Cascade Financial
CORPORATION

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UST Seq. #65

March 4, 2009

Mr. Neil M. Barofsky
Special Inspector General
Trouble Asset Relief Program
1500 Pennsylvania Ave. NW, Suite 1064
Washington, DC 20220

Dear Mr. Barofsky,

In response to your letter of February 6, 2009, Cascade Financial Corporation (Cascade) has employed the $39 million that we received from the issuance of preferred shares to the U.S. Treasury to better serve our customers' credit needs, while at the same time bolstering our capital position.

In reference to your specific questions:

(1)(a) Anticipated use of TARP funds

At the time that Cascade applied for TARP funding, our risk based capital ratio was 10.36%. We were therefore constrained for originating new loans for our portfolio, especially those that carry a risk weighting of 100%. Also, there was and is a perception that banks, such as Cascade, with high concentrations of commercial real estate loans would be mandated by the FDIC to have risk based capital at a level exceeding 10%, perhaps 12% or even higher.

Our ability to issue the Treasury preferred stock equal to 3% of our risk weighted assets, improved our risk based capital ratio to over 13%. Again, this infusion gave Cascade the wherewithal to continue to meet its customers' credit needs by growing its loan portfolio.

(1)(b) Segregation of TARP funds

The funds acquired through the Capital Purchase Program have been used to increase our capital. We have not segregated the cash that we received, but have used the additional capital to increase our lending activities.

(1)(c) Actual Use of TARP funds

During the fourth quarter of 2008, Cascade increased its total loans outstanding by $41 million from October 31st to December 31, 2008. As the attached table indicates, a level

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of growth that would not have been possible without the issuance of the senior preferred stock. Without the senior preferred stock, the theoretical maximum amount of loan growth would have been $16 million, which would have taken us to our internal guideline for our minimum ratio of risk based capital at 10.50%. If a 12% risk based capital standard had been applied, we would have had to shrink our loan portfolio.

(1)(d) Expected Use of TARP funds

We expect to continue to prudently leverage our preferred equity and our entire capital base to meet our customers' credit needs. [redacted] b(4)

(2) Limits on Executive Compensation

As of the enclosed the draft from the Compensation Discussion and Analysis (CDA) that is part of our 2008 Proxy Statement, which shall be submitted March 24, 2009, Cascade has taken the required steps to meet the requirements by our participation in the Capital Purchase Program. The steps taken by Cascade include:

The modification of existing employment contracts and change of control agreements to prohibit the payment of golden parachutes; provide claw back provisions for any payment made based upon statements of earnings or other criteria that have been proven to be materially inaccurate.

Cascade's Compensation Committee has reviewed the Corporation's incentive programs to ensure that they do not encourage unnecessary and excessive risk taking. As part of the CDA , the Compensation Committee has certified that this review has occurred.

As mandated by the Participation Agreement, I have provided the CEO certification that the original risk analysis had been completed. In addition, I provided the First Fiscal Year Certification, as well. Both certifications are embodied in the CDA statement.

Cascade is reviewing the compensation provisions pertaining to the recipient's of TARP funds contained in the recently enacted in the American Reinvestment and Recovery Act. Cascade is committed to changing all its compensation policies, procedures, and agreements to be in compliance with the Act.

Cascade is committed to complying with the provisions of the American Recovery and Reinvestment Act of 2009 when the final rules are issued by the Treasury Department.

While Cascade does not have any single family loans currently in the process of foreclosure, we are taking steps to assure we have procedures in place to deal if we reach that point with any of our borrowers. We are studying the new Freddie Mac guidelines in reference to residential mortgage refinancing and loan modifications.

I certify the accuracy of all statements, representations, documentation and supporting information.

Lars H. Johnson

Lars H. Johnson
EVP & CFO
Cascade Financial Corporation

CASCADE FINANCIAL CORP

Month-End Balances
(in 000s)

		WITH TARP FUNDS		NO TARP FUNDS	
	PRE-TARP Oct-08	POST-TARP Dec-08	ACTUAL GROWTH	ESTIMATE NO TARP Dec-08	Max GROWTH NO TARP
TOTAL Assets	1,574,335	1,637,904	63,569	1,590,335	16,000
Total Loans	1,217,273	1,258,242	40,969	1,233,273	16,000
TAF Borrowings	30,400	30,000	(400)	30,000	
TARP Preferred	0	39,020	39,020		
TOTAL Capital	119,900	160,811	40,911	121,791	1,891
EST. Risk-Based CAPITAL RATIO	10.32%	13.19%		10.50%	

PROPOSAL 2 – ADVISORY (NON-BINDING) VOTE ON EXECUTIVE COMPENSATION

On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act of 2009 into law. The Act includes a provision, commonly referred to as "Say-on-Pay," that amends existing law and requires a TARP recipient to: "permit a separate shareholder vote to approve the compensation of executives, as disclosed pursuant to the compensation disclosure rules of the Commission (which disclosure shall include the compensation discussion and analysis, the compensation tables, and any related material)." We are a TARP recipient because of our participation in the U.S. Department of the Treasury's Capital Purchase Program, pursuant to which we issued preferred stock and warrants to purchase our common stock to the Treasury. See section titled Employment/Change of Control/Severance Agreements – Compliance with the U.S. Treasury Department's Capital Purchase Program.

We are providing you the opportunity, as a shareholder, to endorse or not endorse our executive pay program and policies through the following resolution:

"RESOLVED, that the shareholders approve the compensation of executive officers as described in the Compensation Discussion and Analysis and the tabular disclosure regarding named executive officer compensation (together with the accompanying narrative disclosure) in this Proxy Statement."

As provided in the Act, the vote is not binding on the board of directors and may not be construed as overruling a decision by the board of directors, nor creating or implying any additional fiduciary duty by the board of directors, nor be construed to restrict or limit the ability of shareholders to make proposals for inclusion in proxy materials related to executive compensation.

We believe that our compensation policies and procedures are strongly aligned with the long-term interests of our shareholders. Because your vote is advisory, it will not be binding upon the Board. However, the Compensation Committee will take into account the outcome of the vote when considering future executive compensation arrangements.

THE BOARD UNANIMOUSLY RECOMMENDS A VOTE "FOR" APPROVAL OF THE COMPENSATION OF EXECUTIVE OFFICERS AS DESCRIBED IN THE COMPENSATION DISCUSSION AND ANALYSIS AND THE TABULAR DISCLOSURE REGARDING NAMED EXECUTIVE OFFICER COMPENSATION (TOGETHER WITH THE ACCOMPANYING NARRATIVE DISCLOSURE) IN THIS PROXY STATEMENT.

COMPLIANCE WITH SECTION 16(a) OF THE EXCHANGE ACT

Based upon a review of reports and written representations furnished to it, the Company believes that during fiscal year 2008, all filings with the Securities and Exchange Commission by its executive officers and directors complied with requirements for reporting ownership and changes in ownership of the Company's common stock pursuant to Section 16(a) of the Securities Exchange Act of 1934.

REPORT OF COMPENSATION COMMITTEE

COMPENSATION DISCUSSION AND ANALYSIS

Philosophy

The purpose of Cascade Financial Corporation's (the Company) Executive Compensation Philosophy is to ensure that the Company is able to attract, retain and motivate highly skilled executives. It is the philosophy of the Company that executive compensation be tied to corporate and individual performance. The Company's executive compensation package consists of base salary, short-term incentives, long-term incentives and benefits.

Specifically, the compensation philosophy is to target base salaries near the median (50th percentile) and target total compensation (including annual incentives, long-term incentives, and benefits) near the 75th percentile of a regional peer group of bank holding companies similar in size and performance to Cascade Financial Corporation. The Company believes targeting total compensation near the 75th percentile is critical for attracting and retaining the qualified executives it needs to achieve its business objectives. Executives will be paid near the 75th percentile depending on their achievement of corporate and individual performance goals.

The goals established in the compensation plans flow directly from the Company's Strategic Plan and/or its Board approved Annual Profit Plan. Such goals address Company-wide objectives such as total net income, growth in net income as well as growth on a per share basis, and profitability measures such as return on equity, return on assets, and operating efficiency ratio. In addition, sales goals are established such as the level of loans and deposits as well as an emphasis on credit quality. The Company's policies also seek to align and balance the interests of shareholders, employees and customers by employing a mix of base salary, incentive compensation and stock based awards.

The Company has utilized stock options as part of its strategy to align the interests of stockholders and employees. The Company recognizes that if the stock does not appreciate, the options would have little or no value. If the stock price increases, then the option holders/employees would benefit as would all shareholders.

As an issuer of Preferred Stock to the U.S. Treasury, the Company has agreed to meet all the requirements regarding executive compensation embodied in the Securities Purchase Agreement entered into between the Company and the U.S. Treasury. The Company's existing employment and change of control agreements have been modified to comply with the restrictions related to executive compensation.

These modifications include the prohibition from making a golden parachute payment to any Senior Executive Officer as long as any debt or equity securities issued by the Company are held by the Treasury (the "CPP Covered Period"). Also included is the ability, during the CPP Covered Period for the Company to "claw back" any payment made to the Executive if the payment is later determined to have been based on any materially inaccurate financial statements or any other materially inaccurate metric criteria within the meaning of Section 111(b)(2)(B) of the Emergency Economic Stabilization Act.

In addition, the Compensation Committee is required to annually review its incentive plans to ensure that they do not encourage Senior Executive Officers to take unnecessary and excessive risks that threaten the value of the Company. This assessment was completed on February 9, 2009, in conjunction with the Bank's Chief Risk Officer. The Compensation Committee reviewed the incentive structures for the Bank's Senior Executive Officers and found no indicators of the aforementioned risk contained in the Bank's incentive structures. Thus, the Compensation Committee did not believe it was necessary to modify the Bank's incentive structures at this time.

Authority

The Board has delegated to the Compensation Committee the responsibility to establish and administer policies that govern executive compensation for the Company. The Committee evaluates the individual performance of the President and Chief Executive Officer after receiving feedback from the entire Board. The Committee receives input from the President on the other executive officers' performance and has final authority to set individual compensation levels.

The Committee is charged with monitoring and analyzing conditions and changes in the market for executive talent. The Committee has the discretion to employ any consulting assistance it deems necessary to accomplish this task.

The Committee considers a variety of subjective and objective factors in determining the total compensation for individual executives. These factors include the performance of the Company overall, the responsibilities assigned to each executive, and the performance of each executive in their assigned areas of oversight. (The executive officers of the Company are the President and CEO, the EVP/Chief Financial Officer, as well as the EVPs of Commercial Banking and Retail Banking, the EVP/Chief Credit Officer and the EVP/ Chief Administrative Officer of Cascade Bank.)

The Committee evaluates the performance of the President and CEO and determines her total compensation, which is ratified by the full Board. The President and CEO negotiates goals and objectives with each executive officer to develop a performance scorecard. That scorecard is reviewed by the Compensation Committee quarterly and the scorecard for the following year is reviewed during the fourth quarter of the preceding year (see "Compensation of Named Executives."). Each executive's performance is then measured against that scorecard over the course of the year. The President and CEO administers the appropriate level of incentive payments based on performance, for each executive within a range of payouts that were approved by the Committee.

Components

By mixing base pay with a component of pay for performance, the Company seeks to be competitive, but prudent, in its compensation practices. The Company augments its cash compensation, which is designed to incentivize current performance, with stock option grants, which offer long-term incentives.

The Company does not offer its executives and board members many perquisites, believing that direct compensation is in the best interests of both the employees and shareholders. Direct compensation, which includes cash compensation and the economic value of long-term incentive compensation, is more efficient and cost effective to administer and more transparent to monitor. The largest component of "Other Income" on Table 1 is the Company's 401(k) match that is available to all employees.

Base Salary. Salary levels are analyzed against the banking industry based on a peer group review of twenty West Coast financial institutions. The analysis, as well as the achievements of the Company and the individual employees, are available to the Compensation Committee and are used when considering salary adjustments. Base salaries are set within the framework of the Company's compensation philosophy as previously discussed.

Incentive Programs. An incentive plan is in effect for the executive officers of the Company that is designed to compensate for performance as defined by meeting the goals established in the scorecard. In determining the amount of the President and CEO's incentive, the Compensation Committee considers the Company's earnings, return on equity, asset quality, the President and CEO's leadership and other factors as it deems appropriate. The plan for all other executive officers is based upon the attainment of certain negotiated goals including Company and line of business profitability; loan levels and credit quality; expense management; as well as service, leadership and teamwork. Performance for these officers is evaluated by the President and CEO and reviewed by the Compensation Committee.

Option Grants. The 2003 Long-Term Incentive Plan (the Plan) grants the Company the ability to offer equity based compensation including restricted stock and/or stock options. The Company has established a stock option grant policy. Stock options are designed to provide long-term incentives for key employees. These grants were made at current market prices under the rules of the Plan adopted by the shareholders. Option grants are generally made each year at the March Board meeting. The amount of total options available for grant is based upon the attainment of specific financial objectives, specifically the growth in net income. Under the American Recovery and Reinvestment Act of 2009 ("ARRA"), no stock options can be granted to the senior executive officers (SEOs) during the time a TARP recipient has outstanding obligations to the Federal government arising from its financial assistance (the "TARP Period").

Deferred Compensation Plan. One of the major projects of the Compensation Committee in 2007 was to develop and recommend to the Board of Directors a non-qualified deferred compensation plan that would provide specified benefits to a select group of management and highly compensated employees. On January 16, 2008 the Cascade Bank Non-Qualified Deferred Compensation Plan ("Plan") was adopted by the Board of Directors, with an effective date of February 1, 2008. This Plan replaced an earlier deferred compensation plan which had been inactive since 2006. Under the terms of the Plan, participants may contribute up to 50 percent of base salary and 100 percent of the annual incentive bonus to the Plan. In addition, the Compensation Committee has the authority to authorize an employer contribution to the Plan for these same participants. The contribution will be based upon the performance of the Company as well as the individual performance of each participant. The Non-Qualified Deferred Compensation Plan will also be available to directors of the Company. Each director may contribute up to 100 percent of their director compensation to the Plan. No Company contributions will be made for directors.

Pension and Post-Retirement Benefits. Currently, the Company does not have a pension plan for any of its employees. Other than those contained within the President and CEO's employment agreement, the Company does not offer post-retirement benefits.

Perquisites. The Company applies the same matching formula for 401(k) contributions for all employees, 50% of an employee's contribution up to a maximum of $6,000. All executive officers are granted five weeks of vacation annually. Ms. Nelson receives a car allowance of $8,400 per annum.

Stock Option Grants

As a general policy, the Compensation Committee will consider incentive stock option grants to key employees on an annual basis based upon the attainment of company-wide and individual goals. The current policy provides that stock options will be granted to existing employees only when the Company's earnings per share increases by at least ten percent (10%) over the prior year. In the event the Company's net income growth meets that requirement, the Committee will award incentive stock options to existing employees according to a formula established to keep the Company's options practices consistent with industry norms. For example, if net income grows by 10%, the options granted will equal .4% of the outstanding shares. The maximum annual number of stock options granted to existing employees would be .8% of outstanding shares and would occur if net income increased by 15% or more on a year over year basis. Based upon the application of this policy a pool of available stock options may be created and discretionary awards can then be made to eligible participants of that pool.

The Committee may make discretionary individual stock option grants after receiving and considering the recommendations of the President and CEO. The grants will be based primarily on each employee's contribution to the Company's success in meeting or exceeding its goals. The Committee may also grant options upon the employment of selected senior level employees.

During 2008, 97,382 incentive options were granted as the Company's earnings per share growth exceeded the 10% threshhold in 2007. No incentive options will be granted in 2009 for the year 2008, because the 10% net income threshold was not met. This decision is consistent with the general policy as stated previously. The strike price of all option grants is the closing price of Cascade Financial stock (CASB) on the date of the grant.

Under the program adopted in 2003, incentive stock options vest over a five-year period, with 10% vesting at the end of year 1, 20% vesting per year at the end of years 2, 3, and 4, and 30% at the end of year 5. Previously, the vesting schedule was 6 years, with 20% vested after year 2, and 20% per year in years 3 through 6.

Vested options may be exercised at any time prior to their expiration at the discretion of the option holder. The Company also allows the holder to exercise options by tendering outstanding shares of the Company's stock. The value of that stock is determined by using the average closing price of the Company's stock for the ten previous trading days prior to the tender.

As of December 31, 2008, options to purchase a total of 656,883 shares remain available for issuance under the Plan. The following table sets forth information regarding outstanding options and shares reserved for future issuance under the equity compensation plans as of February 17, 2009.

Plan Category	**Number of Shares to be Issued Upon Exercise of Outstanding Options** *(in thousands)*	**Weighted Average Exercise Price of Outstanding Options**	**Number of shares Remaining Available for Future Issuance** *(in thousands)*
Equity compensation plans approved by shareholders—1997 Plan	236	$ 5.01	-
Equity compensation plans approved by shareholders—2003 Plan	421	13.44	505
Equity compensation plans not approved by shareholders	-	-	-
Total	657	$ 10.41	505

In 2007, the Company adopted its "Real Rewards" Program, which granted each employee that met individual performance criteria 25 shares of restricted stock, which vest after three years, provided that the Company meets the financial objectives established by the Board of Directors under the program. The Compensation Committee determined that those objectives were met in 2007 and granted 137 employees the 25 shares of restricted stock, which had a closing price of $10.19 per share as of the date of the grant, on May 9, 2008.

Pension Benefits and Deferred Compensation

The Company does not have a defined benefit pension program. It offers all its employees a 401(k) in which the Company will match 50% of the employee's contribution up to $6,000 on an annual basis.

The CEO's employment agreement states that if Ms. Nelson retires after age 57, she is entitled to receive a retirement benefit equal to two times her base compensation plus incentive before salary deferrals over the 12 month period prior to her retirement, the vesting of all her stock options and health care benefits until she and her spouse become entitled to receive Medicare benefits or until she reaches age 65, whichever occurs first.

Summary

The Company seeks a balance of base salary and pay for performance in the form of incentive payments. Stock option grants have been used to help align the long-term interests of the employees and the shareholders. As a TARP recipient, the Company will comply with the provisions of ARRA which prohibit paying the SEOs any bonus, retention or incentive compensation other than certain long-term restricted stock that (a) does not fully vest during the TARP Period, (b) has a value not greater than one-third of the total annual compensation of the employee receiving the stock, and (c) is subject to such other restrictions as the Treasury may determine are in the public interest. The Company will not issue any stock option grants as long as any debt or equity securities issued by the Company are held by the Treasury (the "CPP Covered Period").

Compensation of the Chief Executive Officer. Carol K. Nelson was appointed Chief Executive Officer of Cascade Financial Corporation on May 1, 2002. Previously, Ms. Nelson was President and Chief Operating Officer of Cascade Financial Corporation. Ms. Nelson remained President and Chief Executive Officer of Cascade Bank. For the year ended December 31, 2008, Ms. Nelson's base compensation was $263,050. Ms. Nelson's salary was set by the Compensation Committee in January of 2008 based upon the philosophy of the committee to target salaries near the median (50th percentile) as well as considering her individual performance related to the achievement of the goals set by the Board in it's Strategic Plan. The Committee also used information provided by it's consultant, Almalfi Consulting in determining the appropriate compensation based upon a group of twenty companies chosen as our "benchmark group".

The Compensation Committee retains the discretion to determine any incentive paid to the CEO. It is the Committee's intent to pay an incentive, subject to the achievement of targeted levels of performance covering net income, level of earnings per share, and return on equity. The targeted incentive the Committee has agreed to use is 1.5% of net profit before tax excluding any extraordinary items according to generally accepted accounting principles (GAAP). For the year ended December 31, 2008, Ms. Nelson received an incentive of $24,765. Ms. Nelson was awarded on March 25, 2008, 15,000 incentive stock options with an exercise price of $12.63. Ms. Nelson also received 25 shares of restricted stock as part of the "Real Rewards" Program which had a closing price of $10.19 per share on the date of the grant. The Committee believes this compensation is consistent with the Company's compensation philosophy given the Company's level of profitability, complexity and asset size compared to the benchmark group.

Compensation of Named Executives. Lars H. Johnson, EVP—Chief Financial Officer, Steven R. Erickson, EVP—Commercial Banking, Debbie E. McLeod, EVP—Retail Banking, and Robert G. Disotell, EVP—Chief Credit Officer are the named executives.

The level of total compensation for the named executives is targeted to be competitive with comparable financial institutions for positions of similar scope and responsibility—see Benchmarks. The components of total compensation reflect the nature of the position, e.g. those employees with a higher component of sales in his/her goals will generally have a higher component of compensation in incentive payments. In 2008, Mr. Johnson and Ms. McLeod had approximately 30% of their maximum compensation in the form of a potential incentive and Mr. Disotell had approximately 23% of compensation in the form of potential incentive. Mr. Erickson, who has loan production responsibility, in addition to his sales and general management responsibilities, had 33% of his maximum compensation in the form of an incentive.

Annually, each executive negotiates with the President/CEO a balanced scorecard with targets based upon the Company's goals and his/her position's responsibilities. Each executive has a component of his/her incentive calculation based upon leadership, teamwork and expense control as well as the attainment of personal, business unit, and/or Company goals. Most scorecards include a category of additional negotiated items which typically include specific improvement goals for the year that affect departments under each Senior Executive Officer's management. Those Senior Executive Officers dealing with credit also have at least a twenty percent credit quality component to mitigate production risks. This system of checks and balances mitigates the risk of both the production and decision-making side of lending at the Bank, thus keeping risks in alignment with the Bank's risk policies.

The incentive payments for 2008 reflect the quantitative progress toward those goals. The following table provides the percentages assigned to various goals of each named executive.

Named Executive	Expense Management %	Sales %	Service/Leadership %	Credit Quality/Other %
Lars H. Johnson	20	20	40	20
Steven R. Erickson	0	40	40	20

Named Executive	Expense Management %	Sales %	Service/Leadership %	Credit Quality/Other %
Debbie E. McLeod	20	40	40	0
Robert G. Disotell	15	0	40	45

Benchmarks

With the assistance of Amalfi Consulting, the Company has established a group of 20 bank holding companies as a benchmark universe to compare the compensation levels for senior management and the Board of Directors. These companies are publicly traded, headquartered in Washington, Oregon or California, and with total assets ranging from $745 million to $4.5 billion. As of December 31, 2008, the Company had consolidated assets of $1.64 billion. By asset size, Cascade Financial Corporation would be the seventh largest institution among the selected peers. Benchmarking is at the direction of the Compensation Committee. The Committee is responsible for selecting the independent outside company to perform the survey as well as determining the frequency of the survey and the appropriate peer group.

Base salaries are targeted near the median (50th percentile) and target total compensation (including annual incentives, long-term incentives, and benefits) at or near the 75th percentile of the benchmark group provided the Company's overall performance is also at or near the 75th percentile of the benchmark group.

For 2008, base salaries for the named executives were adjusted toward the median of the benchmark group if such adjustments were warranted. Relative performance of the Company and compensation of the named executives will be reviewed by the Compensation Committee in 2009 when the compensation data for the benchmark group becomes available. As of March 1, 2009 none of the named executives, except EVP Steve Erickson, have been awarded any increase to base salary for 2009. Mr. Erickson took over responsibility for Business Banking as well as his current responsibility for Real Estate Lending. His new title is EVP of Commercial Banking. It was the decision of the Committee that these added responsibilities warranted an increase in annual salary of 5.46% or $9,039.

The following table lists peer groups of 20 publicly traded financial institutions that are comparable to Cascade Financial Corporation in asset size, geography, and performance.

COMPANY NAME	TICKER	CITY	STATE
Banner Bank	BANR	Walla Walla	WA
Frontier Financial Corporation	FTBK	Everett	WA
Columbia Banking System, Inc.	COLB	Tacoma	WA
West Coast Bancorp	WCBO	Lake Oswego	OR
Cascade Bancorp	CACB	Bend	OR
AmericanWest Bancorporation	AWBC	Spokane	WA
Farmers & Merchants Bancorp	FMCB	Lodi	CA
Heritage Commerce Corp	HTBK	San Jose	CA
Horizon Financial Corp.	HRZB	Bellingham	WA
City Bank	CTBK	Lynnwood	WA
Sierra Bancorp	BSRR	Porterville	CA
Venture Financial Group, Inc.	-	Du Pont	WA
PremierWest Bancorp	PRWT	Medford	OR
Columbia Bancorp	CBBO	The Dalles	OR
Bank of Marin Bancorp	BMRC	Novato	CA
Rainier Pacific Financial Group	RPFG	Tacoma	WA
San Joaquin Bancorp	SJQU	Bakersfield	CA
Riverview Bancorp, Inc.	RVSB	Vancouver	WA
Bridge Capital Holdings	BBNK	San Jose	CA
Heritage Oaks Bancorp	HEOP	Paso Robles	CA

Employment/Change of Control/Severance Agreements

The following is a brief description of each agreement entered into by the Bank with named executive officers that provide potential payments upon termination or a change of control.

Employment Agreement. The Bank entered into an employment agreement with Carol K. Nelson dated November 27, 2007, as modified effective November 21, 2008, to meet the requirements set by the Treasury discussed in this report, which replaced a previous agreement dated July 12, 2005. This agreement replaced a prior agreement dated March 26, 2002, and extended on January 27, 2004. The current agreement may be terminated upon 90 days written notice. The employment of Ms. Nelson is terminable at any time for cause as defined in the agreement, and she may be terminated without cause in which case she would receive a severance benefit equal to two times her annual base compensation plus incentive. Such payment would, at the option of the Bank, be made in a lump sum or in accordance with the Bank's regular payroll schedule and would commence as soon as practicable, but not less than six (6) months, after the date that Ms. Nelson's entitlement to such payments arose.

In the case that Ms. Nelson terminates her employment for "good reason," as defined in the agreement, Ms. Nelson would receive a severance benefit equal to two (2) times her base compensation plus incentive before salary deferrals over the twelve (12) months preceding the month of termination, less statutory payroll deductions. Such payment would, at the option of the Bank, be made in a lump sum or in accordance with the Bank's regular payroll schedule and would commence as soon as practicable, but not less than six (6) months, after the date that Ms. Nelson's entitlement to such payment arose.

The agreement also provides for the payment of severance benefits to Ms. Nelson in the event of her termination of employment following a change of control of the Company or the Bank. All of

Ms. Nelson's equity grants/benefits would become fully vested upon the effective date of the change of control. If Ms. Nelson left the employment of the Bank, whether voluntarily or involuntarily, within twelve (12) months after such change of control, Ms. Nelson would be entitled to receive an amount equal to two (2) times her base compensation plus incentive before salary deferrals over the twelve (12) month period prior to the change of control. Such payment would not be made less than six (6) months after Ms. Nelson's entitlement to the payment arose. During the term of the agreement and for twenty-four (24) months thereafter, if Ms. Nelson receives compensation due to a change of control, she would be prohibited from, directly or indirectly, soliciting or attempting to solicit: (i) any employees of the Bank to leave their employment; or (ii) any customers of the Bank to remove their business from the Bank to participate in any manner in any financial institution or trust company that competes with or will compete with the Bank in King, Snohomish or Pierce Counties, or any start-up or other financial institution or trust company in King, Snohomish or Pierce Counties.

The agreement also provides that, if Ms. Nelson retires after attaining the age fifty-seven (57), Ms. Nelson will receive a severance benefit in an amount equal to two (2) times her base compensation plus incentive before salary deferrals over the twelve (12) months prior to her retirement, with such amounts payable in twenty-four (24) consecutive, equal, monthly installments, with the first such payment due on the first day of the seventh month following her retirement. In addition, Ms. Nelson would be entitled to the vesting of all stock-based compensation and certain health benefits. During the term of the agreement and for twenty-four (24) months thereafter, if Ms. Nelson receives compensation due to her retirement after attaining the age of fifty-seven (57), she would be restricted from becoming or serving as an officer, director, founder or employee of any financial institution with its main office in King, Snohomish or Pierce Counties, or any other financial institution which, in the judgment of the Board, is in substantial competition with the Bank, unless Ms. Nelson had first obtained the Board's written consent. Furthermore, during the term of the agreement and for twenty-four (24) months thereafter, if Ms. Nelson receives compensation due to her retirement after age fifty-seven (57), she would be prohibited from, directly or indirectly, soliciting or attempting to solicit: (i) any employees of the Bank to leave their employment, or (ii) any customers of the Bank to remove their business from the Bank to participate in any manner in any financial institution or trust company that competes with or will compete with the Bank in King, Snohomish or Pierce Counties, or any start-up or other financial institution or trust company in King, Snohomish or Pierce Counties.

If termination of the agreement occurs due to Ms. Nelson's death, her estate would be entitled to receive, under her employment contract, only the compensation, benefits earned and expenses reimbursable through the date the agreement is terminated. If termination occurs due to Ms. Nelson's disability, Ms. Nelson would continue to receive her salary until payments under the Bank's long-term disability plan commenced, or in the event the Bank had no long-term disability plan on the date of disability, her salary would continue for a period of six (6) months. In the event of Ms. Nelson's death or disability while employed by the Bank, all of her then outstanding, stock-based compensation which had not vested would be accelerated and fully vested.

Change of Control/Severance Agreements for Named Executives. The Bank has entered into Change of Control/Severance Agreements dated November 30, 2007, and modified November 21, 2008, to meet the requirements set by the Treasury discussed in this report, which replaced prior agreements, with Lars H. Johnson, Steven R. Erickson, Debbie E. McLeod, Robert G. Disotell and another executive officer who is not a Named Executive Officer. These agreements generally provide that if for the period of time starting six (6) months prior to the date the Change of Control is effected and ending twenty-four (24) months after a Change of Control, if an executive is terminated other than for cause or the executive should terminate for good reason (as such terms are defined in the agreements), such executive will generally be entitled to: (i) receive a severance payment equal to two times the executive's annual base compensation plus incentive for the prior year, (ii) continued life, medical, dental and disability coverage substantially identical to the coverage maintained by the Bank for the executive prior to the effective date of a change of control for twenty-four (24) months after the effective date of a change of control, except to the extent such coverage may be changed in its application to all the Bank's employees on a nondiscriminatory basis; and (iii) the acceleration of any unvested stock-based compensation so any such stock-based compensation shall be 100% vested and immediately exercisable in full as of the date of such termination. Payments incident to a Change of Control would be paid to the executive in a lump sum no sooner than six (6) months after the date of the executive's termination. The agreements generally define a Change of Control as the acquisition of all or a substantial part of the Company or the Bank, the merger of the Company or the Bank into another company that is the surviving company, the sale of substantially all of the assets of the Company or the Bank to another company, or a hostile acquisition of substantially all of the stock of the Company or the Bank.

At December 31, 2008 in the event of a Change of Control, the potential payout (if all executives were terminated) would have been $2,402,149. Details on an executive-by-executive basis, of the estimated compensation and benefits that would be provided to each named executive officer in the event that such executive officer's employment is terminated are located on pages 27-31 of this report.

<u>Compliance with the U.S. Treasury Department's Capital Purchase Program</u>

Prohibition on Incentive Compensation Encouraging Excessive Risk

The guidance from the Treasury outlines a procedure for institutions that participate in the Capital Purchase Program, i.e. issue Preferred Stock to the U.S. Treasury, to establish procedures to assure the compliance with the prohibition on incentive compensation programs that encourage Senior Executive Officers (SEOs) to take unnecessary and excessive risk that threatens the value of the financial institution.

The Company's Compensation Committee has completed its assessment of whether the incentive plans of the Company encourage or reward unnecessary and excessive risk. In the process of preparing its assessment, the Compensation Committee met with the Company's Chief Risk Officer and reviewed the incentive structure for each of the Company's SEOs. The Committee found no indicators of the aforementioned risks contained in the Company's incentive structures.

To arrive at its determination, the Committee reviewed the components of each SEO's incentive plan. The structure of each SEO's incentive is based upon performance detailed in each individual's scorecard, with the exception of the Company's CEO. The scorecards in all cases include at least a 40% weighting on service and leadership. Most scorecards include a category of negotiated items, which typically include goals specific for that division's operations during the year. The scorecard for SEOs with credit responsibility also contained a credit quality component of at least 20%.

The CEO's contract, as approved by the Board of Directors, also contains goals such as leadership and is balanced with specific measurable metrics that keep the incentives consistent with the goals elucidated in the Company's strategic plan.

Each SEO has signed an Agreement to Amend Compensation Arrangements that prohibits Golden Parachutes, provides for the recovery of Incentive Compensation (clawbacks) and acknowledging that participation in the Capital Purchase Program may require the modification of any and all aspects of that person's compensation. Each SEO's Change of Control and Severance Agreement was also modified to be consistent with requirements of the Capital Purchase Program.

No Senior Executive Officer received total compensation in 2008 in excess of $500,000. Under certain circumstances, the Company's Chief Executive Officer, could, in one year, receive total compensation in excess of $500,000. To comply with the compensation requirements applicable to companies participating in the Capital Purchase Program, the Company has agreed to limit its deduction for compensation paid to any Senior Executive Officer to the $500,000 per annum limit.

The Compensation Committee will be responsible for the implementation of any additional changes to the Company's compensation and incentive programs that may be required in the future under regulations promulgated under the Capital Purchase Program.

Compensation of the Board of Directors

The goal of Cascade Financial Corporation's Director Compensation Philosophy is to ensure that the Company is able to attract, motivate and reward qualified directors. The Corporate Governance and Nominating Committee is responsible for developing recommendations to the full Board regarding director compensation. To create a focus on long-term success and reduce any conflict of interest, the compensation for the Board of Directors is limited to a set fee for service. Total director compensation consists of a retainer, meeting fees and an equity grant.

Specifically, the compensation philosophy is to target total compensation near the median (50^{th} percentile) of the regional peer group of bank holding companies similar in size and performance to Cascade Financial Corporation. Compensation may vary per individual based upon role (e.g. committee chairs may receive additional compensation to reflect additional responsibilities). The regional peer group is identical to that used by the Compensation Committee for executive officers.

For the year ended December 31, 2008, all members of the Board received an $18,000 annual retainer and $9,000 annual meeting fee. The Chair of the Board (Dr. Murphy) received an additional fee of $18,000 per year. As an additional annual fee, the Chair of the Audit and Finance Committee (Mr. Anderson) received $12,000, the Chair of Compensation Committee (Ms. Halladay) received $8,000, the Chair of the Loan Committee (Mr. O'Connor) received $6,000, and the Chair of the Corporate Governance and Nominating Committee (Mr. Duce) received $6,000. All members of the Loan Committee received an additional $6,000 per annum. Each director also received 1,032 shares of restricted Cascade Financial Corporation stock worth approximately $12,000.

Compensation and Personnel Interlocks and Insider Participation

No member of the Compensation Committee is an executive officer or former officer of the Company. No executive officer of the Company served on the board of directors of any entity whose executive officers included a director of the Company.

The Compensation Committee met the requirement as prescribed in the Securities Purchase Agreement entered into between the Company and the U.S. Treasury to complete an assessment of the bonus/incentive plans to ensure that they did not encourage Senior Executive Officers to take unnecessary and excessive risks that threaten the value of the Company. This assessment was completed on February 9, 2009 which was within the 90 day period, as required by the Treasury, of the receipt of TARP funds.

As of March 9, 2009, the Compensation Committee has reviewed and discussed the Compensation Discussion and Analysis included in this Proxy Statement with management of the Company, and based upon those discussions, the Committee has recommended to the Company's Board of Directors that the Compensation Discussion and Analysis be included in this Proxy Statement.

COMPENSATION COMMITTEE

Janice E. Halladay, Chair
David W. Duce, Vice Chair
Jim Gaffney
Dwayne R. Lane
Katherine M. Lombardo

CEO Certification

"I, Carol K. Nelson, certify, based on my knowledge, that the Compensation Committee of Cascade Financial Corporation has reviewed within 90 days of the Department of the Treasury's purchase of the Preferred Stock of Cascade Financial under the Capital Purchase Program the incentive compensation arrangements of the Senior Executive Officers (SEOs), as defined in subsection 111(b)(3) of the Emergency Economic Stabilization Act of 2008 and regulations and guidance issued thereunder, of Cascade Financial with senior risk officers of Cascade Financial Corporation to ensure that the SEO incentive compensation arrangements do not encourage the SEOs to take unnecessary and excessive risks that threaten the value of Cascade Financial Corporation."

Carol K. Nelson
President and CEO

First Fiscal Year Certification:

"I, Carol K. Nelson, certify, based on my knowledge, that:

(i) The Compensation Committee of Cascade Financial Corporation met in February 2009 with the senior risk officer to discuss and review the relationship between the risk management policies and practices of Cascade Financial Corporation and the incentive compensation arrangements of the Senior Executive Officers (SEOs), as defined in subsection 111(b)(3) of the Emergency Economic Stabilization Act of 2008 (EESA) and regulations and guidance issued thereunder to ensure that the SEO incentive compensation arrangements do not encourage the SEOs to take unnecessary and excessive risks that threaten the value of Cascade Financial Corporation; (ii) The Compensation Committee of Cascade Financial Corporation has certified to the review of the SEO incentive compensation arrangements required under (i) above; (iii) Cascade Financial Corporation has required that SEO incentive compensation be subject to recovery or "clawback" by Cascade Financial Corporation if the payments were based on materially inaccurate financial statements or any other materially inaccurate performance metric criteria; (iv) Cascade Financial Corporation has prohibited any golden parachute payment, as defined in the regulations and guidance issued under section 111(b) of EESA, to a SEO; (v) Cascade Financial Corporation has instituted controls and procedures to limit the deduction for remuneration for federal income tax purposes to $500,000 for each SEO for the most recently ended fiscal year as if section 162(m)(5) of the Internal Revenue Code applied to Cascade Financial Corporation; and (vi) The following individuals are the SEOs for the current fiscal year: Robert Disotell, EVP/Credit Administration, Steven Erickson, EVP/Commercial Banking, Lars Johnson, EVP/Chief Financial Officer and Debbie McLeod, EVP/Retail Banking.

Carol K. Nelson
President and CEO