.0 million for the three and nine months ended September 30, 2007, respectively. The fair value of our mortgage servicing rights was \$17.0 million and \$12.4 million at September 30, 2008 and December 31, 2007, respectively.

The gross carrying value and accumulated amortization related to our intangible assets are presented below:

	<u>September 30, 2008</u>			<u>December 31, 2007</u>		
	<u>Gross Carrying Value</u>	<u>Accumulated Amortization</u>	<u>Net</u>	<u>Gross Carrying Value</u>	<u>Accumulated Amortization</u>	<u>Net</u>
	(Dollars in thousands)					
Core deposit premium	\$ 44,642	\$ (17,898)	\$ 26,744	\$ 44,642	\$ (15,892)	\$ 28,750
Mortgage servicing rights	26,054	(10,929)	15,125	20,520	(9,298)	11,222
Customer relationships	1,400	(35)	1,365	-	-	-
Non-compete agreements	300	(15)	285	-	-	-
	<u>\$ 72,396</u>	<u>\$ (28,877)</u>	<u>\$ 43,519</u>	<u>\$ 65,162</u>	<u>\$ (25,190)</u>	<u>\$ 39,972</u>

Based on the core deposit premium, mortgage servicing rights, customer relationships and non-compete agreements held as of September 30, 2008, estimated amortization expense for the remainder of fiscal 2008, the next five succeeding fiscal years and all years thereafter are as follows:

	Estimated Amortization Expense				
	Core Deposit Premium	Mortgage Servicing Rights	Customer Relationships	Non-Compete Agreements	Total
	(Dollars in thousands)				
2008 (remainder)	\$ 669	\$ 315	\$ 35	\$ 15	\$ 1,034
2009	2,674	1,885	140	60	4,759
2010	2,674	1,684	140	60	4,558
2011	2,674	1,480	140	60	4,354
2012	2,674	1,294	140	60	4,168
2013	2,674	1,130	140	30	3,974
Thereafter	12,705	7,337	630	-	20,672
	<u>\$ 26,744</u>	<u>\$ 15,125</u>	<u>\$ 1,365</u>	<u>\$ 285</u>	<u>\$ 43,519</u>

9. DERIVATIVES

In January 2008, we entered into a derivative transaction to hedge future cash flows from a portion of our then existing variable rate loan portfolio. Effective January 2008 through January 2013, we will receive payments equal to a fixed interest rate of 6.25% from the counterparty on a notional amount of \$400 million. In return, we will pay to the counterparty a floating rate, namely our prime rate, on the same notional amount. The purpose of this derivative transaction is to minimize the risk of fluctuations in interest payments received on our variable rate loan portfolio. The derivative transaction has been designated as a cash flow hedge.

As required by SFAS 133, "Accounting for Derivative Instruments and Hedging Activities," we measure the derivative at fair value on our consolidated balance sheet. At each reporting period, depending on whether the derivative is in an asset or liability position, we record the derivative in other assets or other liabilities. We record the effective portion of the changes in the fair value of the derivative in accumulated other comprehensive income (loss), net of tax, until earnings are affected by the variability of cash flows of the hedged transaction. We immediately recognize the portion of the gain or loss in the fair value of the derivative that represents hedge ineffectiveness in current period earnings.

At September 30, 2008, the derivative was in a net asset position and we recorded the derivative at its fair value of \$0.1 million in other assets. At September 30, 2008, there was no unrealized gain or loss for the effective portion of the change in fair value of the derivative. During the nine months ended September 30, 2008, we recognized a gain related to hedge ineffectiveness of \$0.1 million.

10. SHARE REPURCHASE

In January 2008, the Company's board of directors authorized the repurchase and retirement of up to 1,200,000 shares of the Company's common stock (the "2008 Repurchase Plan"). Repurchases may be made from time to time on the open market or in privately negotiated transactions. During the nine months ended September 30, 2008, we repurchased and retired a total of 100,000 shares of common stock for approximately \$1.8 million. Although, a total of 1,100,000 shares remained authorized for repurchase under the 2008 Repurchase Plan at September 30, 2008, the Company is not currently making any repurchases.

11. SHARE-BASED COMPENSATION

The following table reflects total share-based compensation recognized for the periods indicated:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(Dollars in thousands)			
Salaries and employee benefits	\$ 600	\$ 743	\$ 1,764	\$ 2,920
Income tax benefit	(240)	(298)	(707)	(1,170)
Net share-based compensation effect	\$ 360	\$ 445	\$ 1,057	\$ 1,750

In accordance with SFAS 123R, we are required to base initial share-based compensation expense on the estimated number of awards for which the requisite service and performance is expected to be rendered.

Stock Option Activity

The following is a summary of stock option activity for the Company's stock option plans for the nine months ended September 30, 2008:

	Shares	Weighted Average Exercise Price
Outstanding at January 1, 2008	872,912	\$ 27.90
Changes during the period:		
Granted	95,000	18.75
Exercised	(1,000)	9.24
Expired	(2,564)	26.82
Forfeited	(42,499)	34.81
Outstanding at September 30, 2008	921,849	26.66

We estimate the fair value of stock options granted using the Black-Scholes option pricing formula and a single option award approach. This fair value is then amortized on a straight-line basis over the requisite service periods of the awards, which is generally the vesting period. The fair value of the Company's stock options granted to employees for the three and nine months ended September 30, 2008 and 2007 was estimated using the following weighted-average assumptions:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Expected volatility	-%	30.9%	32.0%	33.1%
Risk free interest rate	-%	4.5%	2.8%	4.5%
Expected dividends	-%	3.6%	5.4%	2.9%
Expected life (in years)	-	6.5	6.5	7.4
Weighted average fair value	\$ -	\$ 7.57	\$ 3.47	\$ 11.20

There were no stock options granted during the three months ended September 30, 2008.

Restricted Stock Awards

The table below presents the activity of restricted stock awards for the nine months ended September 30, 2008:

	<u>Shares</u>	<u>Weighted Average Grant Date Fair Value</u>
Nonvested at January 1, 2008	44,620	\$ 34.87
Changes during the period:		
Forfeited	(2,500)	36.95
Nonvested at September 30, 2008	<u>42,120</u>	34.74

We awarded restricted stock awards to our non-officer directors and certain senior management personnel. The awards typically vest over a three or five year period. Compensation expense is measured as the market price of the stock awards on the grant date, and is recognized over the specified vesting periods.

Performance Shares and Stock Appreciation Rights

In 2005 and 2008, we established Long Term Incentive Plans (the “2005 LTIP” and “2008 LTIP”) that covers certain executive and senior management personnel. Awards granted under the 2005 LTIP are comprised of three components: performance shares, stock appreciation rights (“SARs”) and cash awards, while awards granted under the 2008 LTIP consists of performance shares and SARs. All performance shares and SARs awarded under both the 2005 LTIP and 2008 LTIP are granted from the Company’s 2004 Stock Compensation Plan.

Performance shares granted under the 2005 LTIP vest based on achieving both performance and service conditions. Performance conditions require achievement of stated goals including earnings per share, credit quality and efficiency ratio targets. The service condition required employees to be employed continuously with the Company through March 15, 2008. The fair value of the grant to be recognized over this service period is determined based on the market value of the stock on the grant date, multiplied by the probability of the granted shares being earned. This requires us to assess the expectation over the performance period of the performance targets being achieved as well as to estimate expected pre-vested cancellations.

Performance shares granted under the 2008 LTIP vest based on achieving both market and service conditions. Market conditions require attainment of specified market-based conditions tied to the market value of our common stock. The service condition requires employees to be employed continuously with the Company through March 12, 2011. The fair value of the grant, which is based on the market value of the stock on the grant date, will be recognized as compensation over this service period and must be recognized as expense over the service period regardless of whether the market conditions are met, so long as the grantee meets the service condition.

The table below presents activity of performance shares for both the 2005 LTIP and 2008 LTIP during the nine months ended September 30, 2008:

	<u>Shares</u>	<u>Weighted Average Grant Date Fair Value</u>
Nonvested at January 1, 2008	45,957	\$ 34.74
Changes during the period:		
Granted	97,907	18.88
Vested	(44,670)	34.77
Forfeited	(1,287)	33.86
Nonvested at September 30, 2008	<u>97,907</u>	18.88

SARs granted under the 2005 LTIP require the employee to achieve the same performance conditions as the performance shares described for above for the 2005 LTIP, as well as to satisfy service conditions that approximate three years from the date of grant. Similar to the performance shares under the 2005 LTIP addressed above, the amount of compensation cost to be recognized is the fair value of the SAR grant adjusted based on expectations of achieving the performance requirements and also the expected pre-vested cancellations. Compensation costs arising from the SARs will be recognized ratably over the requisite service period.

SARs granted under the 2008 LTIP require the achievement of the same market and service conditions described above for the 2008 LTIP. Similar to the performance shares awarded under the 2008 LTIP, the fair value of the SARs granted will be recognized as compensation over the service period and must be recognized as expense over the service period regardless of whether the market conditions are met, so long as the grantee meets the service condition.

Upon exercise of SARs under the 2005 LTIP and 2008 LTIP, for each SAR exercised, the grantee shall be entitled to receive value equal to the difference between the market value of a share on the date of exercise minus the market value of a share on the date of grant. We shall pay the value owing to the grantee upon exercise in whole shares. No cash will be awarded upon exercise, and no fractional shares will be issued or delivered.

As the Company's SARs plan is a stock-settled SAR, this plan is an equity-classified award under SFAS 123R. As such, the financial and income tax accounting for this type of award is identical to that of a nonqualified stock option plan. Therefore, the grant date fair value for all SARs issued under the SARs plan is determined at the grant date using the same method as would be used for determining the fair value of a grant of a nonqualified stock option, which has historically been the Black-Scholes formula.

The fair value of SARs granted to employees were estimated using the Black-Scholes option pricing formula with the following weighted-average assumptions:

	Nine Months Ended	
	September 30,	
	2008	2007
Expected volatility	32.0%	31.7%
Risk free interest rate	2.8%	4.5%
Expected dividends	5.3%	2.8%
Expected life (in years)	6.5	6.5
Weighted average fair value	\$ 3.50	\$ 10.49

There were no grants of SARs for the three months ended September 30, 2008 and 2007.

The table below presents activity of SARs under both the 2005 LTIP and 2008 LTIP for the nine months ended September 30, 2008:

	Shares	Weighted Average
		Exercise Price
Outstanding at January 1, 2008	56,549	\$ 35.00
Changes during the period:		
Granted	210,963	18.88
Vested	(21,368)	34.41
Forfeited	(8,166)	35.57
Outstanding at September 30, 2008	<u>237,978</u>	20.74

12. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

Components of accumulated other comprehensive loss, net of taxes, were as follows:

	<u>September 30,</u> <u>2008</u>	<u>December 31,</u> <u>2007</u>
	(Dollars in thousands)	
Unrealized holding losses on available-for-sale investment securities	\$ (10,909)	\$ (401)
Pension adjustments	(9,409)	(9,973)
Tax effect	8,144	4,160
Accumulated other comprehensive loss, net of tax	<u>\$ (12,174)</u>	<u>\$ (6,214)</u>

Components of comprehensive income (loss) for the periods indicated were as follows:

	<u>Three Months Ended</u> <u>September 30,</u>		<u>Nine Months Ended</u> <u>September 30,</u>	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>
	(Dollars in thousands)			
Net income (loss)	\$ 3,041	\$ 9,107	\$ (141,559)	\$ 50,258
Unrealized gain (loss) on investment securities, net of taxes	(3,095)	5,871	(6,297)	2,793
Unrealized gain on derivatives, net of taxes	5,050	-	-	-
Pension adjustments, net of taxes	113	165	337	493
Comprehensive income (loss)	<u>\$ 5,109</u>	<u>\$ 15,143</u>	<u>\$ (147,519)</u>	<u>\$ 53,544</u>

13. PENSION PLANS

Central Pacific Bank, our bank subsidiary, has a defined benefit retirement plan (the "Pension Plan") which covers certain eligible employees. The plan was curtailed effective December 31, 2002, and accordingly, plan benefits were fixed as of that date. The following table sets forth the components of net periodic benefit cost for the Pension Plan:

	<u>Three Months Ended</u> <u>September 30,</u>		<u>Nine Months Ended</u> <u>September 30,</u>	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>
	(Dollars in thousands)			
Interest cost	\$ 451	\$ 446	\$ 1,353	\$ 1,338
Expected return on assets	(574)	(560)	(1,722)	(1,680)
Amortization of unrecognized loss	186	264	558	792
Net periodic cost	<u>\$ 63</u>	<u>\$ 150</u>	<u>\$ 189</u>	<u>\$ 450</u>

Central Pacific Bank also established Supplemental Executive Retirement Plans (“SERPs”), which provide certain officers of Central Pacific Bank with supplemental retirement benefits. The following table sets forth the components of net periodic benefit cost for the SERPs:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(Dollars in thousands)			
Service cost	\$ 75	\$ 140	\$ 225	\$ 420
Interest cost	138	136	414	408
Amortization of unrecognized transition obligation	5	5	15	15
Amortization of prior service cost	5	5	15	15
Amortization of unrecognized (gain) loss	(8)	1	(24)	3
Net periodic cost	<u>\$ 215</u>	<u>\$ 287</u>	<u>\$ 645</u>	<u>\$ 861</u>

14. EARNINGS PER SHARE

The following table presents the information used to compute basic and diluted earnings per share for the periods indicated:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(In thousands, except per share data)			
Net income (loss)	<u>\$ 3,041</u>	<u>\$ 9,107</u>	<u>\$ (141,559)</u>	<u>\$ 50,258</u>
Weighted average shares outstanding - basic	28,665	30,192	28,668	30,480
Dilutive effect of employee stock options and awards	34	186	-	227
Weighted average shares outstanding - diluted	<u>28,699</u>	<u>30,378</u>	<u>28,668</u>	<u>30,707</u>
Basic earnings (loss) per share	<u>\$ 0.11</u>	<u>\$ 0.30</u>	<u>\$ (4.94)</u>	<u>\$ 1.65</u>
Diluted earnings (loss) per share	<u>\$ 0.11</u>	<u>\$ 0.30</u>	<u>\$ (4.94)</u>	<u>\$ 1.64</u>

A total of 909,442 and 1,321,222 potentially dilutive securities have been excluded from the dilutive share calculation for the three and nine months ended September 30, 2008 as their effect was antidilutive, compared to 399,514 and 390,106 for the three and nine months ended September 30, 2007, respectively.

15. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

Effective January 1, 2008, we partially adopted the provisions of SFAS 157. The statement defines fair value, establishes a consistent framework for measuring fair value and expands disclosure requirements for fair value measurements.

Under SFAS 157, we group our financial assets and liabilities at fair value into three levels based on the markets in which the financial assets and liabilities are traded and the reliability of the assumptions used to determine fair value as follows:

- Level 1 – Valuation is based upon quoted prices (unadjusted) for identical assets or liabilities traded in active markets. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available.
- 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 3 – Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect our own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of discounted cash flow models and similar techniques that requires the use of significant judgment or estimation.

Under SFAS 157, we base our fair values on the price that we would expect to receive if an asset were sold or pay to transfer a liability in an orderly transaction between market participants at the measurement date. As required under SFAS 157, we maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements.

We use fair value measurements to record adjustments to certain financial assets and liabilities and to determine fair value disclosures. Available for sale securities and derivatives are recorded at fair value on a recurring basis. From time to time, we may be required to record other financial assets at fair value on a nonrecurring basis such as loans held for sale, impaired loans and mortgage servicing rights. These nonrecurring fair value adjustments typically involve application of the lower of cost or fair value accounting or write-downs of individual assets.

The following table below presents the balances of assets and liabilities measured at fair value on a recurring basis:

	September 30, 2008			
	Level 1	Level 2	Level 3	Total
	(Dollars in thousands)			
Available for sale securities	\$ 925	\$ 763,676	\$ 14,415	\$ 779,016
Net Derivatives	-	226	-	226
Total	\$ 925	\$ 763,902	\$ 14,415	\$ 779,242

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis are summarized as follows:

	September 30, 2008	
	Available For Sale Securities	
	(Dollars in thousands)	
Balance at January 1, 2008	\$	14,821
Principal payments received on mortgage revenue bonds		(406)
Balance at September 30, 2008	\$	14,415

For assets measured at fair value on a nonrecurring basis that were recorded at fair value on our balance sheet at September 30, 2008, the following table provides the level of valuation assumptions used to determine the respective fair values:

	September 30, 2008			
	Level 1	Level 2	Level 3	Total
	(Dollars in thousands)			
Loans held for sale (1)	\$ -	\$ 13,122	\$ -	\$ 13,122
Impaired loans (1)	-	113,431	-	113,431

- (1) Represents carrying value and related write-downs of loans for which adjustments are based on agreed upon purchase prices for the loans or the appraised value of the collateral.

16. SEGMENT INFORMATION

We have three reportable segments: Commercial Real Estate, Hawaii Market and Treasury. The segments reported are consistent with internal functional reporting lines. They are managed separately because each unit has different target markets, technological requirements, marketing strategies and specialized skills. The Commercial Real Estate segment includes construction and real estate development lending in Hawaii, California and Washington. The Hawaii Market segment includes retail branch offices, commercial lending, residential mortgage lending and servicing, indirect auto lending, trust services and retail brokerage services. A full range of deposit and loan products and various other banking services are offered. The Treasury segment is responsible for managing the Company's investment securities portfolio and wholesale funding activities.

The All Others category includes activities such as electronic banking, data processing and management of bank owned properties.

The accounting policies of the segments are consistent with the Company's accounting policies that are described in Note 1 to the consolidated financial statements in the Annual Report on Form 10-K for the year ended December 31, 2007 filed with the Securities and Exchange Commission. The majority of the Company's net income is derived from net interest income. Accordingly, management focuses primarily on net interest income, rather than gross interest income and expense amounts, in evaluating segment profitability.

Intersegment net interest income (expense) was allocated to each segment based upon a funds transfer pricing process that assigns costs of funds to assets and earnings credits to liabilities based on market interest rates that reflect interest rate sensitivity and maturity characteristics. All administrative and overhead expenses are allocated to the segments at cost. Cash, investment securities, loans and their related balances are allocated to the segment responsible for acquisition and maintenance of those assets. Segment assets also include all premises and equipment used directly in segment operations.

Segment profits and assets are provided in the following table for the periods indicated.

	<u>Commercial Real Estate</u>	<u>Hawaii Market</u>	<u>Treasury</u>	<u>All Others</u>	<u>Total</u>
	(Dollars in thousands)				
Three months ended September 30, 2008:					
Net interest income	\$ 30,940	\$ 20,397	\$ (753)	\$ -	\$ 50,584
Intersegment net interest income (expense)	(19,960)	13,295	3,000	3,665	-
Provision for loan losses	(18,600)	(4,300)	-	-	(22,900)
Other operating income	62	9,865	1,699	84	11,710
Other operating expense	(4,223)	(20,020)	(686)	(12,536)	(37,465)
Administrative and overhead expense allocation	(1,313)	(10,707)	(95)	12,115	-
Income taxes	5,711	(3,386)	(1,272)	59	1,112
Net income (loss)	<u>\$ (7,383)</u>	<u>\$ 5,144</u>	<u>\$ 1,893</u>	<u>\$ 3,387</u>	<u>\$ 3,041</u>
Three months ended September 30, 2007:					
Net interest income	\$ 44,853	\$ 12,408	\$ (4,431)	\$ -	\$ 52,830
Intersegment net interest income (expense)	(28,502)	20,418	2,164	5,920	-
Provision for loan losses	(20,270)	(930)	-	-	(21,200)
Other operating income	23	9,036	2,645	48	11,752
Other operating expense	(1,182)	(16,257)	(505)	(13,609)	(31,553)
Administrative and overhead expense allocation	(1,952)	(10,955)	(103)	13,010	-
Income taxes	1,618	(3,157)	53	(1,236)	(2,722)
Net income (loss)	<u>\$ (5,412)</u>	<u>\$ 10,563</u>	<u>\$ (177)</u>	<u>\$ 4,133</u>	<u>\$ 9,107</u>
Nine months ended September 30, 2008:					
Net interest income	\$ 100,010	\$ 57,477	\$ (4,662)	\$ -	\$ 152,825
Intersegment net interest income (expense)	(65,261)	46,277	7,524	11,460	-
Provision for loan losses	(137,500)	(7,472)	-	-	(144,972)
Other operating income	239	31,408	5,913	360	37,920
Goodwill impairment	(94,279)	-	-	-	(94,279)
Other operating expense (excluding goodwill impairment)	(40,619)	(57,681)	(1,960)	(34,669)	(134,929)
Administrative and overhead expense allocation	(1,461)	(30,833)	(289)	32,583	-
Income taxes	56,036	(11,082)	(2,047)	(1,031)	41,876
Net income (loss)	<u>\$ (182,835)</u>	<u>\$ 28,094</u>	<u>\$ 4,479</u>	<u>\$ 8,703</u>	<u>\$ (141,559)</u>
Nine months ended September 30, 2007:					
Net interest income	\$ 132,919	\$ 37,335	\$ (10,854)	\$ -	\$ 159,400
Intersegment net interest income (expense)	(82,872)	59,461	4,297	19,114	-
Provision for loan losses	(20,330)	(4,470)	-	-	(24,800)
Other operating income	104	27,401	6,850	87	34,442
Other operating expense	(4,773)	(50,197)	(1,719)	(36,671)	(93,360)
Administrative and overhead expense allocation	(5,543)	(27,267)	(631)	33,441	-
Income taxes	(7,829)	(13,294)	707	(5,008)	(25,424)
Net income (loss)	<u>\$ 11,676</u>	<u>\$ 28,969</u>	<u>\$ (1,350)</u>	<u>\$ 10,963</u>	<u>\$ 50,258</u>
At September 30, 2008:					
Investment securities	\$ -	\$ -	\$ 802,984	\$ -	\$ 802,984
Loans and leases (including loans held for sale)	2,117,104	1,999,632	-	-	4,116,736
Other	(58,330)	207,894	250,750	184,270	584,584
Total assets	<u>\$ 2,058,774</u>	<u>\$ 2,207,526</u>	<u>\$ 1,053,734</u>	<u>\$ 184,270</u>	<u>\$ 5,504,304</u>
At December 31, 2007:					
Investment securities	\$ -	\$ -	\$ 881,254	\$ -	\$ 881,254
Loans and leases (including loans held for sale)	2,228,739	1,950,538	-	-	4,179,277
Other	31,891	208,135	244,453	135,376	619,855
Total assets	<u>\$ 2,260,630</u>	<u>\$ 2,158,673</u>	<u>\$ 1,125,707</u>	<u>\$ 135,376</u>	<u>\$ 5,680,386</u>

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

Overview

Central Pacific Financial Corp. ("CPF") is a Hawaii corporation and a bank holding company. Our principal business is to serve as a holding company for our bank subsidiary, Central Pacific Bank. We refer to Central Pacific Bank herein as "our Bank" or "the Bank," and when we say "the Company," "we," "us" or "our," we mean the holding company on a consolidated basis with the Bank and our other consolidated subsidiaries.

Central Pacific Bank is a full-service community bank with 39 branches and more than 95 ATMs located throughout the State of Hawaii. The Bank offers a broad range of products and services including accepting time and demand deposits and originating loans, including commercial loans, construction loans, commercial and residential mortgage loans, and consumer loans. The Bank also has four loan production offices serving customers in California.

On July 31, 2008, we announced that our Board of Directors elected Mr. Ronald K. Migita to succeed Mr. Clint Arnoldus as President and Chief Executive Officer of CPF and the Bank, effective August 1, 2008. Mr. Migita has been Chairman of the Board of Directors of CPF and the Bank since September 2004 and will continue to serve in those roles. Prior to joining the Company, Mr. Migita served as the President and Chief Executive Officer of CB Bancshares, Inc. ("CBBI"), which merged with CPF in 2004. CBBI's principal subsidiary, City Bank, merged with the Bank in 2005. Mr. Migita's four decades of banking experience includes an extensive background in corporate and retail banking.

Critical Accounting Policies

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires that management make certain judgments and use certain estimates and assumptions that affect amounts reported and disclosures made. Accounting estimates are deemed critical when a different estimate could have reasonably been used or where changes in the estimate are reasonably likely to occur from period to period and would materially impact our consolidated financial statements as of or for the periods presented. Management has discussed the development and selection of the critical accounting estimates noted below with the Audit Committee of the Board of Directors, and the Audit Committee has reviewed the accompanying disclosures.

Allowance for Loan and Lease Losses

We maintain an allowance for loan and lease losses (the "Allowance") at an amount we expect to be sufficient to absorb probable losses inherent in our loan and lease portfolio based on a projection of probable net loan charge-offs. For loans classified as impaired, which includes nonaccrual loans, an estimated impairment loss is calculated. To estimate loan charge-offs on other loans, we evaluate the level and trend of nonperforming and potential problem loans and historical loss experience. We also consider other relevant economic conditions and borrower-specific risk characteristics, including current repayment patterns of our borrowers, the fair value of collateral securing specific loans, changes in our lending and underwriting standards and general economic factors, nationally and in the markets we serve, including the real estate market generally and the residential construction market. Estimated loss rates are determined by loan category and risk profile, and an overall required Allowance is calculated. Based on our estimate of the level of Allowance required, a provision for loan and lease losses (the "Provision") is recorded to maintain the Allowance at an appropriate level. During the first nine months of 2008, we increased certain loan loss factors assigned to portions of our portfolio in light of the current economic environment and overall uncertainty in the credit markets.

Since we cannot predict with certainty the amount of loan and lease charge-offs that will be incurred, and because the eventual level of loan and lease charge-offs are impacted by numerous conditions beyond our control, a range of loss estimates could reasonably have been used to determine the Allowance and Provision. In addition, various regulatory agencies, as an integral part of their examination processes, periodically review our Allowance. This may result in additions to the Allowance based on their judgments about information available to them at the time of their examination. Accordingly, actual results could differ from those estimates.

Loans Held for Sale

Loans held for sale consists of Hawaii residential mortgage loans, as well as mainland residential and commercial construction loans. Hawaii residential mortgage loans classified as held for sale are carried at the lower of cost or fair value on an aggregate basis while mainland residential and commercial construction loans are recorded at the lower of cost or fair value on an individual basis.

Loans originated with the intent to be held in our portfolio are subsequently transferred to held for sale when a decision is made to sell these loans. At the time of a loan's transfer to the held for sale account, the loan is recorded at the lower of cost or fair value. Any reduction in the loan's value is reflected as a write-down of the recorded investment resulting in a new cost basis, with a corresponding reduction in the Allowance.

In subsequent periods, if the fair value of a loan classified as held for sale is less than its cost basis, a valuation adjustment is recognized in our consolidated statement of operations in other operating expense and the carrying value of the loan is adjusted accordingly. The valuation adjustment may be recovered in the event that the fair value increases, which is also recognized in our consolidated statement of operations in other operating expense.

The fair value of loans classified as held for sale are generally based upon quoted prices for similar assets in active markets, acceptance of firm offer letters with agreed upon purchase prices, discounted cash flow models that take into account market observable assumptions, or independent appraisals of the underlying collateral securing the loans.

Goodwill and Other Intangible Assets

In accordance with Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"), we review the carrying amount of goodwill for impairment on an annual basis. Additionally, we perform an impairment assessment of goodwill and other intangible assets whenever events or changes in circumstances indicate that the carrying value of goodwill and other intangible assets may not be recoverable. Significant changes in circumstances can be both internal to our strategic and financial direction, as well as changes to the competitive and economic landscape.

Our impairment assessment of goodwill and other intangible assets involves the estimation of future cash flows and the fair value of reporting units to which goodwill is allocated. Estimating future cash flows and determining fair values of the reporting units is only an estimate and often involves the use of significant assumptions. These estimates and assumptions could have a significant impact on whether or not an impairment charge is recognized and also the magnitude of the impairment charge.

During the second quarter of 2008, we determined that an impairment test was required under SFAS 142 as the negative effects of the continued deterioration in the California residential construction market contributed to a decrease in our market capitalization. As a result of our impairment test, we concluded that the remaining goodwill associated with our Commercial Real Estate reporting segment, which includes the California residential construction loan portfolio, was impaired and we recorded a non-cash charge of \$94.3 million in the second quarter of 2008. Following this impairment charge, our remaining goodwill balance was \$150.5 million, all of which was attributable to our Hawaii Market reporting segment. At September 30, 2008, we performed an impairment assessment and concluded that our remaining goodwill was not impaired.

Deferred Tax Assets and Tax Contingencies

We account for income taxes in accordance with SFAS 109, "Accounting for Income Taxes" and FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes."

Deferred tax assets and liabilities are recognized for the estimated future tax effects attributable to temporary differences and carryforwards. A valuation allowance may be required if, based on the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized. In determining whether a valuation allowance is necessary, we consider the level of taxable income in prior years, to the extent that carrybacks are permitted under current tax laws, as well as estimates of future taxable income and tax planning strategies that could be implemented to accelerate taxable income if necessary. If our estimates of future taxable income were materially overstated, or if our assumptions regarding the tax consequences of tax planning strategies were inaccurate, some or all of our deferred tax assets may not be realized, which would result in a charge to earnings.

We have established income tax contingencies reserves for potential tax liabilities related to uncertain tax positions. Tax benefits are recognized when we determine that it is more likely than not that such benefits will be realized. Where uncertainty exists due to the complexity of income tax statutes, and where the potential tax amounts are significant, we generally seek independent tax opinions to support our positions. If our evaluation of the likelihood of the realization of benefits is inaccurate, we could incur additional income tax and interest expense that would adversely impact earnings, or we could receive tax benefits greater than anticipated which would positively impact earnings.

Defined Benefit Retirement Plan

Defined benefit plan obligations and related assets of our defined benefit retirement plan are presented in Note 14 to the Consolidated Financial Statements for the year ended December 31, 2007 included in the Company's Annual Report on Form 10-K. In 2002, the defined benefit retirement plan was curtailed and all plan benefits were fixed as of that date. Plan assets, which consist primarily of marketable equity and debt securities, are typically valued using market quotations. Plan obligations and the annual pension expense are determined by independent actuaries through the use of a number of assumptions. Key assumptions in measuring the plan obligations include the discount rate and the expected long-term rate of return on plan assets. In determining the discount rate, we utilize a yield that reflects the top 50% of the universe of bonds, ranked in the order of the highest yield. Asset returns are based upon the anticipated average rate of earnings expected on the invested funds of the plans. At December 31, 2007, we used a weighted-average discount rate of 6.5% and an expected long-term rate of return on plan assets of 8.0%, which affected the amount of pension liability recorded as of year-end 2007 and the amount of pension expense to be recorded in 2008. For both the discount rate and the asset return rate, a range of estimates could reasonably have been used which would affect the amount of pension expense and pension liability recorded. A 0.25% change in the discount rate assumption would impact 2008 pension expense by \$0.1 million and year-end 2007 pension liability by \$0.7 million, while a 0.25% change in the asset return rate would impact 2008 pension expense by \$0.1 million. We believe our assumption of future asset return rates is reasonable given past experience. We will continue to assess such assumptions in the future, particularly in light of the recent volatility in the financial markets. A decrease in our expected long-term rate of return on plan assets may result in future contributions to the pension plan and an increase in future pension expense.

Financial Summary

During the third quarter of 2008, we returned to profitability with net income of \$3.0 million, or \$0.11 per diluted share, compared to a net loss of \$146.3 million, or \$5.10 per diluted share, in the second quarter of 2008. Quarterly results for the three months ended September 30, 2008 included an improvement in credit costs, which decreased from \$116.1 million in the second quarter of 2008 to \$23.0 million in the third quarter of 2008. The decrease in credit costs reflects our strategy of reducing our exposure to the California residential construction market, which has decreased to \$95.4 million at September 30, 2008 from \$310.6 million at 2007 year-end. Net income for the third quarter of 2007 was \$9.1 million, or \$0.30 per diluted share.

Despite our return to profitability in the third quarter of 2008, deterioration in the California residential construction market and related declines in collateral values significantly impacted our operating results for the first nine months of 2008. Although not to the extent seen in the California residential construction market, our operations have also been negatively impacted by the lingering weakness in the overall credit markets, downturns in the local and national economies, and signs of weakness in a few of our California commercial construction and Hawaii residential construction borrowers. During the nine months ended September 30, 2008, we recognized a net loss of \$141.6 million, or \$4.94 per diluted share, compared to net income of \$50.3 million, or \$1.64 per diluted share, in the comparable prior year period. Our results for the first nine months of 2008 were reflective of the challenging economic environment that we, along with many other financial institutions across the country, continue to experience. Despite the turmoil and uncertainty in the financial markets, we remain committed to investing in our core Hawaii franchise and strengthening our asset quality.

The following table presents annualized returns on average assets, average shareholders' equity, average tangible equity and basic and diluted earnings per share for the periods indicated. Average tangible equity is calculated as average shareholders' equity less average intangible assets, which includes goodwill and core deposit premium. Average intangible assets were \$178.8 million and \$240.9 million for the three and nine months ended September 30, 2008, respectively, and \$322.3 million and \$324.3 million for the three and nine months ended September 30, 2007, respectively.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Return (loss) on average assets	0.22%	0.65%	(3.30) %	1.22%
Return (loss) on average shareholders' equity	2.36%	4.80%	(30.07) %	8.84%
Return (loss) on average tangible equity	3.61%	8.35%	(48.81) %	15.45%
Basic earnings (loss) per share	\$ 0.11	\$ 0.30	\$ (4.94)	\$ 1.65
Diluted earnings (loss) per share	\$ 0.11	\$ 0.30	\$ (4.94)	\$ 1.64

Material Trends

The global and U.S. economies are currently experiencing a slowdown in business activity as a result of disruptions in the financial system, including the recent freeze in the worldwide credit markets. Declines in the housing market during the past year, along with falling home prices and increasing foreclosures and unemployment, have resulted in significant write-downs of asset values. These write-downs have caused many financial institutions to seek additional capital, to merge with larger and stronger institutions and, in some cases, to fail. As a result of the current uncertainties regarding the stability of the financial markets, many financial institutions have reduced and/or ceased to provide funding to borrowers, including other financial institutions. Accordingly, the availability of credit, confidence in the financial sector, and level of volatility in the financial markets have been adversely affected and have contributed to the recent volatility and disruption in the capital and credit markets which have reached unprecedented levels.

In response to the financial crises affecting the banking system and financial markets, the Emergency Economic Stabilization Act of 2008 (the "EESA") was signed into law on October 3, 2008. Under the EESA, the U.S. Department of the Treasury (the "Treasury") will have the authority to purchase up to \$700 billion of mortgages, mortgage-backed securities and certain other financial instruments from financial institutions for the purpose of stabilizing and providing liquidity to the U.S. financial markets. On October 14, 2008, the Treasury announced that it will purchase equity stakes in a wide variety of banks and thrifts under a program known as the Troubled Asset Relief Program's ("TARP") Capital Purchase Program (the "CPP"). Under the CPP, the Treasury will make \$250 billion (a third of the amount authorized by the EESA) of capital available to U.S. financial institutions in the form of preferred stock. In conjunction with the purchase of preferred stock, the Treasury will receive warrants to purchase common stock with an aggregate market price equal to 15% of the preferred investment. Participating financial institutions will also be required to adopt the Treasury's standards for executive compensation and corporate governance for the period during which the Treasury holds equity issued under the CPP. We have submitted an application to participate in the TARP's CPP, however, there can be no assurance that we will be selected to participate.

Prior to the financial crises and actions taken by the government to stabilize the credit markets, Hawaii's economy was expected to remain flat in 2008 as the continued effects of several airline failures, the surge in fuel prices and the loss of a cruise ship have taken an effect on Hawaii's tourism industry. Visitor arrivals were expected to decrease 6.7%, visitor days were expected to decline 6.4% and average daily spending was expected to decrease 6.4% from the previous year. Hawaii economists predicted small net declines in both real income and jobs for the remainder of 2008, with real personal income expected to increase 0.4% in 2008, following a 1.5% increase in 2007. The state's unemployment rate was 4.5% in September 2008, which remained below the national unemployment rate of 6.1%, but has increased from 3.2% at December 31, 2007. In September 2008, the number of single-family home resales on Oahu decreased by 25.8% from a year ago, while the median sales price decreased by 3.5%. Despite the anticipated slowdown in home resales, the Hawaii housing market was expected to experience lower levels of price declines compared to the national housing market. Hawaii economists also predicted that a significant recovery of the Hawaii economy may not begin until 2010. These economic projections may be optimistic given the recent deterioration in the global financial markets and macroeconomic environment.

Prior to the financial crises and the actions taken by the government to stabilize the credit markets, California's economy continued to face pressure caused by falling home prices, tight credit conditions, dysfunctional financial markets and soaring food and energy prices. Job growth in 2008 was expected to decrease by 0.2% from 2007 levels, while California real personal income was expected to increase 4.5% in 2008, compared to 5.9% in 2007 and 6.5% in 2006. California's unemployment rate has increased to 7.7% in September 2008 from 5.9% in December 2007, further validating a weakening in the economy. The residential real estate market in California continues to be affected by the current downturn and ongoing effects of the credit crisis. In September 2008, the number of single-family home resales in California increased 96.7%, while the median sales price decreased 40.9% from a year ago. The significant increase in sales activity and significant decline in the median price from the past year are largely due to a dramatic shift in the sales mix since the onset of the credit crisis and the increase in the share of distressed sales in 2008. This trend of higher sales activity with declining median prices was expected to continue for the remainder of 2008 and parts of 2009 as increases in distressed sales activities were anticipated. Sales in 2008 were previously forecasted to be ahead of last year by 12.0%, while the median price was expected to fall by 31.7% percent. These economic projections may be optimistic given the recent deterioration in the global financial markets and macroeconomic environment.

It is not clear at this time what impact the EESA, TARP Program, other liquidity and funding initiatives of the Federal Reserve and other agencies that have been previously announced, and any additional programs that may be initiated in the future will have on the financial markets, the U.S. banking and financial industries, the broader U.S. and global economies, and more importantly, the local economies in the markets that we serve. As we have seen in the past year with the deteriorating market conditions of the California residential and commercial construction market, our results of operations in future periods may be significantly impacted by the economies in Hawaii, California or other markets we serve. Loan demand, deposit growth, provision for loan and lease losses, asset quality, noninterest income and noninterest expense may be affected by changes in economic conditions. If the California and Hawaii residential real estate markets do not improve or continue to deteriorate, the California commercial real estate market worsens, or the economic environments in Hawaii, California or other markets we serve suffer an adverse change or a material external shock, our results of operations may be negatively impacted.

Results of Operations

Net Interest Income

Net interest income, when expressed as a percentage of average interest earning assets, is referred to as “net interest margin.” Interest income, which includes loan fees and resultant yield information, is expressed on a taxable equivalent basis using an assumed income tax rate of 35%. A comparison of net interest income on a taxable equivalent basis (“net interest income”) for the three and nine months ended September 30, 2008 and 2007 is set forth below.

	Three Months Ended September 30, 2008			Three Months Ended September 30, 2007		
	Average Balance	Average Yield/Rate	Amount of Interest	Average Balance	Average Yield/Rate	Amount of Interest
(Dollars in thousands)						
Assets						
Interest earning assets:						
Interest-bearing deposits in other banks	\$ 946	1.59%	\$ 4	\$ 6,362	5.14%	\$ 82
Federal funds sold & securities purchased under agreements to resell	6,799	1.94	33	9,761	5.10	125
Taxable investment securities (1)	690,643	5.04	8,703	726,971	4.66	8,469
Tax-exempt investment securities (1)	143,943	5.77	2,078	152,714	5.41	2,066
Loans and leases, net of unearned income (2)	4,134,700	6.19	64,224	4,025,552	7.73	78,325
Federal Home Loan Bank stock	48,797	1.40	171	48,797	0.60	73
Total interest earning assets	5,025,828	5.96	75,213	4,970,157	7.13	89,140
Nonearning assets	527,877			604,942		
Total assets	\$ 5,553,705			\$ 5,575,099		
Liabilities and Shareholders' Equity						
Interest-bearing liabilities:						
Interest-bearing demand deposits	\$ 469,966	0.21%	\$ 251	\$ 437,150	0.13%	\$ 139
Savings and money market deposits	1,085,721	1.16	3,171	1,216,407	2.06	6,321
Time deposits under \$100,000	669,914	2.70	4,544	621,215	3.91	6,127
Time deposits \$100,000 and over	988,691	2.57	6,388	1,018,347	4.60	11,798
Short-term borrowings	262,865	2.39	1,583	22,279	5.39	302
Long-term debt	882,017	3.59	7,965	816,761	5.29	10,900
Total interest-bearing liabilities	4,359,174	2.18	23,902	4,132,159	3.42	35,587
Noninterest-bearing deposits	592,505			599,995		
Other liabilities	86,293			84,128		
Shareholders' equity	515,733			758,817		
Total liabilities and shareholders' equity	\$ 5,553,705			\$ 5,575,099		
Net interest income			\$ 51,311			\$ 53,553
Net interest margin		4.07%			4.29%	

	Nine Months Ended September 30, 2008			Nine Months Ended September 30, 2007		
	Average Balance	Average Yield/Rate	Amount of Interest	Average Balance	Average Yield/Rate	Amount of Interest
(Dollars in thousands)						
Assets						
Interest earning assets:						
Interest-bearing deposits in other banks	\$ 714	1.99%	\$ 11	\$ 4,063	5.14%	\$ 156
Federal funds sold & securities purchased under agreements to resell	4,617	2.21	76	6,304	5.18	244
Taxable investment securities (1)	713,360	5.11	27,317	734,260	4.75	26,140
Tax-exempt investment securities (1)	149,000	5.72	6,393	153,973	5.42	6,263
Loans and leases, net of unearned income (2)	4,242,621	6.30	200,195	3,970,276	7.79	231,561
Federal Home Loan Bank stock	48,797	1.27	464	48,797	0.53	195
Total interest earning assets	5,159,109	6.07	234,456	4,917,673	7.19	264,559
Nonearning assets	566,330			593,007		
Total assets	\$ 5,725,439			\$ 5,510,680		

Liabilities and Shareholders' Equity

Interest-bearing liabilities:

Interest-bearing demand deposits	\$ 464,374	0.16%	\$ 567	\$ 437,345	0.13%	\$ 418
Savings and money market deposits	1,112,667	1.19	9,936	1,218,547	2.06	18,773
Time deposits under \$100,000	597,990	2.94	13,151	629,146	3.85	18,114
Time deposits \$100,000 and over	1,049,155	3.08	24,216	966,326	4.58	33,068
Short-term borrowings	287,181	2.73	5,863	27,037	5.49	1,110
Long-term debt	899,855	3.81	25,661	797,665	5.28	31,484
Total interest-bearing liabilities	4,411,222	2.40	79,394	4,076,066	3.38	102,967
Noninterest-bearing deposits	599,684			589,518		
Other liabilities	86,936			87,179		
Shareholders' equity	627,597			757,917		
Total liabilities and shareholders' equity	\$ 5,725,439			\$ 5,510,680		

Net interest income			\$ 155,062			\$ 161,592
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Net interest margin		4.01%			4.39%	
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(1) At amortized cost.

(2) Includes nonaccrual loans.

Net interest income of \$51.3 million for the third quarter of 2008, decreased by \$2.2 million, or 4.2%, from the third quarter of 2007, while net interest income for the first nine months of 2008 decreased by \$6.5 million, or 4.0%, to \$155.1 million from the comparable prior year period. The decrease in net interest income for the third quarter and first nine months of 2008 was primarily the result of interest reversals related to loans being placed on non-accrual status (\$0.4 million and \$4.0 million for the three and nine months ended September 30, 2008, respectively) and a decrease in average loan yields as certain variable rate loans repriced downward in connection with the Federal Reserve's actions to decrease interest rates. Net interest income was positively impacted by a decrease in interest expense as average rates on interest-bearing liabilities have decreased also as a result of the Federal Reserve's actions.

Interest Income

Taxable-equivalent interest income of \$75.2 million for the third quarter of 2008, decreased by \$13.9 million, or 15.6%, from the third quarter of 2007, while taxable-equivalent interest income of \$234.5 million for the first nine months of 2008, decreased by \$30.1 million, or 11.4%, from the comparable prior year period. The current quarter decrease in taxable-equivalent interest income was attributable to the aforementioned decrease in average loan yields, which declined to 6.19% for the third quarter of 2008 from 7.73% in the comparable prior year period. The decrease in average loan yields, including the effects of the previously mentioned interest reversals of \$0.4 million on certain nonaccrual loans, contributed to approximately \$15.5 million of the current quarter decrease in taxable-equivalent interest income. Partially offsetting this decrease was the \$109.1 million, or 2.7%, increase in average loans and leases (net of write-downs, charge offs and transfers to held for sale) in the third quarter of 2008 over the comparable prior year period. This increase in loans and leases resulted in a \$2.1 million increase in taxable-equivalent interest income for the third quarter of 2008 when compared to the comparable prior year period. The increase in average loans and leases for the current quarter was primarily driven by an increase in residential mortgage originations as Central Pacific HomeLoans, our residential mortgage subsidiary, was able to capitalize on the establishment of strategic alliances with real estate brokers and developers to provide additional origination opportunities in Hawaii.

The year-to-date decrease in taxable-equivalent interest income was attributable to the aforementioned reversal of \$4.0 million of interest income on certain nonaccrual loans during the nine months ended September 30, 2008 and also the decrease in average loan yields. The decrease in the average loan yields, including the effects of the reversal of interest mentioned above, contributed to approximately \$44.4 million of the year-to-date decrease in taxable-equivalent interest income from the comparable prior year period, while the volume increase in average loan balances resulted in an increase in taxable-equivalent interest income of \$15.9 million over the comparable prior year period.

Interest Expense

Interest expense of \$23.9 million for the third quarter of 2008, decreased by \$11.7 million, or 32.8%, from the comparable quarter one year ago, while interest expense of \$79.4 million for the first nine months of 2008, decreased by \$23.6 million, or 22.9%, from the comparable prior year period. The decrease in interest expense for the third quarter and first nine months of 2008 was primarily attributable to the decrease in average rates paid on average interest-bearing liabilities.

The weighted average rates paid on interest bearing deposits decreased by 116 basis points (“bp”) during the current quarter when compared to the third quarter of 2007. This decrease contributed to approximately \$9.6 million of the reduction in interest expense during the current quarter when compared to the third quarter of 2007. The 170 bp decrease in average rates paid on long-term debt resulted in a reduction in interest expense of approximately \$3.5 million for the same period. Offsetting these decreases was the increase in average short-term borrowings, which rose by \$240.6 million during the current quarter from the third quarter of 2007. This increase resulted in an increase in taxable-equivalent interest expense of \$3.2 million when compared to the third quarter of 2007. Short-term borrowings at September 30, 2008, consisted primarily of Federal Home Loan Bank advances of \$275.0 million, which carried a weighted average interest rate of 2.4%. During the nine months ended September 30, 2008, the maximum amount of Federal Home Loan Bank advances was \$472.0 million in May 2008.

For the first nine months of 2008, the 91 bp decrease in the weighted average rates paid on all interest bearing deposits contributed to \$22.3 million of the year-to-date reduction in interest expense from the comparable prior year period, while the 147 bp decrease in average rates paid on long term debt contributed to \$8.8 million of the year-to-date reduction. Increases in average short-term borrowings of \$260.1 million and average long-term debt of \$102.2 million during the first nine months of 2008 resulted in an increase in interest expense of \$10.7 million and \$4.0 million, respectively, for the first nine months of 2008 when compared to the first nine months of 2007.

Net Interest Margin

Our net interest margin was 4.07% for the third quarter of 2008 compared to 4.29% for the third quarter of 2007, while our net interest margin for the first nine months of fiscal 2008 was 4.01% compared to 4.39% for the comparable prior year period. The compression in our net interest margin for the three and nine months ended September 30, 2008 was primarily attributable to the previously mentioned interest reversals of \$0.4 million and \$4.0 million, during the respective periods. Additionally, average yields earned on interest earning assets have declined faster during the nine months ended September 30, 2008 than the average rates paid on interest-bearing liabilities as the rate of downward repricing of interest-bearing liabilities has been tempered by the continued strong competition for deposits in the Hawaii market. Our increased reliance on short-term borrowings to compensate for net decreases in our deposit balances further contributed to the compression in our net interest margin when compared to the previous fiscal periods.

Nonperforming Assets, Accruing Loans Delinquent for 90 Days or More, Restructured Loans Still Accruing Interest

The following table sets forth nonperforming assets, accruing loans delinquent for 90 days or more and restructured loans still accruing interest at the dates indicated.

(Dollars in thousands)	<u>September 30, 2008</u>	<u>December 31, 2007</u>
<u>Nonperforming Assets</u>		
Nonaccrual loans (including loans held for sale):		
Commercial, financial and agricultural	\$ 1,762	\$ 231
Real estate:		
Construction	108,290	61,017
Mortgage-residential	5,427	-
Mortgage-commercial	5,485	293
Total non accrual loans	<u>120,964</u>	<u>61,541</u>
Other real estate	11,590	-
Total nonperforming assets	<u>132,554</u>	<u>61,541</u>
<u>Accruing loans delinquent for 90 days or more:</u>		
Commercial, financial and agricultural	-	18
Real estate:		
Mortgage-residential	358	586
Consumer	282	299
Total accruing loans delinquent for 90 days or more	<u>640</u>	<u>903</u>
<u>Restructured loans still accruing interest:</u>		
Total restructured loans still accruing interest	<u>-</u>	<u>-</u>
Total nonperforming assets, accruing loans delinquent for 90 days or more and restructured loans still accruing interest	<u>\$ 133,194</u>	<u>\$ 62,444</u>
Total nonperforming assets as a percentage of loans and leases, loans held for sale and other real estate	3.21%	1.47%
Total nonperforming assets and accruing loans delinquent for 90 days or more as a percentage of loans and leases, loans held for sale and other real estate	3.23%	1.49%
Total nonperforming assets, accruing loans delinquent for 90 days or more and restructured loans still accruing interest as a percentage of loans and leases, loans held for sale and other real estate	3.23%	1.49%

Nonperforming assets, which includes nonaccrual loans and leases, nonperforming loans classified as held for sale and foreclosed real estate, totaled \$132.6 million at September 30, 2008, compared to \$61.5 million at fiscal 2007 year-end and \$145.9 million at June 30, 2008. Nonperforming assets at September 30, 2008 were comprised of \$107.9 million in nonaccrual loans, \$13.1 million in nonperforming loans classified as held for sale and \$11.6 million in other real estate.

The increase in nonperforming assets during the first nine months of 2008 was primarily attributable to the troubled California residential construction market, as \$194.2 million of California residential construction loans were placed on nonaccrual status during the first nine months of 2008, of which, \$13.1 million were classified as held for sale at September 30, 2008. In addition, \$51.7 million of California commercial real estate and construction loans, \$21.4 million in Hawaii residential construction loans, \$5.5 million of Hawaii commercial mortgage loans and \$5.1 million of Hawaii residential mortgage loans were also placed on nonaccrual status during the nine months ended September 30, 2008.

Offsetting the increase in nonperforming assets were charge-offs of California residential construction loans totaling \$118.6 million and California commercial real estate and construction loans totaling \$5.8 million, write-downs of California residential construction loans classified as held for sale of \$22.5 million and California other real estate owned of \$6.5 million, as well as \$48.7 million in California residential construction loan sales during the first nine months of 2008.

The decrease in our nonperforming assets from June 30, 2008 was attributable to the aforementioned sale of assets totaling \$44.2 million, a partial charge-off of one California residential construction loan totaling \$6.8 million and a full charge-off of one California residential construction loan totaling \$0.7 million. Partially offsetting this decrease was the addition of eight California commercial real estate and construction loans to three borrowers totaling \$29.0 million, two California residential construction loans to the same borrower totaling \$2.1 million, three Hawaii commercial construction loans to two borrowers totaling \$5.4 million, and one Hawaii commercial real estate loan totaling \$1.4 million.

Included in non-performing assets at September 30, 2008 were three residential mortgage loans, one residential construction loan and one commercial real estate loan to two Hawaii borrowers which were restructured. The principal balance and accrued interest of these restructured loans were \$10.7 million and \$0.2 million, respectively, and were matured and/or in default at the time of restructure. In exchange for a payoff amount of \$10.9 million and additional collateral of \$3.1 million, we granted the borrowers a forbearance period until January 31, 2009 and agreed to waive all late fees and attorneys' fees and costs, as well as accrued interest from August 1, 2008 to the payoff date. We have no commitments to lend additional funds to these borrowers.

Allowance and Provision for Loan and Lease Losses

A discussion of our accounting policy regarding the Allowance and Provision is contained in the Critical Accounting Policies section of this report. The following table sets forth certain information with respect to the Allowance as of the dates and for the periods indicated:

(Dollars in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Allowance for loan and lease losses:				
Balance at beginning of period	\$ 86,050	\$ 51,409	\$ 92,049	\$ 52,280
Provision for loan and lease losses	22,900	21,200	144,972	24,800
Charge-offs:				
Commercial, financial and agricultural	662	14	981	3,573
Real estate:				
Construction	7,500	-	134,546	-
Mortgage-residential	-	-	-	358
Consumer	867	821	2,550	2,582
Leases	112	-	131	-
Total charge-offs	9,141	835	138,208	6,513
Recoveries:				
Commercial, financial and agricultural	77	260	214	319
Real estate:				
Construction	-	-	-	7
Mortgage-residential	37	15	98	210
Mortgage-commercial	2	3	8	9
Consumer	302	465	1,094	1,403
Leases	-	-	-	2
Total recoveries	418	743	1,414	1,950
Net charge-offs	8,723	92	136,794	4,563
Balance at end of period	\$ 100,227	\$ 72,517	\$ 100,227	\$ 72,517
Annualized ratio of net charge-offs to average loans	0.84%	0.01%	4.30%	0.15%

Our Allowance at September 30, 2008 totaled \$100.2 million, an increase of \$8.2 million, or 8.9%, from year-end 2007. When expressed as a percentage of total loans, our Allowance was 2.46% at September 30, 2008 compared to 2.22% at year-end 2007. The increase in our Allowance was a direct result of the \$145.0 million Provision recognized during the nine months ended September 30, 2008, partially offset by \$136.8 million in net loan charge-offs during the period, concentrated primarily on loans with direct exposure to the California residential construction market. Net loan charge-offs for the first nine months of the year included charge-offs for loans transferred to held for sale of \$79.5 million. Given the uncertainty in the current economic environment, the increase in our Allowance was deemed appropriate in response to nonaccrual loans (excluding loans held for sale) and reflects the reduced value of the collateral supporting our impaired loans with exposure to the California residential construction market as well as increased credit risk in other parts of our loan portfolio. In accordance with generally accepted accounting principles in the United States, loans held for sale and other real estate assets are not included in our assessment of the Allowance.

The increase in total nonaccrual and impaired loans, combined with reduced collateral values and increases in our loan loss factors, have contributed to the increased Provision recognized during the nine months ended September 30, 2008. Collateral values are determined based on appraisals received from qualified valuation professionals and are obtained periodically or when indicators that property values may be impaired are present. Risk volatility in our loan portfolio has been increasing, resulting in higher risk rating adjustment activity in recent quarters. Over the past year, rapid risk rating migration has occurred within our mainland residential tract development portfolio and began to spill over into portions of our mainland commercial construction portfolio and a few of our Hawaii residential construction borrowers beginning in the first half of 2008. Recent events within the financial markets, retrenching consumer confidence, rising inflation and slow to negative job growth, have resulted in heightened risk within our various commercial and commercial real estate loan portfolios.

California Residential Construction Market Exposure

As previously noted, our credit risk position worsened during the nine month period ended September 30, 2008 as issues facing California residential real estate developers, including declining home prices, lower absorption rates and increased inventory, continue to adversely impact our mainland loan portfolio resulting in significant write-downs and higher credit costs. Additional information regarding our exposure to this sector follows:

(Dollars in thousands)	<u>September 30, 2008</u>	<u>June 30, 2008</u>	<u>December 31, 2007</u>
Total exposure - California residential construction market:			
Loan portfolio	\$ 76,724	\$ 87,187	\$ 305,230
Loans held for sale	13,122	53,182	5,400
Other real estate	5,590	-	-
Total	<u>\$ 95,436</u>	<u>\$ 140,369</u>	<u>\$ 310,630</u>
Percentage of California residential construction loan portfolio to total loans	1.9%	2.1%	7.4%
Non performing assets - California residential construction market:			
Nonaccrual loans	\$ 32,837	\$ 41,200	\$ 52,334
Nonaccrual loans held for sale	13,122	53,182	5,400
Other real estate	5,590	3,501	-
	<u>\$ 51,549</u>	<u>\$ 97,883</u>	<u>\$ 57,734</u>
Total nonperforming assets with exposure to the California residential construction market assets as a percentage of total assets	0.9%	1.7%	1.0%

We engaged the services of seasoned real estate professionals to assist us in assessing and managing our risk exposure to this troubled market. As a result of these efforts and given the uncertainties in the outlook for this market, we initiated loan sale proceedings on several California residential construction loans during the first nine months of 2008 and continue to pursue a variety of options to reduce our credit risk exposure to this market. In July 2008, we completed the bulk sale of certain non-performing assets with a combined carrying value of \$44.2 million at June 30, 2008. No gain or loss was recorded on the sale in July as these assets were written down to their sales price during the second quarter of 2008.

Other Operating Income

Total other operating income of \$11.7 million for the third quarter of 2008 decreased slightly from the comparable quarter one year ago. During the three months ended September 30, 2008, income from bank-owned life insurance decreased to \$0.9 million from \$1.9 million in the third quarter of 2007, primarily due to death benefits received in the prior year. Offsetting the decrease in income from bank-owned life insurance was a \$0.7 million increase in net gain on sales of residential loans. The increase in net gain on sales of residential loans was reflective of increased residential mortgage originations and sales during the third quarter of 2008 in comparison to the comparable prior year period as our residential mortgage subsidiary, Central Pacific HomeLoans, capitalized on the establishment of strategic alliances with real estate brokers and developers to provide additional origination opportunities.

For the first nine months of 2008, total other operating income of \$37.9 million increased by \$3.5 million, or 10.1%, over the comparable prior year period. The improvement was primarily due to increases in net gains on sales of residential loans of \$2.0 million, miscellaneous operating income of \$1.0 million and other service charges and fees of \$0.6 million. The increase in miscellaneous operating income was attributable to the mandatory partial redemption of our shares in Visa, Inc. during the first quarter of 2008 resulting in a gain of \$0.9 million.

Other Operating Expense

Total other operating expense for the third quarter of 2008 was \$37.5 million, up \$5.9 million, or 18.7%, from the comparable quarter one year ago. The increase from the year-ago quarter was primarily attributable to increases in salaries and employee benefits expense of \$1.3 million, legal and professional services expense of \$1.0 million and other miscellaneous expense of \$1.9 million. The increase in salaries and employee benefits in the third quarter of 2008 was primarily attributable to the payment of higher commissions resulting from the previously mentioned increase in residential mortgage originations, and the recognition of certain executive retirement and severance compensation accruals. The current quarter increase in legal and professional services expense was related to consultative costs associated with the maintenance of our mainland assets, while the increase in other miscellaneous expense included higher deposit insurance costs.

For the first nine months of 2008, total other operating expense of \$229.2 million increased by \$135.8 million, or 145.5%, over the comparable prior year period. The increase from the comparable prior year period was primarily attributable to a non-cash goodwill impairment charge of \$94.3 million, the write-downs of certain loans held for sale totaling \$22.5 million, the write-downs of foreclosed property totaling \$6.7 million and the recognition of \$1.9 million in losses related to the sale of mainland commercial real estate loans. The non-cash goodwill impairment charge was due to the continued deterioration in the California residential construction market and the resultant decline in our market capitalization and asset values with exposure to this sector. The impairment charge had no impact on our cash flows, tangible equity or regulatory capital. Following the impairment charge, all remaining goodwill at September 30, 2008 is attributable to our Hawaii operations. As discussed above, the increase in total other operating expense from the comparable prior year period was also attributable to the \$4.0 million increase in salaries and employee benefits due to the payment of higher commissions and the accrual of certain executive retirement and severance compensation, higher legal and professional services expense and higher deposit insurance costs.

Income Taxes

In the third quarter and first nine months of 2008, the Company recognized income tax benefits of \$1.1 million and \$41.9 million on pre-tax income of \$1.9 million and a pre-tax loss of \$183.4 million, respectively. In the comparable prior year periods, the Company recorded income tax expenses of \$2.7 million and \$25.4 million on pre-tax income of \$11.8 million and \$75.7 million, respectively. The Company's effective tax rate for the third quarter and first nine months of 2008 were impacted by the disproportionate recognition of federal and state tax credits and the generation of tax-exempt income. The effective rate for the first nine months of 2008 was also impacted by the recognition of the non-cash goodwill impairment charge, which is not deductible for tax purposes.

The Company earns a tax benefit from tax credits and tax exempt income irrespective of the level of pre-tax income. This results in a favorable impact to the total tax benefit and the effective tax rate especially during periods in which the Company is near break-even or experiencing a pre-tax loss. The effective tax rate for the third quarter and first nine months of 2008 (excluding the impact of the non-cash goodwill impairment charge of \$94.3 million recognized in the second quarter of 2008) was -57.9% and 47.0%, respectively, which differs from the expected tax rate of approximately 35.0% due to the recognition of the tax benefits from tax credits of \$1.8 million and \$5.4 million and tax exempt income of \$2.4 million and \$8.3 million for the third quarter and first nine months of 2008, respectively.

Factors that may affect the effective tax rate for the remainder of 2008 include the level of tax-exempt income recognized, the amount of nondeductible expenses incurred and the amount of federal and state tax credits available to offset future taxable income.

Financial Condition

Total assets of \$5.5 billion at September 30, 2008, decreased by \$176.1 million, or 3.1%, from year-end 2007.

Loans and leases, net of unearned income, of \$4.1 billion at September 30, 2008, decreased by \$61.4 million from year-end 2007. The decrease was primarily attributable to charge-offs totaling \$138.2 million; the reclassification of \$92.0 million of California residential construction loans, \$60.5 million of Hawaii residential mortgage loans, and \$14.8 million of Washington commercial real estate loans from the held to maturity loan portfolio to loans held for sale; and the securitization of \$36.5 million of Hawaii residential mortgages, in each case during the nine months ended September 30, 2008. The reclassification of the California residential construction loans to the held for sale portfolio and completed loan sales reflects our continued effort to reduce our exposure to this sector, while the reclassification of the Hawaii residential mortgage loans and Washington commercial real estate loans were done for asset/liability management purposes. After considering the effects of these charge-offs and reclassifications, our Hawaii loan portfolio grew by approximately \$147.9 million, primarily driven by increases in construction and residential mortgage loans, while our mainland loan portfolio decreased by \$209.3 million. Our Hawaii loan portfolio, while not unaffected by current market conditions, has not experienced the challenging market conditions faced in California and continues to perform within our expected credit parameters.

During 2008, we have experienced fluctuations in the amount of total deposits from quarter to quarter. During the first quarter of 2008, total deposits decreased approximately 5.6% from the balance at December 31, 2007. During the second quarter, total deposits increased approximately 3.7% over the balance at March 31, 2008. During the third quarter total deposits decreased approximately 3.7% over the balance at June 30, 2008. At September 30, 2008 total deposits of \$3.8 billion had a net decrease of \$225.6 million, or 5.6%, from year-end 2007. Interest-bearing deposits at September 30, 2008 decreased by \$157.5 million, or 4.7%, while noninterest-bearing deposits decreased by \$68.1 million, or 10.2%, from year-end 2007. The recent decrease in our deposits is consistent with other financial institutions in Hawaii and is partly related to the softening of the local economy. Specifically, the net decrease was primarily attributable to declines in sales volumes within the Hawaii real estate market, which have impacted deposits from our title and escrow customers, a decrease in deposit balances from some of our foreign customers due to concerns about the overall United States economy, customer reaction to the nationwide financial crisis and the resulting uncertainty, and to eroding customer confidence in financial institutions. While we cannot predict when the financial markets will stabilize or when economic conditions will improve, we believe some of the recent changes to the Federal Deposit Insurance Corporation (the "FDIC") deposit insurance limits and other government initiatives may help reassure our customers and mitigate concerns affecting all financial institutions during these challenging economic times.

Capital Resources

Shareholders' equity was \$510.1 million at September 30, 2008, compared to \$674.4 million at year-end 2007. Book value per share at September 30, 2008 was \$17.75, compared to \$23.45 at year-end 2007.

On July 30, 2008, the Company's board of directors declared a third quarter cash dividend of \$0.10 per share, a decrease of 60% from the \$0.25 per share dividend declared in the third quarter of 2007. For the first nine months of 2008, dividends declared totaled \$0.60 per share, a decrease of 17.8% from the \$0.73 per share declared in the first nine months of 2007. Our ability to pay dividends with respect to common stock is subject to obtaining approval from the Federal Reserve.

In January 2008, the Company's board of directors authorized the repurchase and retirement of up to 1,200,000 shares of the Company's common stock (the "2008 Repurchase Plan"). Under the 2008 Repurchase Plan, repurchases may be made from time to time on the open market or in privately negotiated transactions. There were no repurchases of common stock during the three months ended September 30, 2008. During the nine months ended September 30, 2008, we repurchased and retired a total of 100,000 shares of common stock for approximately \$1.8 million under the 2008 Repurchase Plan. Although a total of 1,100,000 shares remained authorized for repurchase under the 2008 Repurchase Plan at September 30, 2008, the Company is not currently making any repurchases.

We have five statutory trusts: CPB Capital Trust I, CPB Capital Trust II, CPB Statutory Trust III, CPB Capital Trust IV and CPB Statutory Trust V, which issued a total of \$105.0 million in trust preferred securities. Our obligations with respect to the issuance of the Securities constitute a full and unconditional guarantee by the Company of the Trust's obligations with respect to the Securities. Subject to certain exceptions and limitations, we may elect from time to time to defer subordinated debenture interest payments, which could result in a deferral of distribution payments on the related Securities. Our ability to pay dividends on these statutory trusts is subject to approval by the Federal Reserve and there is no assurance that such approval can be obtained. The Federal Reserve has determined that certain cumulative preferred securities having the characteristics of the Securities qualify as minority interest, and are included in Tier 1 capital for bank holding companies.

In January 2004, in accordance with FASB Interpretation No. 46(R) (as amended), our statutory trusts were deconsolidated from our financial statements. This resulted in the removal of the trust preferred securities from the long-term debt category of our balance sheets and the addition of our subordinated debentures.

Regulations on capital adequacy guidelines adopted by the Federal Reserve Board and the FDIC are as follows. An institution is required to maintain a minimum ratio of qualifying total capital to risk-adjusted assets of 8% and a minimum ratio of Tier 1 capital to risk-adjusted assets of 4%. In addition to the risk-based guidelines, federal banking regulators require banking organizations to maintain a minimum amount of Tier 1 capital to total assets, referred to as the leverage ratio. For a banking organization to be rated in the highest of the five categories used by regulators to rate banking organizations, the minimum leverage ratio of Tier 1 capital to total assets must be 3%. In addition to these uniform risk-based capital guidelines and leverage ratios that apply across the industry, the regulators have the discretion to set individual minimum capital requirements for specific institutions at rates significantly above the minimum guidelines and ratios.

Management and the Company's board of directors continue to closely evaluate our capital levels. Given the uncertainty in the economy and capital markets, we will continue to evaluate our capital levels and requirements and consider ways to increase our capital if appropriate, including through further asset reductions or the possibility of raising additional capital independently or by participating in the TARP's CPP. There can be no assurance that we will be able to independently raise additional capital on terms favorable to us or that we will be selected to participate in the TARP's CPP.

The following table sets forth the Company's capital ratios and capital adequacy requirements applicable as of the dates indicated. In addition, FDIC-insured institutions such as our principal banking subsidiary, Central Pacific Bank, must maintain leverage, Tier 1 and total risk-based capital ratios of at least 5%, 6% and 10%, respectively, to be considered "well capitalized" under the prompt corrective action provisions of the FDIC Improvement Act of 1991.

(Dollars in thousands)	Actual		Minimum Required for Capital Adequacy Purposes		Minimum Required to be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Company						
At September 30, 2008:						
Leverage capital	\$ 465,131	8.7%	\$ 214,936	4.0%	\$ 268,670	5.0%
Tier 1 risk-based capital	465,131	10.1	183,707	4.0	275,561	6.0
Total risk-based capital	523,117	11.4	367,413	8.0	459,266	10.0
At December 31, 2007:						
Leverage capital	\$ 535,670	9.8%	\$ 218,477	4.0%	\$ 273,096	5.0%
Tier 1 risk-based capital	535,670	11.5	187,049	4.0	280,574	6.0
Total risk-based capital	594,620	12.7	374,098	8.0	467,623	10.0
Central Pacific Bank						
At September 30, 2008:						
Leverage capital	\$ 443,977	8.3%	\$ 215,004	4.0%	\$ 268,755	5.0%
Tier 1 risk-based capital	443,977	9.7	183,236	4.0	274,854	6.0
Total risk-based capital	501,817	11.0	366,472	8.0	458,090	10.0
At December 31, 2007:						
Leverage capital	\$ 518,923	9.5%	\$ 218,143	4.0%	\$ 272,679	5.0%
Tier 1 risk-based capital	518,923	11.1	186,743	4.0	280,115	6.0
Total risk-based capital	577,779	12.4	373,487	8.0	466,859	10.0

Although our capital ratios at September 30, 2008 were lower than 2007 year-end, they have improved from the second quarter of 2008.

Liquidity

Our objective in managing liquidity is to maintain a balance between sources and uses of funds in order to economically meet the cash requirements of customers for loans and deposit withdrawals and participate in lending and investment opportunities as they arise. We monitor our liquidity position in relation to changes in loan and deposit balances on a daily basis to assure maximum utilization, maintenance of an adequate level of readily marketable assets and access to short-term funding sources.

Core deposits have historically provided us with a sizeable source of relatively stable and low cost of funds. In addition to core deposit funding, we also access a variety of other short-term and long-term funding sources, which include proceeds from maturities of our investment securities, as well as secondary funding sources, such as the Federal Home Loan Bank of Seattle (“FHLB”) and the Federal Reserve discount window. The Bank is a member of and maintained a \$1.3 billion line of credit with the FHLB as of September 30, 2008. Short-term and long-term borrowings under this arrangement totaled \$275.0 million and \$747.4 million, respectively, at September 30, 2008, compared to no short-term borrowings and \$781.5 million of long-term borrowings at 2007 year-end. Approximately \$272.7 million remained available for future borrowings at September 30, 2008. The FHLB has the right to suspend future advances. Proceeds from common stock offerings may also provide another source of funds as it has done in the past. Management does not rely on any one source of liquidity and manages availability in response to changing balance sheet needs.

Our liquidity may be affected by an inability to access the capital markets or by unforeseen demands on cash. Over the past year, sources of credit in the capital markets have tightened as mortgage loan delinquencies increased, demand for mortgage loans in the secondary market decreased, securities and debt ratings were downgraded and a number of institutions defaulted on their debt. The market disruptions that started in 2007 have continued in 2008 making it significantly more difficult for financial institutions to obtain capital/funds by selling loans in the secondary market or through borrowings.

We cannot predict with any degree of certainty how long these market conditions may continue, nor can we anticipate the degree of impact such market conditions will have on loan origination volumes and gains or losses on sale results. Deterioration in the performance of other financial institutions, including write-downs of securities, debt-rating downgrades and defaults, have resulted in industry-wide reductions in liquidity and further deterioration in the financial markets may affect our liquidity position.

Contractual Obligations

Information regarding our contractual obligations is provided in Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of our Annual Report on Form 10-K for the year ended December 31, 2007. There have been no material changes in our contractual obligations since December 31, 2007.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Market risk is the risk of loss in a financial instrument arising from adverse changes in market rates/prices such as interest rates, foreign currency rates, commodity prices and equity prices. Our primary market risk exposure is interest rate risk that occurs when rate-sensitive assets and rate-sensitive liabilities mature or reprice during different periods or in differing amounts. Asset/liability management attempts to coordinate our rate-sensitive assets and rate-sensitive liabilities to meet our financial objectives. The Asset/Liability Committee (“ALCO”) monitors interest rate risk through the use of interest rate sensitivity gap, net interest income and market value of portfolio equity simulation, and rate shock analyses. Adverse interest rate risk exposures are managed through the shortening or lengthening of the duration of assets and liabilities.

The primary analytical tool we use to measure and manage our interest rate risk is a simulation model that projects changes in net interest income (“NII”) as market interest rates change. Our ALCO policy requires that simulated changes in NII should be within certain specified ranges, or steps must be taken to reduce interest rate risk. The results of the model indicate that the mix of rate-sensitive assets and liabilities at September 30, 2008 would not result in a fluctuation of NII that would exceed the established policy limits.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report and pursuant to Rule 13a-15 of the Securities Exchange Act of 1934, as amended, (the "Exchange Act"), the Company's management, including the Chief Executive Officer and Principal Financial and Accounting Officer, conducted an evaluation of the effectiveness and design of the Company's disclosure controls and procedures (as that term is defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act). Based upon that evaluation, the Company's Chief Executive Officer and Principal Financial and Accounting Officer concluded, as of the end of the period covered by this report, that the Company's disclosure controls and procedures were effective in recording, processing, summarizing and reporting information required to be disclosed by the Company, within the time periods specified in the Securities and Exchange Commission's rules and forms.

Changes in Internal Controls

As of the end of the period covered by this report, there have been no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) of the Exchange Act) during the quarter to which this report relates that have materially affected or is reasonably likely to materially affect, the internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are involved from time to time in various claims, disputes and other legal actions in the ordinary course of business. We believe that the resolution of such additional matters will not have an adverse material effect upon our financial position or results of operations when resolved.

Item 1A. Risk Factors

The following risk factors have been updated from the risk factors previously disclosed in our Annual Report on Form 10-K for the period ended December 31, 2007, filed with the SEC.

Our ability to maintain adequate sources of funding and liquidity and required capital levels may be negatively impacted by the current economic environment which may, among other things, impact our ability to pay dividends.

Liquidity is essential to our business. An inability to raise funds through deposits, borrowings, the sale of investments or loans, and other sources could have a substantial negative affect on our liquidity. Our access to funding sources in amounts adequate to finance our activities on terms which are acceptable to us could be impaired by factors that affect us specifically or the financial services industry or economy in general. Factors that could detrimentally impact our access to liquidity sources include a decrease in the level of our business activity as a result of a downturn in the markets in which our loans or deposits are concentrated or adverse regulatory action against us. Our ability to borrow could also be impaired by factors that are not specific to us, such as a disruption in the financial markets or negative views and expectations about the prospects for the financial industry in light of the recent turmoil faced by banking organizations and the continued deterioration in credit markets.

The management of liquidity risk is critical to the management of our business and to our ability to service our customer base. In managing our balance sheet, our primary source of funding is customer deposits. Our ability to continue to attract these deposits and other funding sources is subject to variability based upon a number of factors including volume and volatility in the securities markets, our credit rating and the relative interest rates that we are prepared to pay for these liabilities. The availability and level of deposits and other funding sources is highly dependent upon the perception of the liquidity and creditworthiness of the financial institution, which perception can change quickly in response to market conditions or circumstances unique to a particular company. Concerns about our financial condition, or concerns about our credit exposure to other persons could adversely impact our sources of liquidity, financial position, including regulatory capital ratios, results of operations and our business prospects.

During 2008, the amount of our total deposits has fluctuated. If the level of deposits were to materially decrease, we would have to raise additional funds by increasing the interest that we pay on certificates of deposits or other depository accounts, seek other debt or equity financing or draw upon our available lines of credit. Our ability to grow may be impacted because of our inability to fund loan growth. We are monitoring our activities with respect to liquidity and evaluating closely our utilization of our cash assets, however, there can be no assurance that our liquidity or the cost of funds to us may not be materially and adversely impacted as a result of economic, market or operational considerations that we may not be able to control.

We are required to maintain certain capital levels in accordance with banking regulations. Our bank may be subject to a number of enforcement restrictions by the federal regulatory authorities. These may include limitations on the ability to pay dividends, including dividends on our trust preferred securities, the issuance by the regulatory authority of a capital directive to increase capital, and the termination of deposit insurance by the FDIC, as well as other possible enforcement actions.

Our capital ratios have declined in 2008. Because our capital levels have declined and may continue to decline, we may need to increase our capital base by further reducing our assets or by raising additional capital independently or by participating in the TARP's CPP. Our ability to reduce our assets or raise additional capital will depend, in part, on market conditions that are outside of our control. Accordingly, we cannot be certain of our ability to increase our capital base.

Our allowance for loan and lease losses may not be sufficient to cover actual loan losses, which could adversely affect our results of operations. Additional loan losses will likely occur in the future and may occur at a rate greater than we have experienced to date.

As a lender, we are exposed to the risk that our loan customers may not repay their loans according to their terms and that the collateral or guarantees securing these loans may be insufficient to assure repayment. During the first nine months of 2008, our provision for loan and lease losses amounted to \$145.0 million, compared to \$24.8 million for the comparable prior year period, and our current allowance may not be sufficient to cover future loan losses. We may experience significant loan losses that could have a material adverse effect on our operating results. Management makes various assumptions and judgments about the collectibility of our loan portfolio, which are regularly reevaluated and are based in part on:

- Current economic conditions and their estimated effects on specific borrowers;
- An evaluation of the existing relationships among loans, potential loan losses and the present level of the allowance for loan and lease losses;
- Results of examinations of our loan portfolios by regulatory agencies; and
- Management's internal review of the loan portfolio.

In determining the size of the allowance, we rely on an analysis of our loan portfolio, our experience and our evaluation of general economic conditions. If our assumptions prove to be incorrect, our current allowance may not be sufficient. We have made significant adjustments to our allowance this year and additional adjustments may continue to be necessary if the local or national real estate markets and economies continue to deteriorate. Material additions to the allowance would materially decrease our net income. In addition, federal regulators periodically evaluate the adequacy of our allowance and may require us to increase our provision for loan and lease losses or recognize further loan charge-offs based on judgments different than those of our management. Any further increase in our allowance or loan charge-offs could have a material adverse effect on our results of operations.

During the second quarter of 2008, we wrote off all of the remaining goodwill associated with our Commercial Real Estate reporting segment as it was considered to be impaired. We continue to evaluate goodwill assigned to our Hawaii Market reporting segment for impairment. Estimates of fair value of our Hawaii Market reporting segment are determined based on a complex model using cash flows and company comparisons. If management's estimates of future cash flows are inaccurate, the fair value determined could be inaccurate and impairment may not be recognized in a timely manner.

Recent market disruptions and related governmental actions could materially and adversely affect our business, financial condition, results of operations or prospects.

Our business is affected by global economic conditions, political uncertainties and volatility and other developments in the financial markets. Factors such as interest rates and commodity prices, regional and national rates of economic growth, liquidity and volatility of fixed income, credit and other financial markets and investors' confidence can significantly affect the businesses in which we and our customers are engaged. Such factors have affected, and may further unfavorably affect, both economic growth and stability in markets where we and our customers operate, creating adverse effects on many companies, including us, in ways that are not predictable or that we may fail to anticipate. Since mid-2007 credit and other financial markets have suffered substantial stress, volatility, illiquidity and disruption. These forces reached unprecedented levels in September and October 2008, resulting in the bankruptcy or acquisition of, or government assistance to several major domestic and international financial institutions. These events have significantly diminished overall confidence in the financial markets and in financial institutions, generally. This reduced confidence could further exacerbate the overall market disruption and increase risks to market participants including the Company.

The recent market developments and the potential for increased and continuing disruptions present a material risk to our business and that of other financial institutions. Subsequent to September 30, 2008 market conditions continue to worsen. Further deterioration or a continuation of recent market conditions may lead to a decline in the value of the assets that we hold or in the creditworthiness of our borrowers. In response to recent market disruptions, legislators and financial regulators implemented a number of mechanisms designed to add stability to the financial markets, including the provision of direct and indirect assistance to distressed financial institutions, assistance by the banking authorities in arranging acquisitions of weakened banks and broker dealers, implementation of programs by the Federal Reserve to provide liquidity to the commercial paper markets and other matters. On October 3, 2008 the Emergency Economic Stabilization Act of 2008 was signed into law by the President empowering the Secretary of the Treasury to purchase from financial institutions up to \$700 billion of troubled assets. On October 14, 2008 the U.S. Secretary of the Treasury announced the TARP CPP, a program in which we have applied to participate. The overall effects of these and other legislative and regulatory efforts on the financial markets are uncertain, and they may not have the intended stabilization effects. While these measures have been taken to support the markets, these actions may have unintended consequences on the financial system or our business, including reducing competition or increasing the general level of uncertainty in the markets. Should these or other legislative or regulatory initiatives fail to stabilize and add liquidity to the financial markets, our business, financial condition, results of operations and prospects could be adversely affected.

Even if these efforts essentially stabilize and add liquidity to the financial markets, we may need to modify our strategy or operations and we may incur increased capital requirements and constraints or additional costs in order to satisfy regulatory requirements or to compete in a changed business environment. Given the volatile nature of the current market disruption and the uncertainties underlying efforts to mitigate or reverse the disruption, we may not timely anticipate or manage these risks, contingencies or developments. Our failure to do so could materially and adversely affect our business, financial condition, results of operations or prospects.

Item 2. Unregistered Sales of Equity and Use of Proceeds

None.

Item 3. Defaults upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

None.

Item 5. Other Information

None.

Item 6. Exhibits

<u>Exhibit No.</u>	<u>Document</u>
4.1	Rights Agreement dated as of August 26, 1998 between Registrant and the Rights Agent (1)
10.1	Advances, Security and Deposit Agreement with Federal Home Loan Bank Seattle Dated June 23, 2004 *
31.1	Rule 13a-14(a) Certification of Chief Executive Officer in accordance with Section 302 of the Sarbanes-Oxley Act of 2002 *
31.2	Rule 13a-14(a) Certification of Chief Financial Officer in accordance with Section 302 of the Sarbanes-Oxley Act of 2002 *
32.1	Section 1350 Certification of Chief Executive Officer in accordance with Section 906 of the Sarbanes-Oxley Act of 2002 **
32.2	Section 1350 Certification of Chief Financial Officer in accordance with Section 906 of the Sarbanes-Oxley Act of 2002 **

* Filed herewith.

** Furnished herewith.

(1) Incorporated by reference from Exhibit 4.1 to the Registrant's Current Report on Form 8-K, filed with the Securities and Exchange Commission on August 26, 2008.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CENTRAL PACIFIC FINANCIAL CORP.
(Registrant)

Date: November 7, 2008

/s/ Ronald K. Migita
Ronald K. Migita
Chairman, President & Chief Executive Officer

Date: November 7, 2008

/s/ Dean K. Hirata
Dean K. Hirata
Vice Chairman and Chief Financial Officer

Central Pacific Financial Corp.
Exhibit Index

<u>Exhibit No.</u>	<u>Description</u>
10.1	Advances, Security and Deposit Agreement with Federal Home Loan Bank Seattle Dated June 23, 2004
31.1	Certification of the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of the Principal Financial and Accounting Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of the Principal Financial and Accounting Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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Section 2: EX-10.1 (EXHIBIT 10.1)

Exhibit 10.1



1501 Fourth Ave., Ste. 1900, Seattle, WA 98101-1693 206.340.2300 tel 206.340.2485 fax www.fhlbsea.com

Advances, Security and Deposit Agreement

This Advances, Security and Deposit Agreement (“Agreement”), dated as of June 23, 2004 (Date of Agreement) is entered between Central Pacific Bank (Full Corporate Name of Customer) having its principal place of business at 220 South King Street Honolulu, HI 96813 (Full Address of Customer's Executive Offices) (“Customer”) and the Federal Home Loan Bank of Seattle, 1501 Fourth Avenue, Suite 1900, Seattle, WA 98101 (“Seattle Bank”).

RECITALS

Whereas, Customer is a Member of Seattle Bank and desires from time to time to apply for extensions of credit, deposit accounts and other services from Seattle Bank in accordance with the terms and conditions of this Agreement; and

Whereas, Seattle Bank requires that all existing and future indebtedness of Customer to Seattle Bank be secured pursuant to this Agreement.

AGREEMENT

NOW THEREFORE, Customer and Seattle Bank agree as follows:

Article 1. Definitions

Section 1.1 Definitions As used in this Agreement, the following terms will have the following meanings:

- 1.1.1 “Account” or “Accounts” means Customer’s deposit account(s) with Seattle Bank, including demand and time deposit accounts.
- 1.1.2 “Act” means the Federal Home Loan Bank Act, as amended from time to time.
- 1.1.3 “Advance” or “Advances” means any loans heretofore, now or hereafter made to Customer by Seattle Bank.
- 1.1.4 “Advance Master Application” means a writing executed by Customer and accepted by Seattle Bank, in form and content satisfactory to Seattle Bank, under which Customer may make Requests from time to time to receive Advances, subject to the terms of this Agreement, the Seattle Bank’s Credit Policy, the Act and the Regulations.
- 1.1.5 “Advances Note” means any promissory note executed by Customer and accepted by Seattle Bank, in form and content satisfactory to Seattle Bank, relating to Advances or Other Credit Accommodations.
- 1.1.6 “Advance Confirmation Advice” means a writing or an electronic transmission issued at any time by Seattle Bank, in form and content satisfactory to Seattle Bank, confirming particular terms of an Advance made at the Request of Customer.

- 1.1.7 “Borrowing Capacity” means the maximum amount of Advances, Commitments and Other Credit Accommodations which Borrower may have outstanding at any time. Borrowing Capacity is limited by the Act and Regulations, the Stock Ownership Requirement and Collateral Maintenance Requirement of the Credit Policy, and by Customer’s creditworthiness and the quality of Customer’s Eligible Collateral, as determined by Seattle Bank from time to time.
- 1.1.8 “Capital Plan” means the Capital Plan of the Federal Home Loan Bank of Seattle, adopted March 5, 2002, as amended November 22, 2002 and as hereafter amended.
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- 1.1.9 “Capital Stock” means all of Customer’s capital stock in Seattle Bank.
- 1.1.10 “Collateral” means all property, including the proceeds thereof, heretofore, now or hereafter assigned, transferred or pledged to Seattle Bank by Customer as security for Indebtedness.
- 1.1.11 “Collateral Coverage Factor” means the percentage of value, as determined by Seattle Bank from time to time, of various types of Eligible Collateral which will support the aggregate amount of all outstanding Advances, Commitments or Other Credit Accommodations made to Customer against such Eligible Collateral.
- 1.1.12 “Collateral Manual” means the Collateral Manual of the Seattle Bank, as published and revised by the Seattle Bank from time to time.
- 1.1.13 “Collateral Maintenance Requirement” means the minimum level of aggregate Eligible Collateral, discounted by applicable Collateral Coverage Factors, which Customer must pledge to Seattle Bank, and maintain at or above such minimum level, to secure Customer’s outstanding Advances, Commitments or Other Credit Accommodations, as determined by Seattle Bank from time to time.
- 1.1.14 “Commitment” means any written agreement under which Seattle Bank is contractually obligated to make Advances to Customer, or payments on behalf of or for the account of Customer, at a future date, irrespective of whether Seattle Bank’s obligation under such agreement is contingent upon the occurrence or non-occurrence of a condition subsequent. Commitments include, without limitation, Letters of Credit, firm commitments, guarantees or other financial arrangements made by Seattle Bank in writing to facilitate transactions between Customer and third parties. This Agreement is neither a Commitment nor an undertaking or obligation to provide any Commitment.
- 1.1.15 “Credit Policy” means the credit and collateral policies of Seattle Bank, including without limitation the credit and collateral policies set forth in the Users Guide and the Collateral Manual, as published and revised by the Seattle Bank from time to time. In addition to the Users Guide and Collateral Manual, the Credit Policy includes other policies adopted from time to time by Seattle Bank. The Credit Policy is subject to the Act and Regulations, and in the event of any inconsistency between the Credit Policy and the Act or Regulations, the more restrictive statute, regulation or policy shall be controlling.
- 1.1.16 “De-Pledge” means the partial release, re-assignment and/or re-delivery by Seattle Bank or its approved custodian of any part of the Collateral pledged to Seattle Bank for Indebtedness.
- 1.1.17 “Eligible Collateral” means Collateral other than Capital Stock which: (i) qualifies as security for Advances or Other Credit Accommodations under the Act and Regulations; (ii) qualifies as security for Advances or Other Credit Accommodations under the Credit Policy, as amended by Seattle Bank from time to time, which may be more restrictive than the Act or Regulations; (iii) is owned by Customer free and clear of any liens, encumbrances or other interests, other than the pledge of such Collateral to Seattle Bank under this Agreement; and (iv) is not a home mortgage on which any director, officer, employee, attorney or agent of Customer or any federal home loan bank is personally liable, unless acceptance of such mortgage is specifically approved by formal resolution of the Seattle Bank’s board of directors, and the Finance Board has endorses such resolution.
- 1.1.18 “Eligible CFI Collateral” means, if Customer is a community financial institution as defined in the Regulations, certain small agri-business loans, small farm loans or small business loans which meet the requirements of Eligible Collateral described in Subsection 1.1.17 above.
- 1.1.19 “Eligible Securities Collateral” means securities, now owned or hereafter acquired by Customer, whether certificated or uncertificated, which meets the requirements of Eligible Collateral described in Subsection 1.1.17 above.
- 1.1.20 “Eligible Mortgage Collateral” means Mortgage Collateral which meets the requirements of Eligible Collateral described in Subsection 1.1.17 above.
- 1.1.21 “Finance Board” means the Federal Housing Finance Board, or any successor agency thereto.
- 1.1.22 “Funds” means money maintained in Customer’s Account(s) with Seattle Bank.
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- 1.1.23 “Indebtedness” means all obligations of Customer to Seattle Bank, defined in the broadest and most comprehensive sense, to mean all primary, secondary, direct, indirect, fixed or contingent, debts, duties, agreements, undertakings, obligations, covenants and conditions now or at any time in the future to be paid or performed by Customer in connection with or relating to Advances, Other Credit Accommodations, Commitments, Accounts of Other Obligations, including, without limitation, all of Customer’s obligations to pay principal, interest, fees (including, without limitation, loan fees and prepayment fees), charges (including, without limitation, overdraft charges), costs, reimbursements (including, without limitation, attorneys fees) and losses (including, without limitation, damages for Customer’s breach of any contractual obligations to Seattle Bank), which at any time may be owing under or in connection therewith.
- 1.1.24 “Letter of Credit” means any standby letter of credit issued by Seattle Bank for the account of Customer.
- 1.1.25 “Listed Collateral” is defined in Section 3.4 below.
- 1.1.26 “Master Backup Support Agreement” means any agreement now or hereafter made by Seattle Bank and one or more other federal home loan bank(s) under which such other federal home loan bank(s) may make Advances or Other Credit Accommodations to Customer in the event of a loss of power, communications or computer failure, property damage or other forms of business interruption adversely affecting Seattle Bank’s normal operations.
- 1.1.27 “Member” means an owner of Capital Stock in Seattle Bank.
- 1.1.28 “Member Advance Stock Purchase Requirement” is described in Section 6.10 of this Agreement and in the Capital Plan.
- 1.1.29 “MERS” means Mortgage Electronic Registration Systems, Inc., a corporation organized and existing under the laws of the State of Delaware, or any successor thereto.
- 1.1.30 “MERS Mortgages” means mortgages registered with MERS, in which the Mortgage Documents name MERS as mortgagee, solely as nominee, for the originators of such mortgages and their successors and assigns.
- 1.1.31 “Mortgage Collateral” means Mortgage Documents (excluding participation or other fractional interests therein) and all ancillary security agreements, policies and certificates of insurance, guarantees, indemnities, evidences of recordation, applications, underwriting materials, surveys, appraisals, notices, opinions of counsel and loan servicing data and all other electronically stored and written records or materials relating to the loans evidenced or secured by the Mortgage Documents.
- 1.1.32 “Mortgage Documents” means mortgages and deeds of trust (in this Agreement, “mortgages”) and all notes, bonds or other instruments evidencing loans secured thereby (in this Agreement, “mortgage notes”) and any endorsements and assignments thereof to Customer.
- 1.1.33 “Mortgage Purchase Program” means any program offered by Seattle Bank for the purchase from a Member of mortgage notes and related mortgages.
- 1.1.34 “Other Credit Accommodations” means credit products, other than Advances, authorized under the terms and conditions of the Act and Regulations and offered from time to time by Seattle Bank under its Credit Policy, including, without limitation, Swap Transactions, Letters of Credit and other Commitments.
- 1.1.35 “Other Eligible Collateral” means property, other than Eligible Mortgage Collateral or Eligible Securities Collateral, which meets the requirements of Eligible Collateral described in Subsection 1.1.17 above, including, if Customer is a community financial institution as defined in the Regulations, any Eligible CFI Collateral.
- 1.1.36 “Other Obligations” means obligations of Customer to Seattle Bank other than those relating to Advances or Other Credit Accommodations, including, without limitation, any repurchase obligations of Customer under a Mortgage Purchase Program, if applicable; overdraft charges, wire charges, Account fees and charges for other miscellaneous services provided to Customer by Seattle Bank; and all other amounts, of any nature whatsoever, now or hereafter owed to the Seattle Bank by Customer.
- 1.1.37 “Physical Possession Collateral” is defined in Section 3.5 below.
- 1.1.38 “Regulations” means the regulations of the Finance Board, as amended from time to time.
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- 1.1.39 “Request” or “Requests” means any request(s) made by Customer via telephone, or other means made available by Seattle Bank from time to time, for Advances.
- 1.1.40 “Stock Ownership Requirement” means the obligation of Customer to own minimum amounts of Capital Stock in accordance with the Capital Plan.
- 1.1.41 “Swap Transaction” means an interest rate swap, cap or collar, currency exchange transaction, or any other similar transaction (including any option to enter into any of the foregoing) or any combination of the foregoing, entered into between the Seattle Bank and Customer pursuant to the terms of the Credit Policy, this Agreement or other related documentation, including without limitation any form of master agreement published by the International Swaps and Derivatives Association, Inc.
- 1.1.42 “UCC” means the Uniform Commercial Code, as amended from time to time, of the State of Washington or the state of formation of Customer, as applicable under Section 6.13 of this Agreement.
- 1.1.43 “Users Guide” means the Financial Products and Services Users Guide of the Seattle Bank, as published and revised by Seattle Bank from time to time.

Article II. Advances and Other Credit Accommodations

Section 2.1 Procedures for Advances The terms and conditions of this Agreement shall govern each Advance heretofore, now and hereafter made by Seattle Bank to Customer. The Credit Policy of the Seattle Bank is an integral part of the terms and conditions of all such Advances and is incorporated in this Agreement by this reference as if fully set forth herein. Additional terms and conditions of Advances may be set forth in an Advance Master Application and/or Advances Note, which Seattle Bank may require Customer to sign and deliver to Seattle Bank from time to time. Any additional, particular terms and conditions of an Advance orally quoted by Seattle Bank and accepted by Customer at the time of the Customer’s Request for an Advance, including, without limitation, the principal amount, applicable interest rate or due date of the Advance, will be confirmed by Seattle Bank in an Advance Confirmation Advice or, if no Advance Confirmation Advice is issued, will be evidenced by the books and records of the Seattle Bank. In cases in which a Request for an Advance is made orally by Customer of Seattle Bank in an electronically recorded telephone conversation, and a question arises concerning any particulars of such Advance, Customer agrees that such recording or a transcript thereof will be an integral part of the Seattle Bank’s books and records and may be used as evidence of such particulars. In cases in which an Advance requested orally by Customer is made by another federal home loan bank, on behalf of Seattle Bank, under a Master Backup Support Agreement, the books and records of such other federal home loan bank will establish any additional, particular terms of such Advance. If such Advance is requested by Customer of such other federal home loan bank in an electronically recorded telephone conversation, and a question arises concerning any particulars of such Advance, Customer agrees that such recording or a transcript thereof will be an integral part of the such other federal home loan bank’s books and records and may be used as evidence of such particulars. Unless otherwise agreed by Seattle Bank, each Advance will be made by crediting Customer’s demand deposit Account(s) with Seattle Bank. In all cases, funding of any Request for an Advance will be subject to compliance by Customer with the terms and provisions of the Act, the Regulations, the Credit Policy and this Agreement, including, without limitation, the Stock Ownership Requirement and Collateral Maintenance Requirement. In the event that Customer’s access to Advances is subsequently restricted pursuant to the Act, the Regulations or any other provision of applicable law, Seattle Bank will not be required to fund any outstanding Commitment for Advances not funded prior to the effective date of such restriction.

Section 2.2 Repayment of Advances Customer agrees to repay each Advance in accordance with its terms and conditions. Customer will maintain in Customer’s demand deposit Account(s) with Seattle Bank an amount at least equal to the amounts then currently due and payable to Seattle Bank with respect to Advances, and Customer hereby authorizes Seattle Bank to debit Customer’s Account(s) with Seattle Bank for all amounts due and payable with respect to any Advance and for all other amounts due and payable under this Agreement. Customer agrees that, in the event any such debit results in Customer’s demand deposit Account being overdrawn, Customer will pay overdraft charges thereon at the rate that Seattle Bank normally assesses for overdrafts on general demand deposit accounts. In the event that the balance in such demand deposit Account(s) is, at any time, insufficient to pay such due and payable amounts, Seattle Bank may in its discretion and without notice to Customer: (i) make a “flexible balance” or other similar Advance, as provided in the Credit Policy, in the amount of and for the purpose of paying such due and payable amounts; or (ii) apply any other deposits, credits, Funds or other monies of Customer then in the possession of Seattle Bank to the payment of such due and payable amounts. All payments with respect to Advances will be applied to any fees, costs or charges applicable thereto, to interest due thereon and to any principal amount thereof that is then due and payable, in such order and priority as Seattle Bank may determine.

Section 2.3 Estoppel For any Advance evidenced by an Advance Confirmation Advice, failure of Customer, within ten (10) business days of Customer's receipt of the Advance Confirmation Advice, to deliver written notice to Seattle Bank specifying any disputed particulars thereof, including without limitation the principal amount, applicable interest rate or due date of the Advance, will constitute the final agreement and acknowledgment by Customer that the particulars of the Advance Confirmation Advice are accurate and are those that Customer requested and by which Customer agreed to be bound, and Customer will thereafter be estopped from asserting any claim or defense with respect thereto. For any Advance which has such particular terms established by the books and records of the Seattle Bank or another federal home loan bank rather than by an Advance Confirmation Advice, such books and records shall be conclusive in the absence of manifest error. Seattle Bank reserves the right to correct its scrivener's errors, if any, in any Advance Confirmation Advice or such books and records, and no such errors shall affect Customer's obligations in respect to the affected Advance.

Section 2.4 Interest Customer agrees to pay interest on each Advance at a rate per annum determined on the basis described in the Credit Policy, Advance Master Application, Advances Note, Advance Confirmation Advice or the books and records of Seattle Bank or other federal home loan bank, as the case may be, pertaining to such Advance.

Section 2.5 Commitment and Cancellation Fees Customer agrees to pay when due any commitment fees and any cancellation fees applicable to any Commitments used by Seattle Bank for Advances, determined on the basis described in the Credit Policy, the Commitment documentation or the books and records of Seattle Bank or other federal home loan bank, as the case may be, pertaining to such Commitment.

Section 2.6 Other Credit Accommodations

- 2.6.1 Customer may apply to Seattle Bank for the issuance of other credit products, including without limitation Letters of Credit, firm commitments for Advances and Swap Transactions, provided such other credit products, and Customer's intended use thereof, are authorized under the Act, the Regulations and the Credit Policy. The terms and conditions of such Other Credit Accommodations shall be governed by the Act, the Regulations, the Credit Policy, this Agreement and such other documentation as Seattle Bank may require from time to time.
- 2.6.2 The Borrowing Capacity of Customer shall be reduced by Seattle Bank's outstanding obligations under any Letter of Credit, Swap Transaction, Commitment or Other Credit Accommodation, as determined by Seattle Bank from time to time, in the same manner as outstanding Advances.
- 2.6.3 In the event any Commitment, including without limitation a Letter of Credit, is outstanding at the time of an Event of Default under Section 4.1 of this Agreement, Seattle Bank may at its option make an Advance by crediting a special Account with Seattle Bank in an amount equal to the outstanding Commitment. Amounts credited to such special Account will be utilized by Seattle Bank for the purpose of satisfying Seattle Bank's obligations under the outstanding Commitment. When all such obligations have expired or have been satisfied, Seattle Bank will disburse the balance, if any, in such special Account first to the satisfaction of any Indebtedness then owing by Customer to Seattle Bank and then to Customer or its successors in interest. Advances made pursuant to this Subsection 2.7.3 will be payable on demand and will bear interest at the rate in effect and being charged by Seattle Bank from time to time on overdrafts on demand deposit accounts of its Customers.

Section 2.7 Prepayment Fees Customer agrees to pay a prepayment fee upon the prepayment of all or any portion of any Advance or Other Credit Accommodation, made before the due date thereof, whether such prepayment is made voluntarily or involuntarily, including, without limitation, any prepayment resulting from acceleration under Section 4.1 hereof upon an Event of Default. The amount of the prepayment fee shall not be less than zero and shall be determined by the Seattle Bank on the basis described in the Regulations, the Credit Policy and any applicable Advance Master Application, Advances Note, Advance Confirmation Advice or Swap Transaction, as the case may be, pertaining to prepayment of such Advance or Other Credit Accommodation. Any applicable illustrations and examples of prepayment fees in the Users Guide, as published and revised by the Seattle Bank from time to time, are an integral part of the terms and conditions of this Agreement and are incorporated herein by this reference as if fully set forth at length.

Section 2.8 Compliance with the Credit Policy, Act and Regulations Customer hereby agrees to comply with the terms and provisions of the Credit Policy, the Act and the Regulations, including, without limitation, any reporting requirements, application procedures or eligibility requirements imposed by the Credit Policy, the Act or the Regulations with respect to particular types of Advances, Commitments or Other Credit Accommodations. In the event of any inconsistency between the Credit Policy and the Act or the Regulations, Customer hereby agrees to comply with the more restrictive statute, regulation or policy. In the event any provision of the Credit Policy, the Act or the Regulations is amended, Customer agrees to comply with the terms and provisions of the Credit Policy, the Act and the Regulations as so amended from time to time, provided that, to the extent permitted by the Act and the Regulations, any particular terms of outstanding Advances or Commitments existing at the time of any such amendment, including, without limitation, interest rates or prepayment fees, will continue to be governed by the terms and provisions of the Advance Master Application, Advances Note, Advance Confirmation Advice or Commitment documentation which applied to such outstanding Advances or Commitments at the time such Advances or Commitments were made. Notwithstanding the foregoing, Seattle Bank shall retain the right to amend from time to time the Borrowing Capacity, Collateral Coverage Factors and Collateral Maintenance Requirements applicable to Customer and its Eligible Collateral, and Customer agrees to comply with such changes upon Seattle Bank's notice thereof to Customer.

Section 2.9 Additional Covenants by Customer Customer will maintain a copy of this Agreement in its official records at all times. Customer will give Seattle Bank notice of any material event that would cause Customer, pursuant to the provisions of the Act, the Regulations, the Credit Policy or this Agreement, to be ineligible to become a Customer of Seattle Bank or ineligible to obtain Advances, Commitments or Other Credit Accommodations. Any obligation of Seattle Bank to fund any Advance or Other Credit Accommodation, including any Commitment, shall be conditioned upon the satisfaction of each of the following conditions precedent as of the date hereof and at the time of funding of each Advance or Other Credit Accommodation: (a) all representations and warranties of Customer contained in this Agreement, or otherwise made by Customer to Seattle Bank, are and continue to be correct; (b) no Event of Default under this Agreement, or other documentation relating to the Advance or Other Credit Accommodation, has occurred or would result from such Advance; (c) the Seattle Bank has received such approvals, opinions or documents that the Seattle Bank may request in connection with the Advance or Other Credit Accommodation; (d) Customer satisfies all membership and borrowing eligibility criteria under the Act, the Regulations, this Agreement and the Credit Policy; (e) Customer, in the judgment of Seattle Bank, is not engaging or has not engaged in unsafe or unsound banking practices, has adequate capital, is not sustaining operating losses, does not have financial or managerial deficiencies that bear on the Customer's creditworthiness, and has no other deficiencies as determined by Seattle Bank; (f) there has been in Seattle Bank's judgment no material adverse change in Customer, the Collateral or any financial or other information submitted by Customer to Seattle Bank in connection with an Advance, Other Credit Accommodations or any Other Obligations; and (g) there has been in Seattle Bank's judgment no change in governmental laws or regulations that materially affects the Seattle Bank's power, right, authority, or ability to fund the Advance or Other Credit Accommodation.

Article III. Security Agreement

Section 3.1 Creation of Security Interest As security for the timely payment of all Indebtedness and outstanding Commitments, Customer hereby assigns, transfers, and pledges to Seattle Bank, and grants to Seattle Bank a security interest in all of the following Collateral now owned or hereafter acquired by Customer, and all proceeds thereof:

- 3.1.1 All promissory notes and other instruments, all mortgages, deeds of trust and other supporting obligations, all mortgage-backed securities, stock and other investment property, and all accounts, general intangibles, payment intangibles, chattel paper, letter of credit rights, deposit accounts, money, goods, software, commercial tort claims, equipment and inventory, now owned or hereafter acquired by Customer, including without limitation:
- (a) All Capital Stock now owned or hereafter acquired by Customer in Seattle Bank, including all payments which have been or hereafter are made on account of subscriptions to and all unpaid dividends on such stock;
 - (b) All Funds of Customer now and hereafter on deposit with Seattle Bank;
 - (c) All Eligible Mortgage Collateral and related Mortgage Documents now owned or hereafter acquired by Customer;
 - (d) All Eligible Securities Collateral now owned or hereafter acquired by Customer; and
 - (e) All Other Eligible Collateral now owned or hereafter acquired by Customer.
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3.1.2 It is the intention of Seattle Bank and Customer that the Collateral shall include all assets now owned or hereafter acquired by Customer in which a security interest can be created under the UCC, specifically including but not limited to the property types and categories set forth in Subsection 3.1.1 and Subparagraphs 3.1.1(a)-(e) above. All of the Collateral shall secure the Indebtedness, irrespective of whether only part of the Collateral constitutes Eligible Collateral for purposes of satisfying the Collateral Maintenance Requirements of Section 3.3 below.

Section 3.2 Customer's Representations and Warranties Regarding Collateral Customer represents and warrants to Seattle Bank, as of the date of this Agreement and the date of each Advance, Commitment or Other Credit Accommodation made under this Agreement, as follows:

- 3.2.1 Customer owns and has marketable title to all Collateral and has the right and authority to grant a security interest in the Collateral and to subject all of the Collateral to this Agreement, and Customer covenants that it will defend the Collateral against the claims and demands of all persons;
- 3.2.2 With respect to any Eligible Mortgage Collateral originated by any party (whether affiliated or unaffiliated) other than Customer, the Mortgage Documents contain either a complete chain of endorsements (either on the mortgage note or a related allonge) from the originating party to Customer, a complete chain of endorsements in blank from each successive holder of the Mortgage Collateral or are MERS Mortgages for which Customer's ownership has been registered with MERS.
- 3.2.3 The information contained in any financial report, call report, certification, audit, confirmation, report, schedule, or other documents required under this Agreement and any other information given from time to time by Customer as to each item of Eligible Collateral, and any information provided by Customer to its supervising state or federal agency in call reports or other reports, from which Seattle Bank obtains information related to Collateral, is true, accurate and complete in all material respects;
- 3.2.4 All Eligible Collateral meets the standards and requirements from time to time established by the Credit Policy, the Act and the Regulations and, in any case of variances among the Act, the Regulations and the Credit Policy, the most restrictive of such standards and requirements;
- 3.2.5 To Customer's knowledge, no part of any real property encumbered by Mortgage Collateral contains or is subject to the effects of any hazardous materials or other hazardous substances, except as may have been disclosed to and reasonably approved by Customer in its underwriting of Mortgage Collateral, and Customer will indemnify and hold Seattle Bank harmless, and, at the option of Seattle Bank, defend Seattle Bank (with counsel satisfactory to Seattle Bank) from all liabilities, costs, damages, claims or expenses (including attorneys' fees and environmental consultants' fees) suffered, paid or incurred by Seattle Bank resulting from or arising out of any requirement under any applicable federal, state or local law, regulation, ordinance, order, judgment or decree relating to the release or cleanup of any such hazardous material or hazardous substance;
- 3.2.6 Except as permitted under Section 3.3 of this Agreement, Customer will not (i) sell, offer to sell or otherwise transfer Eligible Collateral, nor pledge, mortgage or create or suffer to exist a lien, claim of lien, encumbrance, right to set-off or other security interest or collateral assignment of any kind whatsoever in Eligible Collateral or the proceeds thereof in favor of any person other than Seattle Bank, or (ii) transfer physical possession of the Mortgage Documents evidencing Eligible Mortgage Collateral to any third party or affiliate without the prior written consent of Seattle Bank;
- 3.2.7 All taxes, assessments and governmental charges levied or assessed or imposed upon or with respect to Eligible Collateral, including any real property subject to Eligible Mortgage Collateral, will be paid and if Customer fails to promptly pay such taxes, assessments or governmental changes, Seattle Bank may (but will not be required to) pay the same and any such expense will be an obligation under this Agreement; and
- 3.2.8 Customer will notify Seattle Bank promptly in writing of any change in the location of the Eligible Collateral and of any change in location of its principal place of business or jurisdiction of incorporation, organization or formation.
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Section 3.3 Collateral Maintenance Requirement

- 3.3.1 Customer will at all times maintain an amount of Eligible Collateral, pledged to Seattle Bank under this Agreement, which, after discounting by the Collateral Coverage Factor(s) applicable to such Eligible Collateral, has a value, as determined by Seattle Bank, of not less than the aggregate amount of all Advances, Commitments and Other Credit Accommodations then outstanding. This Collateral Maintenance Requirement may be increased or decreased by Seattle Bank at any time, based upon Customer's creditworthiness or the quality of Customer's Eligible Collateral, as determined by Seattle Bank from time to time. Customer will not, without prior written consent of Seattle Bank, assign, pledge, transfer, create any security interest in, sell, or otherwise dispose of any Eligible Collateral if: (i) such Eligible Collateral is Physical Possession Collateral under Section 3.5 of this Agreement; (ii) immediately after such action, Customer's remaining Eligible Collateral would be insufficient to comply with the Collateral Maintenance Requirement; or (iii) at the time of such action, there is an outstanding Event of Default under Section 4.1 of this Agreement.
- 3.3.2 All Eligible Collateral (other than Physical Possession Collateral held by Seattle Bank of its custodian) will be held by Customer in trust for the benefit of, and subject to the direction and control of Seattle Bank, and will be physically safeguarded by Customer with at least the same degree of care as Customer would ordinarily use in prudently safeguarding its property. Without limiting the foregoing, Customer will take all action necessary or desirable to protect and preserve Eligible Collateral held by Customer, including without limitation the maintaining of insurance on property securing mortgages constituting Eligible Collateral (such policies and certificates of insurance relating to such mortgages are in this Agreement called "insurance"), the collection of payments under all such mortgages and under all such insurance, and otherwise assuring that loans comprising Eligible Mortgage Collateral are serviced in accordance with the standards of a reasonable and prudent mortgagee. Customer, as Seattle Bank's agent, will collect all payments when due on all Eligible Collateral held by Customer in trust for the benefit of Seattle Bank. If Seattle Bank requests, all such collections shall be held separate from Customer's other monies in one or more designated Accounts maintained at Seattle Bank. At Seattle Bank's sole discretion, Seattle Bank may then apply such collections to the payment of Indebtedness as it becomes due; otherwise, and provided there is no outstanding Event of Default under Section 4.1 of this Agreement, Customer may use and dispose of such collections in the ordinary course of its business.
- 3.3.3 Subject to the Collateral Maintenance Requirement of Subsection 3.3.1 above, and provided there is no outstanding Event of Default under Section 4.1 of this Agreement, Customer may use or dispose of all or part of the Collateral and proceeds thereof in the ordinary course of its business. Notwithstanding the foregoing, Customer may not use or dispose of all or part of Physical Possession Collateral or the proceeds thereof, except upon the De-Pledging of such Physical Possession Collateral in accordance with Section 3.6 below.
- 3.3.4 Customer will, upon request of Seattle Bank, immediately take such actions and execute such documentation as Seattle Bank may deem necessary or appropriate to create and perfect Seattle Bank's security interest in the Collateral or otherwise to obtain, preserve, protect, enforce or collect the Collateral; including, without limitation, executing any agreements, instructions or other documents that Seattle Bank deems necessary to establish control of Collateral by Seattle Bank or by its custodian on Seattle Bank's behalf.
- 3.3.5 Any Collateral that is not satisfactory to Seattle Bank may be rejected at any time as Eligible Collateral by Seattle Bank, or in Seattle Bank's discretion may at any time be discounted by a Collateral Coverage Factor that is less than the Collateral Coverage Factor normally ascribed thereto under the Credit Policy. Seattle Bank may require, before or during the period when any Advance is made to Customer, that Customer make any or all Eligible Securities Collateral, all Mortgage Documents for Eligible Mortgage Collateral and any other documents pertaining to Eligible Collateral, including without limitation any agreements between Customer and its servicing agents, available to Seattle Bank for its inspection and approval.
- 3.3.6 In the case of any Eligible Collateral which is physically possessed by Customer, Customer will grant, upon Seattle Bank's written request, an irrevocable license to Seattle Bank, in form and content satisfactory to Seattle Bank (and if requested by Seattle Bank, joined in by any real property owner or landlord of the premises where such Eligible Collateral is located), that will allow representatives of Seattle Bank to enter the premises of Customer in order to inspect from time to time and/or remove and take possession of the Eligible Collateral.
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- 3.3.7 In the case of Eligible Collateral which is physically possessed by any affiliate or servicing agent of Customer, Customer will, upon Seattle Bank's written request, cause Customer's affiliate or servicing agent to (i) grant an irrevocable license to Seattle Bank, in form and content satisfactory to Seattle Bank (and if requested by Seattle Bank, joined in by any real property owner or landlord of the premises where such Eligible Collateral is located), that will allow representatives of Seattle Bank to enter the premises of Customer's affiliate or servicing agent in order to inspect from time to time and/or remove and take possession of the Eligible Collateral; and/or (ii) establish custodial or control agreements, in form and content satisfactory to Seattle Bank, under which the affiliate's or servicing agent's physical possession will be held for the benefit of Seattle Bank as secured party. Seattle Bank may require such arrangements irrespective of whether the Eligible Collateral has been designated as Listed Collateral or Physical Possession Collateral under Sections 3.4 or 3.5 below.
- 3.3.8 Seattle Bank's acceptance as Eligible Collateral of any Mortgage Collateral relating to multifamily or commercial properties may, in the discretion of Seattle Bank, be conditioned upon Customer's execution and delivery of Rider(s) to this Agreement containing warranties and representations required of Customer by Seattle Bank for any Mortgage Collateral relating to multifamily or commercial properties.

Section 3.4 Listed Collateral

- 3.4.1 At any time that Customer's Eligible Mortgage Collateral or Eligible CFI Collateral becomes subject to mandatory listing requirements under the Credit Policy, or at any time, at the sole discretion of Seattle Bank, Customer will deliver to Seattle Bank, upon Seattle Bank's written request, a status report and accompanying schedules, all in form and content acceptable to Seattle Bank, specifying and describing any mortgage loan pledged to Seattle Bank as Eligible Mortgage Collateral and any item of Eligible CFI Collateral pledged to Seattle Bank (collectively, "Listed Collateral"). At such other times as Seattle Bank may request, Customer will deliver to Seattle Bank periodic status reports and accompanying schedules, in form and content acceptable to Seattle Bank, describing the status of the Listed Collateral.
- 3.4.2 Upon Seattle Bank's written request, Customer will physically segregate the mortgages, loan packages and other property comprising Listed Collateral from all other property of Customer in a manner satisfactory to Seattle Bank. Until particular items of Listed Collateral are De-Pledged in accordance with the Credit Policy, the physical segregation of such items shall be maintained.
- 3.4.3 Upon Seattle Bank's written request, Customer will hold each loan package included in Listed Collateral in a separate file folder, with each file folder clearly labeled with the loan identification number and the name of the mortgagor. Upon written request of Seattle Bank, the file folder for each package of loan documents included within Listed Collateral will be clearly marked or stamped with the statement: "The Instrument(s) and Security Relating to this Loan Have Been Pledged to the Federal Home Loan Bank of Seattle."

Section 3.5 Physical Possession Collateral

- 3.5.1 At any time that Customer becomes subject to mandatory physical possession requirements under the Credit Policy, or at any other time, at the sole discretion of Seattle Bank, Customer will deliver to Seattle Bank, or to a custodian approved by Seattle Bank in its discretion, upon Seattle Bank's written request, the mortgage loans pledged to Seattle Bank as Eligible Mortgage Collateral, securities pledged to Seattle Bank as Eligible Securities Collateral, loans pledged to Seattle Bank as Eligible CFI Collateral and each item of Other Eligible Collateral pledged to Seattle Bank (collectively, "Physical Possession Collateral").
- 3.5.2 Eligible Mortgage Collateral delivered to Seattle Bank or its approved custodian as Physical Possession Collateral will be endorsed or assigned by Customer in blank or, if requested by Seattle Bank, to Seattle Bank. For MERS Mortgages, Customer will execute a notification to MERS of its assignment of the MERS Mortgage in blank or, if requested by Seattle Bank, to Seattle Bank. Regardless of whether any endorsement is stated to be "without recourse," Customer shall be liable for any deficiency remaining after any exercise by the Bank of its remedies in respect of Collateral, as provided in Section 4.2 below.
- 3.5.3 With respect to certified Eligible Securities Collateral pledged to Seattle Bank as Physical Possession Collateral, the delivery requirements contained in this Section 3.5 will be satisfied, at the election of Seattle Bank, by one of more of: (i) transfer of physical possession of such certificated securities to Seattle Bank; (ii) re-registration of such securities in Seattle Bank's name; or (iii) possession of such certificated securities, on Seattle Bank's behalf, by a custodian approved by Seattle Bank. Any such possession of certificated securities by an approved custodian, on Seattle Bank's behalf, will be effected and evidenced by documentation acceptable to Seattle Bank in form and content, establishing Seattle Bank's control of such certificated securities under the provisions of the UCC.
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- 3.5.4 With respect to uncertificated Eligible Securities Collateral pledged to Seattle Bank as Physical Possession Collateral, satisfaction of the delivery requirements contained in this Section 3.5 will be effected and evidenced by agreements, instructions or other documentation acceptable to Seattle Bank in form and content, establishing Seattle Bank's control of such uncertificated securities under the provisions of the UCC.
- 3.5.5 Concurrently with the initial delivery of Physical Possession Collateral, and at such other times as Seattle Bank may request, Customer will deliver to Seattle Bank a status report and accompanying schedules, in form and content acceptable to Seattle Bank, describing the status of the Physical Possession Collateral held by Seattle Bank or its custodian. At such other times as Seattle Bank may request, Customer will deliver to Seattle Bank periodic status reports and accompanying schedules, in form and content acceptable to Seattle Bank, describing the status of the Physical Possession Collateral. Until Physical Possession Collateral is De-Pledged in accordance with Section 3.6 below, such physical possession by Seattle Bank or its approved custodian shall be maintained with respect to such Physical Possession Collateral. At Seattle Bank's sole discretion, all proceeds the Physical Possession Collateral, including without limitation all payments made under the loans or securities constituting Physical Possession Collateral, shall be held separate from Customer's other monies in one or more designated Accounts maintained at Seattle Bank. Seattle Bank may apply such monies to the payment of Indebtedness as it becomes due, or hold such monies as part of its Physical Possession Collateral, subject to De-Pledging under the terms and conditions of Section 3.6 below.
- 3.5.6 Customer agrees to pay to Seattle Bank such reasonable fees and charges as may be assessed by Seattle Bank to cover Seattle Bank's overhead and other costs relating to the receipt, holding, De-Pledge, redelivery and reassignment of Physical Possession and to reimburse Seattle Bank upon request for all filing or recording fees and other reasonable expenses, disbursements and advances incurred or made by Seattle Bank in connection therewith, including without limitation reasonable attorneys fees and costs of legal counsel of Seattle Bank. Customer shall pay the fees and expenses, including, without limitation, reasonable attorneys fees and costs, of any custodian approved or retained by Seattle Bank with respect to Collateral. As such sums owed to Seattle Bank or to such custodian may be collected by Seattle Bank, at its option, by debiting Customer's Account(s) with Seattle Bank.

Section 3.6 De-Pledging of Collateral Upon receipt by Seattle Bank of a written request from Customer, in form and content acceptable to Seattle Bank, for the De-Pledging of any part of the Collateral or proceeds thereof in which Seattle Bank has perfected its security interest, setting forth (i) a sufficient description of the Collateral to be withdrawn or reassigned; and (ii) a certificate of an authorized officer of Customer certifying that the immediately after such De-Pledge, Customer's remaining Eligible Collateral will be sufficient to comply with the Collateral Maintenance Requirement, Seattle Bank will promptly return, reassign or partially release to Customer, at Customer's expense, the Collateral specified in said request. Notwithstanding anything to the contrary contained in this Agreement, Customer may not obtain any such withdrawal or reassignment (a) while an Event of Default under this Agreement has occurred and is continuing; (b) at any time that Seattle Bank's records indicate that immediately after such De-Pledge, Customer's remaining Eligible Collateral would be insufficient to comply with the Collateral Maintenance Requirement as determined by Seattle Bank; or (c) at any time that Seattle Bank reasonably and in good faith deems itself insecure. Customer will pay upon request for all filing or recording fees and other reasonable expenses incurred by Seattle Bank or any approved custodian in connection with De-Pledging of any Collateral, including without limitation reasonable attorneys fees and costs of legal counsel of Seattle Bank or such custodian. Any such sums owed to Seattle Bank or to such custodian may be collected by Seattle Bank, at its option, by debiting Customer's demand or time deposit Account (s) with Seattle Bank.

Section 3.7 Reports, Collateral Audits; Access

- 3.7.1 If requested by Seattle Bank at any time, Customer will furnish to Seattle Bank an audit report prepared in accordance with generally accepted auditing standards by an external auditor acceptable to Seattle Bank, certifying the book value of the Eligible Collateral owned by Customer. If requested by Seattle Bank at any time, Customer will furnish to Seattle Bank a written report covering such matters regarding Eligible Collateral as Seattle Bank may require, including without limitation a listing of mortgages comprising Eligible Mortgage Collateral or loans comprising Eligible CFI Collateral, the unpaid principal balances thereof, the status of payments thereon and of taxes and insurance on the property encumbered thereby; securities and the publicly listed market value thereof, and any other information requested by Seattle Bank regarding the Eligible Collateral. Customer will give Seattle Bank access at all reasonable times to Collateral in Customer's possession and to Customer's books and records of account relating to such Collateral, for the purpose of Seattle Bank's examining, verifying or reconciling the Collateral and Customer's report to Seattle Bank thereon.
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3.7.2 All Collateral and the satisfaction by Customer of the Collateral Maintenance Requirement will be subject to audit and verification by or on behalf of Seattle Bank. Such audits and verifications may occur without notice during Customer's normal business hours or upon reasonable notice at such other times as Seattle Bank may reasonably request. Customer will provide access to, and will make adequate working facilities available to, the representatives or agents of Seattle Bank for purposes of such audits and verifications. Customer agrees to pay to Seattle Bank such reasonable fees and charges as may be assessed by Seattle Bank to cover overhead and other costs relating to such audit and verification.

Section 3.8 Additional Documentation Customer will make, execute, record and deliver to Seattle Bank such notices, instructions, assignments, listings, powers, and other documents with respect to the Collateral and Seattle Bank's security interest therein in such form as Seattle Bank may require. Customer authorizes Seattle Bank to file such financing statements as Seattle Bank deems necessary with respect to the Collateral, and Customer hereby ratifies any financing statements previously filed by Seattle Bank with respect to the Collateral.

Section 3.9 Seattle Bank's Responsibilities as to Collateral In the event that Seattle Bank takes possession of any Collateral pursuant to the terms of this Agreement, Seattle Bank's duty as to the Collateral will be solely to use reasonable care in the custody and preservation of the Collateral in its possession, which will not include any steps necessary to preserve Customer's rights against any third parties nor the duty to send notices, perform services, or take any action in connection with management of the Collateral. Seattle Bank will not have any responsibility or liability for the form, sufficiency, correctness, genuineness or legal effect of any instrument or document constituting a part of the Collateral, or any signature thereon or the description or misdescription, or value of property represented, or purported to be represented, by any such document or instrument. Customer agrees that any and all Collateral may be removed by Seattle Bank from the state or location where situated, and may there be dealt with by Seattle Bank as provided in this Agreement.

Section 3.10 Seattle Bank's Rights as to Collateral At any time or times, at the expense of Customer, Seattle Bank will have the right, before or after the occurrence of an Event of Default as set forth in Section 4.1 of this Agreement, but shall not have the obligation, to do any or all things and take any and all actions that are deemed necessary or convenient by Seattle Bank to the protection of its rights and interests under this Agreement and are lawful under the Act, the Regulations and the laws of the State of Washington, including, but not limited to, the following:

- 3.10.1 Terminate any consent given under this Agreement;
- 3.10.2 Notify obligors on any Collateral to make payments thereon directly to Seattle Bank;
- 3.10.3 Endorse any Collateral that is in Customer's name or that has been endorsed by others to Customer's name;
- 3.10.4 Enter into any extension, compromise, settlement, or other agreement relating to or affecting any Collateral;
- 3.10.5 Take any action Customer is required to take or which is otherwise necessary to: (i) file a financing statement or otherwise perfect a security interest in any or all of the Collateral; or (ii) to obtain, preserve, protect, enforce or collect the Collateral;
- 3.10.6 Take control of any funds or other proceeds generated by the Collateral and use the same to reduce Indebtedness as it becomes due; and
- 3.10.7 Cause the Collateral to be transferred to Seattle Bank's name or the name of its nominee.

Section 3.11 Power of Attorney Customer hereby appoints Seattle Bank as its true and lawful attorney, for and on behalf of Customer and in its name, place and stead, to prepare, execute and record endorsements and assignments to Seattle Bank of all or any item of Collateral, giving or granting to Seattle Bank, as such attorney, full power and authority to do or perform every lawful act necessary or proper in connection therewith as fully as Customer might or could do. Customer hereby ratifies and confirms all that Seattle Bank will lawfully do or cause to be done by virtue of this special power of attorney. This special power of attorney is granted for a period commencing on the date of this Agreement and continuing until the discharge of all Indebtedness and Commitments and all obligations of Customer under this Agreement regardless of any Event of Default by Customer, is coupled with an interest and is irrevocable for the period granted. As Customer's true and lawful attorney-in-fact, Seattle Bank has no responsibility to take any steps necessary to preserve rights against prior parties nor the duty to send notices, perform services, or take any action in connection with the management of the Collateral.

Article IV. Default; Remedies

Section 4.1 Events of Default; Acceleration Upon the occurrence of and during the continuation any of the following events or conditions of default (“Event of Default”), Seattle Bank may at its option, by a notice to Customer, declare all Indebtedness and accrued interest thereon, including any prepayment fees or charges which are payable in connection with the payment prior to the originally scheduled maturity of any Advance or Other Credit Accommodation, to be immediately due and payable without presentment, demand, protest or any further notice and/or terminate any obligation on the part of Seattle Bank in respect of any Commitment to make or continue making any Advances:

- 4.1.1 Failure of Customer to pay when due any interest on or principal of any Advance or Other Credit Accommodation; or
 - 4.1.2 Failure of Customer to perform any promise or obligation or to satisfy any condition or liability contained in this Agreement, the Credit Policy or any Advances Note, Advance Master Application or Advance Confirmation Advice, or in any other agreement to which Customer and Seattle Bank are parties, whether pertaining to any Advance, Other Credit Accommodation or Other Obligations; or
 - 4.1.3 Evidence coming to the attention of Seattle Bank that any representations, statements, or warranty made or furnished in any manner to Seattle Bank by or on behalf of Customer in connection with any Advance or Other Credit Accommodation, any specification of Eligible Collateral or any certification of Fair Market Value were false, misleading or incomplete in any material respect when made or, with the passage of time, have become untrue in any material respect; or
 - 4.1.4 Failure of Customer to maintain adequate Eligible Collateral free of any encumbrances or claims as required in this Agreement, or any material damage to or loss of Eligible Collateral, or any sale or encumbrance of any Eligible Collateral except as permitted by this Agreement
 - 4.1.5 The issuance of any tax, levy, seizure, attachment, garnishment, levy of execution, or other process with respect to any of the Collateral; or
 - 4.1.6 Any suspension of payment by Customer to any creditor of sums due or the occurrence of any event which results in another creditor having the right to accelerate the maturity of any indebtedness of Customer under any security agreement, indenture, loan agreement, or comparable undertaking; or
 - 4.1.7 Any taking over of the Customer or any of its assets or affiliates by a supervising agency, or an application for or appointment of a conservator or receiver for Customer or any affiliate of Customer or Customer’s property, entry of a judgment or decree adjudicating Customer or any affiliate of Customer insolvent or bankrupt, an assignment by Customer or any affiliate of Customer for benefit of creditors, or the entry of any supervisory or consent order pertaining to Customer or any affiliate of Customer by any regulatory body or by any court at the request of such regulator; or
 - 4.1.8 Sale by Customer of all or a material part of Customer’s asset or the taking of any other action by Customer to liquidate or dissolve; or
 - 4.1.9 Termination of Customer’s membership in Seattle Bank, or Customer’s ceasing to be a type of financial institution that is eligible under the Act or the Regulations to become a Customer of Seattle Bank; or
 - 4.1.10 Merger, consolidation or other combination of Customer with an entity which is not a Customer of Seattle Bank if the non-Customer entity is the surviving entity; or
 - 4.1.11 Seattle Bank determines in good faith that a material adverse change has occurred in the financial condition of Customer from that disclosed at the time of the making of any Advance or from the condition of Customer as theretofore most recently disclosed to Seattle Bank; or
 - 4.1.12 Seattle Bank in good faith deems itself insecure even though Customer is not otherwise in default; or
 - 4.1.13 Customer has borrowed, or committed to borrow, from any source an amount that is greater than the amount Customer is permitted to borrow under applicable law.
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Section 4.2 Remedies Upon the occurrence of any Event of Default, Seattle Bank will have all of the rights and remedies provided by applicable law, including but not limited to all of the remedies of a secured party under the UCC. In addition, Seattle Bank may take immediate possession of any of the Collateral or any part thereof wherever the same may be found. Seattle Bank may sell, assign and deliver the Collateral or any part thereof at public or private sale for such price as Seattle Bank deems appropriate without any liability for any loss due to decrease in the market value of the Collateral during the period held. Seattle Bank will have the right to purchase all or part of the Collateral at such sale. If the Collateral includes insurance or securities which will be redeemed by the issuer upon surrender, or any accounts or deposits in the possession of Seattle Bank, Seattle Bank may realize upon such Collateral without notice to Customer. If any notification of intended disposition of any of the Collateral is required by applicable law, then, if no greater period of notification is required by applicable law, such notification will be deemed reasonable and properly given if mailed, postage prepaid, at least 10 days before any such disposition to the address of Customer appearing on the records of Seattle Bank. The proceeds of any sale will be applied in the order that Seattle Bank, in its sole discretion, may choose. Customer agrees to pay all the costs and expenses of Seattle Bank in the collection of the Indebtedness and enforcement of Seattle Bank's rights and remedies in case of default, including, without limitation, reasonable attorneys' fees. Seattle Bank will, to the extent required by law, apply any surplus after payment of the Indebtedness, provision for repayment to Seattle Bank of any amounts to be paid or advanced under outstanding Commitments, and all costs of collection and enforcement to third parties claiming a secondary security interest in the Collateral, with any remaining surplus paid to Customer. Customer will be liable to Seattle Bank for any deficiency remaining.

Section 4.3 Payment of Prepayment Charges Any prepayment fees or charges for which provision is made, whether under the Regulations, the Credit Policy, or any applicable Advance Master Application, Advances Note, Advance Confirmation Advice or Swap Transaction, as the case may be, with respect to any Advances or Other Credit Accommodations, will be payable at the time of any voluntary or involuntary payment of the principal of such Advances or Other Credit Accommodations prior to the originally scheduled maturity thereof, including, without limitation, payments that are made as a part of a liquidation of Customer or that become due as a result of an acceleration pursuant to Section 4.1 of this Agreement, whether such payment is made by Customer, by a conservator, receiver, liquidator or trustee of or for Customer, or by any successor to or any assignee of Customer.

Article V. Accounts

Section 5.1 Deposit Accounts The Customer may open Accounts with the Seattle Bank subject to the Act, the Regulations, the Credit Policy and any other policies adopted by the Seattle Bank from time to time in respect to Accounts and related services, including without limitation the wire transfer of funds. Any Customer's funds deposited in Accounts shall be subject to withdrawal or charge at any time and from time to time upon wire transfers or any other orders for the payment of money when made and drawn on behalf of the Customer by a person or persons authorized by Resolution of the Customer under Section 6.7 below. The Seattle Bank is authorized to pay any such wire transfers or other orders, provided they are in the form prescribed by it, and to charge the Customer's Accounts therefore, without inquiry as to the circumstances of issue or the disposition of the proceeds, even if drawn to the individual order of any authorized person or payable to others for his account.

Section 5.2 Bank's Reliance The Seattle Bank, if it acts in good faith and with ordinary care (and without liability if it does so act), can charge the Accounts with orders received by the Seattle Bank by telephone, or otherwise orally, from any person acting for or purporting to act for the Customer as its officer or employee, for the transfer of funds to others, including the person giving such instructions or payable to others for his account, or between Accounts of the Customer. All scheduled charges and fees adopted by the Seattle Bank from time to time in respect to Accounts and related services will be charged monthly to such Accounts.

Section 5.3 Positive Balance Requirement The Customer shall maintain a net positive collected balance in all of its Accounts. The Seattle Bank shall have the option of closing or restricting the use of Accounts in which positive balances are not maintained. For each day the aggregate collected balance of an Account is negative, the Customer shall pay such overdraft charges as are consistent with the scheduled charges and fees adopted by the Seattle Bank from time to time in respect to Accounts and related services.

Article VI. Miscellaneous

Section 6.1 General Representations and Warranties by Customer Customer hereby represents and warrants that, as of the date of this Agreement and the date of each Advance or Other Credit Accommodation, including any Commitment, made pursuant to this Agreement:

- 6.1.1 Customer is not, and neither the execution of nor the performance of any of the transactions or obligations of Customer under this agreement will, with the passage of time, the giving of notice or otherwise, cause Customer to be: (i) in violation of its charter or articles of incorporation, by-laws, the Act, or the Regulations, any other law or administrative regulation, or any court decree; or (ii) in default under or in breach of any indenture, contract, or other instrument or agreement to which Customer is a party or by which it or any of its property is bound.
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- 6.1.2 Customer has full corporate power and authority and has received all corporate and governmental authorizations and approvals (including without limitation those required under the Act and the Regulations) as may be required to enter into and perform its obligations under this Agreement, to borrow each Advance and to obtain each Other Credit Accommodation.
- 6.1.3 The information given by Customer in any document provided, or in any oral statement made, in connection with any application or request for an Advance or Other Credit Accommodation, is true, accurate and complete in all material respects.

Section 6.2 Assignment Seattle Bank may assign or negotiate to any other federal home loan bank or to any other person or entity, with or without recourse, any Indebtedness of Customer or participations therein, and Seattle Bank may assign or transfer all or any part of Seattle Bank's right, title, and interest in and to this Agreement and may assign and deliver the whole or any part of the Collateral to the transferee, which will succeed to all the powers and rights of Seattle Bank in respect thereof, and Seattle Bank will thereafter be forever relieved and fully discharged from any liability or responsibility with respect to the transferred Collateral. Customer hereby acknowledges and agrees that any such disposition will give rise to a direct obligation of Customer to the participant. Customer hereby authorizes Seattle Bank and each participant, in case of default by Customer under this Agreement, to proceed directly, by right of setoff or otherwise, against any assets of Customer which may at the time of such default be in the respective hands of Seattle Bank or any such participant. Customer further agrees that Seattle Bank may furnish any information pertaining to Customer which is in the possession of Seattle Bank to any prospective participant to assist it in evaluating such participation provided that any non-public information reasonably designated in writing to Seattle Bank by Customer as constituting non-public information will be furnished to such prospective participant on a confidential basis. Customer may not assign or transfer any of its rights or obligations under this Agreement without the express prior consent of Seattle Bank, which may be granted or withheld in Seattle Bank's sole discretion.

Section 6.3 Discretion of Seattle Bank to Grant or Deny Advances Nothing contained in this Agreement or in any documents describing or setting forth the Credit Policy or any other policy of Seattle Bank will be construed as an agreement or commitment on the part of Seattle Bank to grant Advances or extend Commitments or Other Credit Accommodations under this Agreement, the right and power of Seattle Bank in its discretion to either grant or deny any of the foregoing being herein expressly reserved.

Section 6.4 Amendment; Waivers No modification, amendment or waiver of any provision of this Agreement or consent to any departure therefrom will be effective unless executed by the party against whom such change is asserted and will be effective only in the specific instance and for the purpose for which given. No notice to or demand on Customer in any case will entitle Customer to any other or further notice or demand in the same, or similar or other circumstances. Any forbearance, failure or delay by Seattle Bank in exercising any right, power or remedy under this Agreement will not be deemed to be a waiver thereof, and any single or partial exercise by Seattle Bank of any right, power or remedy under this Agreement will not preclude the further exercise thereof. Every right, power and remedy of Seattle Bank will continue in full force and effect until specifically waived by Seattle Bank in writing.

Section 6.5 Exceptions to Credit Policy Customer acknowledges and agrees that no exception to the Credit Policy requested of Seattle Bank by Customer shall be binding upon the Seattle Bank unless (i) approved in writing by the Seattle Bank's authorized representative and (ii) authorized by the Act and Regulations.

Section 6.6 Jurisdiction; Legal Fees In any action or proceeding brought by Seattle Bank or Customer in order to enforce any right or remedy under this Agreement, the parties hereby consent to, and agree that they will submit to, the jurisdiction of the United States District Court for the Western District of Washington, or, if such action or proceeding may not be brought in federal court, the jurisdiction of the courts of King County, Washington. Customer agrees that, if any action or proceeding is brought by Customer seeking to obtain any legal or equitable relief against Seattle Bank under or arising out of this Agreement or any transaction contemplated hereby, and such relief is not granted by the final decision, after any and all appeals, of a court of competent jurisdiction, Customer will pay all attorneys' fees and other costs incurred by Seattle Bank in connection therewith. Customer agrees to reimburse Seattle Bank for all costs and expenses (including reasonable fees and out-of-pocket expenses of counsel for Seattle Bank) incurred by Seattle Bank in connection with (i) the administration, enforcement, interpretation or preservation of Seattle Bank's rights under this Agreement including, but not limited to, its rights in respect of any Collateral or the audit or possession thereof, whether or not an Event of Default has occurred or any suit has been brought; (ii) Seattle Bank's rights in any litigation, arbitration or supervisory, receivership, bankruptcy or other insolvency or regulatory proceedings affecting Customer, any Collateral or any Advances, Other Credit Accommodations or Other Obligations; or (iii) Seattle Bank's preparation of additional documentation for Advances, Other Credit Accommodations or Other Obligations or any Collateral, or any amendments, approvals, consents, waivers or releases requested, required, proposed or done from time to time.

Section 6.7 Notices Except as provided in Subsection 6.8.3 below, any notice, advice, request, consent or direction given, made or withdrawn pursuant to this Agreement must be in writing or by machine-readable electronic transmission, and will be deemed to have been given to and received by a party to this Agreement when mailed to such party at its address given above by first class mail, or if given by hand or by electronic transmission, when actually received by such party at its principal office.

Section 6.8 Signatures of Customer; Resolution; Oral Requests

- 6.8.1 The Secretary or the Assistant Secretaries of Customer will from time to time certify to Seattle Bank on forms provided by Seattle Bank the names and specimen signatures of the persons authorized to apply on behalf of Customer to Seattle Bank for Advances and otherwise act for and on behalf of Customer in accordance with this Agreement. Such certifications are incorporated in this Agreement and made a part of this Agreement and will continue in effect until expressly revoked by Customer notwithstanding that subsequent certifications may authorize additional persons to act for and on behalf of Customer.
- 6.8.2 Prior to or at the time of the execution and delivery of this Agreement, the Secretary or the Assistant Secretaries of Customer shall provide the Seattle Bank with a certified copy of a resolution adopted by the Customer's Board of Directors or other governing body ("Resolution") approving this Agreement and authorizing designated officers or employees of the Customer to obtain Advances and Other Credit Accommodations, open and use Accounts, and incur Other Obligations. The Seattle Bank may rely upon, and the Customer is estopped from denying, the authority of the persons designated in the Resolution or of the persons to whom such authority has been delegated pursuant to the terms of the Resolution.
- 6.8.3 Notwithstanding the preceding or any other provision of this Agreement, the Seattle Bank may, but is not obligated to, honor, and Customer shall be bound by, any form of request, including an oral request, for Advances, Other Credit Accommodations or other services from Seattle Bank, whenever such requests are made by persons purporting to act as officers or employees of Customer, if Seattle Bank acts in good faith and with ordinary care (and without liability if it does so act).

Section 6.9 Recording Conversations Customer for itself and its employees hereby authorizes and consents to Seattle Bank's electronic recording of, transcription of and use of all telephone conversations made by Customer's employees to the Seattle Bank for the purpose of requesting Advances or Other Credit Accommodations. The period of time for which such recordings are stored or whether transcriptions are made shall be determined by Seattle Bank.

Section 6.10 Stock Ownership Requirement The Seattle Bank and the Customer acknowledge and agree that the Customer is subject to the Member Advance Stock Purchase Requirement and other terms and conditions set forth in the Capital Plan of the Seattle Bank. The Member Advance Stock Purchase Requirement provides that the Customer hold a specified amount capital stock in the Seattle Bank in connection with Advance transactions. Currently, each Customer is required to hold Class B (1) stock with a par value equal to three and one-half percent (3.5%) of the unpaid principal balances of Advances As set forth in the Capital Plan, the Board of Directors of the Seattle Bank may change the above percentage within a range of not less than two and one-half percent (2.5%) or not greater than four and one-half percent (4.5%). The Customer agrees to be bound by any such change in the Member Advance Stock Purchase Requirement percentage. Any such change in the Member Advance Stock Purchase Requirement will be applied as of the implementation date of the change to all new Advances made by the Seattle Bank to the Customer. In addition, the Customer agrees and acknowledges that it will be subject to all amendments to the Capital Plan, that may be made from time to time.

Section 6.11 Force Majeure Any obligations of the Seattle Bank in connection with the Agreement, any Commitment, or otherwise arising in connection with any Advance, Other Credit Accommodation, Account, Mortgage Purchase Program or other service, shall be excused to the extent delayed or prevented by reason of computer, communications system or power failure, labor disturbances, governmental laws, orders or regulations, riots, insurrection, acts of terror, war or any other causes beyond the reasonable control of the Seattle Bank. In addition, the Seattle Bank shall not be liable for the failure of any wire transfer, fedwire or other such system.

Section 6.12 Limitation of Damages If Seattle Bank, in connection with this Agreement, any Commitment, or any Advance, Other Credit Accommodation, Account, Mortgage Purchase Program or other service, breaches any obligation of Seattle Bank to Customer not otherwise excused by this Agreement or applicable law, Seattle Bank will be obligated to Customer only for Customer's actual, direct damages, if any. Under no circumstances shall Seattle Bank be liable for, and Customer hereby forever waives, any special, indirect or consequential damages or any punitive or exemplary damages.

Section 6.13 Applicable Law; Severability In addition to the terms and conditions specifically set forth in this Agreement and any other related documentation, this Agreement, and all Advances granted and Commitments extended under this Agreement, will be governed by the statutory and common law of the United States and, to the extent Federal law incorporates or defers to state law, the laws (exclusive of the choice of law provisions) of the State of Washington. Notwithstanding the foregoing, the UCC of the State of Washington, as amended from time to time, will be deemed applicable to this Agreement and to any Advance or Other Credit Accommodation made or Collateral pledged under this Agreement, except as otherwise required by the provisions of RCW 62A.9A-301 through 307. In the event that any portion of this Agreement conflicts with applicable law, such conflict will not affect other provisions of this Agreement that can be given effect without the conflicting provision, and to this end the provisions of this Agreement are declared to be severable.

Section 6.14 Successors and Assigns This Agreement will be binding upon and inure to the benefit of the successors and permitted assigns of Customer and Seattle Bank.

Section 6.15 Amendment and Restatement of Any Prior Agreement This Agreement amends and restates the terms of, and is not a novation of, any previous agreements between the parties or their predecessors entitled "Advances, Security and Deposit Agreement," "Deposit Account Resolution" or "Advances Agreement, Pledge Agreement and Security Agreement." This Agreement shall not release or impair the priority position of any existing Collateral for any existing Collateral securing any existing Indebtedness.

NOTICE: ORAL AGREEMENTS OR ORAL COMMITMENTS TO LOAN MONEY, TO EXTEND CREDIT OR TO FORBEAR FROM ENFORCING REPAYMENT OF A DEBT ARE NOT ENFORCEABLE UNDER WASHINGTON LAW.

IN WITNESS WHEREOF, Customer and Seattle Bank have caused this Agreement to be signed in their names by their duly authorized officers as of the date first above mentioned.

Central Pacific Bank

(Full Corporate Name of Customer)

By: /s/ Neal Kanda
(Signature of Authorized Officer)
Neal Kanda
(Name of Authorized Officer)
President and Chief Operating Officer
(Title of Authorized Officer)

and

By: /s/ Denis Isono
(Signature of Authorized Officer)
Denis Isono
(Name of Authorized Officer)
Executive Vice President
(Title of Authorized Officer)

FEDERAL HOME LOAN BANK OF SEATTLE

By: /s/ Dale Jeschke
(Signature of Authorized Officer)
Dale Jeschke
(Name of Authorized Officer)
Vice-President
(Title of Authorized Officer)

CORPORATE ACKNOWLEDGMENT

STATE OF Hawaii (State Where Signed)
) ss.
COUNTY OF Honolulu (County Where Signed)

I certify that I know or have satisfactory evidence that Neal Kanda (Name of Authorized Officer of Customer) is the person who appeared before me, and said person acknowledged that [he/she] signed this instrument, on oath stated that [he/she] was authorized to execute the instrument and acknowledge it as the President and Chief Operating Officer (Title of Authorized Officer) of Central Pacific Bank (Full Corporate Name of Customer) to be the free and voluntary act of such party for the uses and purposes mentioned in the instrument.

12/9/04
(Date of Notary Acknowledgement)

/s/ Stephanie T. Katayama
(Signature of Notary)
Stephanie T. Katayama
(Please print notary's name legibly.)

NOTARY PUBLIC in and for the State of Hawaii, residing at Honolulu, Hawaii. (City Where Notary Resides)
My commission expires: 7/1/2008.

(Include notary seal in space above this line.)

CORPORATE ACKNOWLEDGMENT

STATE OF Hawaii (State Where Signed)
) ss.
COUNTY OF Honolulu (County Where Signed)

I certify that I know or have satisfactory evidence that Denis Isono (Name of Authorized Officer of Customer) is the person who appeared before me, and said person acknowledged that [he/she] signed this instrument, on oath stated that [he/she] was authorized to execute the instrument and acknowledge it as the Executive Vice President (Title of Authorized Officer) of Central Pacific Bank (Full Corporate Name of Customer) to be the free and voluntary act of such party for the uses and purposes mentioned in the instrument.

12/9/04
(Date of Notary Acknowledgement)

/s/ Stephanie T. Katayama
(Signature of Notary)
Stephanie T. Katayama
(Please print notary's name legibly.)

NOTARY PUBLIC in and for the State of Hawaii, residing at Honolulu, Hawaii. (City Where Notary Resides)
My commission expires: 7/1/2008.

(Include notary seal in space above this line.)

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Section 3: EX-31.1 (EXHIBIT 31.1)

Exhibit 31.1

**Certification of the Chief Executive Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Ronald K. Migita, Chairman, President & Chief Executive Officer of Central Pacific Financial Corp. (the "Company"), certify that:

- (1) I have reviewed this quarterly report on Form 10-Q of the Company;
- (2) Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Company as of, and for, the periods presented in this quarterly report;
- (4) The Company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the Company and we have:
 - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our

supervision to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

- (b) evaluated the effectiveness of the Company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this quarterly report based on such evaluation; and
 - (c) disclosed in this quarterly report any change in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting; and
- (5) The Company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Company's auditors and the audit committee of the Company's board of directors (or persons performing the equivalent functions):
- (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Company's ability to record, process, summarize and report financial information; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Company's internal control over financial reporting.

Date: November 7, 2008

/s/ Ronald K. Migita
Ronald K. Migita
Chairman, President & Chief Executive Officer

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Section 4: EX-31.2 (EXHIBIT 31.2)

Exhibit 31.2

Certification of the Principal Financial and Accounting Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Dean K. Hirata, Vice Chairman and Chief Financial Officer of Central Pacific Financial Corp. (the "Company"), certify that:

- (1) I have reviewed this quarterly report on Form 10-Q of the Company;
- (2) Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Company as of, and for, the periods presented in this quarterly report;
- (4) The Company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the Company and we have:
 - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
 - (b) evaluated the effectiveness of the Company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this quarterly report based on such evaluation; and
 - (c) disclosed in this quarterly report any change in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting; and
- (5) The Company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Company's auditors and the audit committee of the Company's board of directors (or persons performing the equivalent functions):
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Company's ability to record, process, summarize and report financial information; and

- (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Company's internal control over financial reporting.

Date: November 7, 2008

/s/ Dean K. Hirata
Dean K. Hirata
Vice Chairman and Chief Financial Officer
(Principal Financial and Accounting Officer)

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Section 5: EX-32.1 (EXHIBIT 32.1)

Exhibit 32.1

Certification of the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Quarterly Report of Central Pacific Financial Corp. (the "Company") on Form 10-Q for the period ended September 30, 2008 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Ronald K. Migita, Chairman, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material aspects, the financial condition and results of operations of the Company.

Date: November 7, 2008

/s/ Ronald K. Migita
Ronald K. Migita
Chairman, President & Chief Executive Officer

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

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Section 6: EX-32.2 (EXHIBIT 32.2)

Exhibit 32.2

Certification of the Principal Financial and Accounting Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Quarterly Report of Central Pacific Financial Corp. (the "Company") on Form 10-Q for the period ended September 30, 2008 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Dean K. Hirata, Vice Chairman and Chief Financial Officer, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material aspects, the financial condition and results of operations of the Company.

Date: November 7, 2008

/s/ Dean K. Hirata
Dean K. Hirata
Vice Chairman and Chief Financial Officer
(Principal Financial and Accounting Officer)

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

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