



10500 NE 8th St, Suite 1800
Bellevue, Washington 98004

Neil M. Barofsky
Special Inspector General
Troubled Asset Relief Program
1500 Pennsylvania Ave., N.W., Suite 1064
Washington, D.C. 20220

Dear Mr. Neil M. Barofsky,

As requested, we are providing you with the information you requested in your February 6, 2009 memo related to our use of the TARP funds received under the Capital Purchase Program.

(1)(a)

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- Second, given the current economic environment, the capital provides a capital cushion in the event of an unforeseen loss.

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(1)(b)

We are not segregating TARP funds. These funds are included in our pool of capital that we are leveraging to grow loans and continue serving our customers.

(1)(c)

We received TARP funds on January 16, 2009. We have booked \$6.6 million of new loan commitments since receiving funds through the end of February 2009. See Attachment 3 for detail of loans booked.



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(1)(d)

See (1)(a). (b) (4)

(2)

Senior executive compensation programs are in compliance with requirements stipulated for participation in the TARP Capital Purchase Program. The agreement to maintain compliance going forward that the four senior executives signed is attached (Attachment 4). The compensation programs for executives do not promote or encourage taking excessive risks including loan risks. The bank's performance demonstrates that the executive group is not encouraged to take excessive risks as the bank has had no nonperforming loans since its inception and was profitable for the full year and every quarter of 2008. In addition, the bank

b(4), b(8)

The senior executives' compensation structure is currently comprised of salary, bonus, and stock options and/or restricted stock grants.

b(4), b(8) b(4), b(8)

I, Philip I. Mitterling certify that: I have reviewed this response and the supporting documents do 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.

Sincerely,

Philip I. Mitterling
EVP & CFO
Puget Sound Bank

Puget Sound Bank 2009 Budget Balance Sheet

Balance Sheet

	FD 2008 December
ASSETS	
Cash & Due from Banks	3,800,000
Dep w/Banks	6,001,979
Fed Funds Sold	66,279
Investment Securities	22,803,000
Commercial Loans	46,778,770
Commercial RE Loans	69,784,994
Personal Loans	13,436,237
Total Loans	130,000,000
Allowance for Loan Losses	(1,751,409)
Deferred Loan Fees	(266,000)
Net Loans	127,982,591
(b) (4)	
Other Assets	1,180,000
Total Assets	161,833,849
LIABILITIES	
Deposits	
Non Interest Bearing Deposits	11,400,000
Interest Bearing Checking	2,450,000
Money Market/Savings Accounts	39,326,363
CDs	25,323,638
CDARS CDs	49,500,000
Brokered/Public CDs	12,000,000
Total Deposits	140,000,000
Other Borrowings	-
Other Liabilities	950,000
Total Liabilities	140,950,000
STOCKHOLDERS EQUITY	
Preferred Stock	-
Common Stock & Paid-in Capital	22,740,659
Unrealized Gain/Loss	300,000
Prior Period Earnings	(2,571,810)
Current Period Earnings	415,000
Total Stockholders Equity	20,883,849
Total Liabilities & Equity	161,833,849



Phil Mitterling

From: Jim Mitchell
Sent: Wednesday, February 04, 2009 5:39 PM
To: Jim Mitchell
Subject: Puget Sound Bank fourth quarter and 2008 financial results
Attachments: Press release - Q4 and 2008.pdf; Financial statements 2008.pdf; Income statements - Fourth quarter and 2008.pdf

Dear Shareholders,

I have attached the: 1) Fourth Quarter and 2008 Press Release, 2) The Balance Sheet for 2008, and 3) The Four Quarter and 2008 Income Statement for Puget Sound Bank. All this information is also posted on our website at www.pugetsoundbank.com.

As you can see, Puget Sound Bank's record earnings, excellent credit quality, strong capital, good loan and deposit growth, and superior liquidity is in stark contrast to most of our financial peers. I attribute these accomplishments during these tough economic times to: 1) Conservatively managing the bank with experienced, knowledgeable, and customer oriented bankers, 2) Focusing from DAY ONE on a conservative credit culture, 3) Lending predominately to small and medium sized businesses where we have experience, and staying away from the residential land development and construction sector that has caused so many problems for banks, and 4) Ensuring that there is always significant capital and liquidity to cushion against down turns.

These precepts have driven our business model. They have allowed us to have fifteen consecutive quarters of NO credit losses. They have allowed Puget Sound Bank to have NO 30 day past due loans at 12-31-08. They have allowed us to grow loans and deposits by 30% and 52% respectively in 2008. It has driven us to maintain a capital ratio (net worth to total assets) of 13.8% when the regulations define the "well capitalized" level at 10%. It has produced 2008 net income of \$416,000, 125% over 2007.

This same approach to business drove us to apply, receive approval, and accept \$4.5 million of capital from the US Treasury on 1-16-09. There are many positive reasons for accepting this capital. Here are a few:

- It is in the form of Perpetual Preferred Stock with a 5% dividend coupon. It is inexpensive capital and is particularly beneficial to shareholders because it is not dilutive because there is no additional common stock issued.
- Although Puget Sound Bank did not need the capital now, we would need capital in approximately eighteen months based on our current growth trajectory. This allows us to take the capital now and ensures the bank can continue to grow even if the capital markets for banks is still bad over the next eighteen months.
- It puts Puget Sound Bank in a pool of banks that qualified for capital under TARP. This capital will only be given to banks with solid financial fundamentals so that they will be in a position to help the current economic situation by lending money. Many will not qualify.
- The added capital and liquidity will put Puget Sound Bank in position to capitalize on opportunities that present themselves.
- Over time this added capital should improve the bank's ratios of Return on Equity (ROE), Return on Assets (ROA), and Earnings per Share (EPS). This, in turn, should improve the bank's stock performance as the economic situation improves.

Other financial highlights of 2008 include:

- TOTAL ASSETS grew to \$166 million, 46% over the 2007 assets of \$114 million.
- TOTAL DEPOSITS grew to \$140 million, 52% over the 2007 deposits of \$92 million.
- TOTAL LOANS grew to \$131 million, 30% over the 2007 loans of \$100 million.

These numbers have kept our stock trading at a multiple of book value of 1.2 times (\$10.4 per share). The publicly traded banks in Washington and Oregon, on average, trade at only 0.50% of book value. Of the 40 publicly traded banks in Washington and Oregon only three trade higher than Puget Sound Bank in this regard.

Puget Sound Bank trades on the Over-The-Counter Bulletin Board under the symbol PUGB.OB.

We count on our shareholders to be Ambassadors for the bank by becoming depositors and continuing to refer credit business to the bank. These referrals become especially important as we enter 2009 and the many challenges the current economy will bring. We specialize in small and medium size businesses that have \$5 million to \$100 million in sales. Selectively we also provide commercial real estate loans. In addition, we offer private banking services to owners, professionals, and high net individuals that seek a higher level of customer service.

Thank you for your continued support.



Jim Mitchell
President and CEO
Puget Sound Bank
10500 NE 8th Street
Suite 1800
Bellevue, Wa. 98004

(b) (6)

NEW LOAN REPORT
Commitments Booked During January & February 2009

Closing Date	Name	Commitment Amount	Risk Rating	Loan Type	Collateral
1/7/09	b(4), b(6)	\$200,000	4	Term	UCC
1/8/09		\$173,000	4	Term	UCC
1/9/09		\$50,000	4	Term	UCC
1/14/09		\$300,000	3	LOC	Securities
2/10/09		\$500,000	5	HELOC	2nd Dot 1-4 Family
2/12/09		\$2,500,000	5	Term	1st Dot Comm. R/E
2/13/09		\$300,000	5	LOC	UCC
2/13/09		\$500,000	5	LOC	UCC
2/18/09		\$822,575	4	Term	1st Dot Comm. R/E
2/23/09		\$2,000,000	5	Draw Down	1st Dot Comm. R/E
2/24/09	\$225,000	4	LOC	Unsecured	

After Jan. 16th and receipt of capital. →

Totals \$7,570,575

Total since 1/16 \$6,622,575

**AGREEMENT TO AMEND COMPENSATION
ARRANGEMENTS WITH SENIOR EXECUTIVE OFFICER**

THIS AGREEMENT TO AMEND COMPENSATION ARRANGEMENTS WITH SENIOR EXECUTIVE OFFICER (this "Agreement") is entered into by and between PUGET SOUND BANK (the "Company"), and _____ (the "Executive"), a senior executive officer of Puget Sound Bank.

RECITALS

A. The Company is entering into a securities purchase agreement (the "Securities Purchase Agreement"), with the United States Department of Treasury ("Treasury") that provides for the Company's participation in the Treasury's TARP Capital Purchase Program (the "CPP"), pursuant to the Emergency Economic Stabilization Act of 2008. If the Company does not participate or ceases at any time to participate in the CPP and Treasury no longer holds any equity or debt position acquired from the Company in the CPP, this Agreement shall be of no further force and effect.

B. For the Company to participate in the CPP and as a condition to the closing of the Treasury's investment contemplated by the Securities Purchase Agreement, the Company is required to establish specified standards for bonus and incentive compensation to its senior executive officers, including the Executive, and to make changes to its compensation agreements, plans, policies and other arrangements. To comply with these requirements, and in consideration of the benefits the Executive will receive as a result of the Company's participation in the CPP, the Executive agrees with Puget Sound Bank as follows:

AGREEMENT

1. *No Golden Parachute Payments.* The Company shall not make any golden parachute payment to the Executive during any "CPP Covered Period". A "CPP Covered Period" is any period during which (A) the Executive is a "senior executive officer" and (B) Treasury holds an equity or debt position acquired from the Company in the CPP.

2. *Recovery of Bonus and Incentive Compensation.* Any bonus and incentive compensation paid to the Executive during a CPP Covered Period is subject to recovery or "clawback" by the Company if the payments were based on statements of earnings, gains or other criteria that are later proven to be materially inaccurate within the meaning of Section 111(b)(2)(B) of EESA. The Executive shall promptly reimburse the Company upon demand for any such payments.

3. *Compensation Program Agreements.* Each of the Company's compensation, bonus, incentive and other benefit plans, arrangements, agreements and policies (including golden parachute, severance and employment agreements) with respect to the Executive (collectively, "Benefit Plans") is hereby amended to the extent necessary to give effect to provisions 1 and 2.

In addition, the Company is required to review its Benefit Plans to ensure that they do not encourage senior executive officers to take unnecessary and excessive risks that threaten the

value of the Company. To the extent any such review or any subsequent regulations or new Benefit Plan referenced in Section 4 requires revisions to any Benefit Plan with respect to the Executive, the Executive and the Company shall negotiate such changes promptly and in good faith, in order to meet the terms of CPP.

4. *Subsequent Regulations/Plans.* The Executive acknowledges and agrees that Section 4.10 of the Securities Purchase Agreement provides that the Company shall take all necessary action to insure that its Benefit Plans with respect to its senior executive officers, including the Executive, comply in all respects with Section 111(b) of EESA as implemented by any guidance or regulation thereunder that has been issued and is in effect as of the Closing Date of the Securities Purchase Agreement (the "Closing Date"), and shall not adopt any new Benefit Plan with respect to its senior executive officers that does not comply therewith.

5. *Definitions and Interpretation.* This Agreement shall be interpreted as follows:

- "Senior executive officer" means the Company's "senior executive officers" as defined in subsection 111(b)(3) of EESA.
- "Golden parachute payment" is used with same meaning as in Section 111(b)(2)(C) of EESA.
- "EESA" means the Emergency Economic Stabilization Act of 2008 as implemented by guidance or regulation issued by the Department of the Treasury and as published in the Federal Register on October 20, 2008.
- The term "Company" includes any other entities treated as a single employer with the Company under 31 C.F.R. § 30.1(b) (as in effect on the Closing Date). The Executive is also delivering a waiver pursuant to the Securities Purchase Agreement, and, as between the Company and the Executive, the term "employer" in that waiver will be deemed to mean the Company as used in this Agreement.
- The term "CPP Covered Period" shall be limited by, and interpreted in a manner consistent with, 31 C.F.R. § 30.11 (as in effect on the Closing Date).
- Paragraphs 1, 2 and 3 of this Agreement are intended to, and will be interpreted, administered and construed to, comply with Section 111 of EESA (and, to the maximum extent consistent with the preceding, to permit operation of the Benefit Plans in accordance with their terms before giving effect to this Agreement).

6. *Company Policy.* The Company's board of directors has adopted the provisions of this Agreement as a statement of policy to govern the terms and conditions of employment for the Company's senior executive officers, including the Executive.

7. *Miscellaneous.* To the extent not subject to federal law, this Agreement will be governed by and construed in accordance with the laws of the State of Washington. This

Agreement may be executed in two or more counterparts, each of which will be deemed to be an original. A signature transmitted by facsimile will be deemed an original signature.

IN WITNESS HEREOF, the undersigned have executed and delivered this Agreement on _____, 2008, to be effective as of the Closing Date of the Securities Purchase Agreement.

PUGET SOUND BANK

EXECUTIVE

By: _____ [Name]
Title: _____ [Title]