FULTON FINANCIAL CORP
Form 10-Q
November 08, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20459

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2013, 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 No. 0-10587
FULTON FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

PENNSYLVANIA (State or other jurisdiction of incorporation or organization)	23-2195389 (I.R.S. Employer Identification No.)
One Penn Square, P.O. Box 4887, Lancaster, Pennsylvania (Address of principal executive offices)	17604 (Zip Code)

(717) 291-2411
(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 ý No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	ý	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 ý

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:
Common Stock, $2.50 Par Value – 192,450,000 shares outstanding as of October 31, 2013.

FULTON FINANCIAL CORPORATION
FORM 10-Q FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013
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Item 1. Financial Statements

FULTON FINANCIAL CORPORATION
CONSOLIDATED BALANCE SHEETS

(in thousands, except per-share data)

	September 30, 2013 (unaudited)	December 31, 2012
ASSETS		
Cash and due from banks	$262,938	$256,300
Interest-bearing deposits with other banks	221,064	173,257
Loans held for sale	39,273	67,899
Investment securities:		
Held to maturity (estimated fair value of $224 in 2013 and $319 in 2012)	206	292
Available for sale	2,686,443	2,793,725
Loans, net of unearned income	12,780,899	12,146,971
Less: Allowance for loan losses	(210,486)	(223,903)
Net Loans	12,570,413	11,923,068
Premises and equipment	227,299	227,723
Accrued interest receivable	44,715	45,786
Goodwill	530,614	530,656
Intangible assets	3,304	4,907
Other assets	464,502	509,484
Total Assets	$17,050,771	$16,533,097
LIABILITIES		
Deposits:		
Noninterest-bearing	$3,338,075	$3,009,966
Interest-bearing	9,383,046	9,474,197
Total Deposits	12,721,121	12,484,163
Short-term borrowings:		
Federal funds purchased	493,274	592,470
Other short-term borrowings	705,303	275,929
Total Short-Term Borrowings	1,198,577	868,399
Accrued interest payable	16,657	19,330
Other liabilities	196,330	185,296
Federal Home Loan Bank advances and long-term debt	889,122	894,253
Total Liabilities	15,021,807	14,451,441
SHAREHOLDERS' EQUITY		
Common stock, $2.50 par value, 600 million shares authorized, 217.6 million shares issued in 2013 and 216.8 million shares issued in 2012	544,052	542,093
Additional paid-in capital	1,431,015	1,426,267
Retained earnings	437,173	363,937
Accumulated other comprehensive income (loss)	(40,871)	5,675
Treasury stock, at cost, 25.3 million shares in 2013 and 17.6 million shares in 2012	(342,405)	(256,316)
Total Shareholders' Equity	2,028,964	2,081,656
Total Liabilities and Shareholders' Equity	$17,050,771	$16,533,097

See Notes to Consolidated Financial Statements

FULTON FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

(in thousands, except per-share data)	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
INTEREST INCOME				
Loans, including fees	$136,150	$140,511	$405,312	$426,398
Investment securities:				
Taxable	12,977	16,658	40,890	53,943
Tax-exempt	2,327	2,558	7,151	7,855
Dividends	958	720	2,523	2,060
Loans held for sale	382	578	1,261	1,547
Other interest income	38	35	95	133
Total Interest Income	152,832	161,060	457,232	491,936
INTEREST EXPENSE				
Deposits	8,743	13,848	28,642	44,841
Short-term borrowings	691	220	1,900	912
Long-term debt	10,865	11,111	32,448	34,077
Total Interest Expense	20,299	25,179	62,990	79,830
Net Interest Income	132,533	135,881	394,242	412,106
Provision for credit losses	9,500	23,000	38,000	76,500
Net Interest Income After Provision for Credit Losses	123,033	112,881	356,242	335,606
NON-INTEREST INCOME				
Service charges on deposit accounts	13,938	15,651	42,700	45,860
Investment management and trust services	10,420	9,429	31,117	28,628
Other service charges and fees	9,518	11,119	27,536	33,181
Mortgage banking income	7,123	10,594	26,293	31,787
Other	3,725	5,108	11,315	14,602
Investment securities gains, net:				
Other-than-temporary impairment losses	(125)	(43)	(146)	(100)
Less: Portion of gain recognized in other comprehensive income (loss) (before taxes)	28	—	22	—
Net other-than-temporary impairment losses	(97)	(43)	(124)	(100)
Net gains on sales of investment securities	2,730	85	8,095	2,931
Investment securities gains, net	2,633	42	7,971	2,831
Total Non-Interest Income	47,357	51,943	146,932	156,889
NON-INTEREST EXPENSE				
Salaries and employee benefits	63,344	62,161	188,046	182,612
Net occupancy expense	11,519	11,161	34,810	33,301
Other outside services	5,048	5,600	13,223	13,614
Data processing	4,757	3,776	13,169	11,223
Equipment expense	3,646	3,816	11,447	10,370
Professional fees	3,329	2,728	9,771	8,294
Operating risk loss	3,297	1,404	6,923	6,827
Software	3,268	2,511	9,110	6,958
FDIC insurance expense	2,918	3,029	8,766	9,052
Marketing	2,251	648	6,045	5,703
Other real estate owned and repossession expense	1,453	2,249	6,248	8,709
Intangible amortization	534	756	1,603	2,318

Other	11,241	10,143	35,510	33,757
Total Non-Interest Expense	116,605	109,982	344,671	332,738
Income Before Income Taxes	53,785	54,842	158,503	159,757
Income taxes	13,837	13,260	38,746	40,152
Net Income	$39,948	$41,582	$119,757	$119,605
PER SHARE:				
Net Income (Basic)	$0.21	$0.21	$0.62	$0.60
Net Income (Diluted)	0.21	0.21	0.61	0.60
Cash Dividends	0.08	0.08	0.24	0.22

See Notes to Consolidated Financial Statements

FULTON FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED)

(in thousands)

	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
Net Income	$39,948	$41,582	$119,757	$119,605
Other Comprehensive Income (Loss), net of tax:				
Unrealized gain (loss) on securities	(6,951)	10,834	(43,784)	4,714
Reclassification adjustment for securities gains included in net income	(1,711)	(28)	(5,181)	(1,840)
Non-credit related unrealized gain (loss) on other-than-temporarily impaired debt securities	(106)	271	1,332	234
Unrealized gain on derivative financial instruments	34	34	102	102
Amortization of net unrecognized pension and postretirement items	329	214	985	642
Other Comprehensive Income (Loss)	(8,405)	11,325	(46,546)	3,852
Total Comprehensive Income	$31,543	$52,907	$73,211	$123,457

See Notes to Consolidated Financial Statements

FULTON FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (UNAUDITED)
NINE MONTHS ENDED SEPTEMBER 30, 2013 AND 2012

(in thousands, except per-share data)

	Common Stock						
	Shares Outstanding	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
Balance at December 31, 2012	199,225	$542,093	$1,426,267	$363,937	$ 5,675	$(256,316)	$2,081,656
Net income				119,757			119,757
Other comprehensive income (loss)					(46,546)		(46,546)
Stock issued, including related tax benefits	1,107	1,959	562			4,838	7,359
Stock-based compensation awards			4,186				4,186
Acquisition of treasury stock	(8,000)					(90,927)	(90,927)
Common stock cash dividends - $0.24 per share				(46,521)			(46,521)
Balance at September 30, 2013	192,332	$544,052	$1,431,015	$437,173	$ (40,871)	$(342,405)	$2,028,964
Balance at December 31, 2011	200,164	$540,386	$1,423,727	$264,059	$ 7,955	$(243,588)	$1,992,539
Net income				119,605			119,605
Other comprehensive income (loss)					3,852		3,852
Stock issued, including related tax benefits	926	1,434	(1,889)			5,565	5,110
Stock-based compensation awards			3,963				3,963
Acquisition of treasury stock	(2,115)					(20,360)	(20,360)
Common stock cash dividends - $0.22 per share				(44,026)			(44,026)
Balance at September 30, 2012	198,975	$541,820	$1,425,801	$339,638	$ 11,807	$(258,383)	$2,060,683

See Notes to Consolidated Financial Statements

FULTON FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(in thousands)

	Nine months ended September 30	
	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	$119,757	$119,605
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	38,000	76,500
Depreciation and amortization of premises and equipment	19,165	16,735
Net amortization of investment securities premiums	8,749	8,039
Investment securities gains, net	(7,971)	(2,831)
Net decrease (increase) in loans held for sale	28,626	(38,468)
Amortization of intangible assets	1,603	2,318
Stock-based compensation	4,186	3,963
Excess tax benefits from stock-based compensation	(237)	(25)
Decrease in accrued interest receivable	1,071	1,314
Decrease in other assets	38,485	12,956
Decrease in accrued interest payable	(2,673)	(3,868)
Decrease in other liabilities	(24,207)	(2,191)
Total adjustments	104,797	74,442
Net cash provided by operating activities	224,554	194,047
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sales of securities available for sale	283,242	225,539
Proceeds from maturities of securities held to maturity	86	228
Proceeds from maturities of securities available for sale	526,393	644,055
Purchase of securities held to maturity	—	(346)
Purchase of securities available for sale	(723,859)	(796,656)
Increase in short-term investments	(47,807)	(26,969)
Net increase in loans	(684,529)	(63,446)
Net purchases of premises and equipment	(18,741)	(30,232)
Net cash used in investing activities	(665,215)	(47,827)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in demand and savings deposits	595,722	510,296
Net decrease in time deposits	(358,764)	(434,952)
Increase (decrease) in short-term borrowings	330,178	(110,062)
Repayments of long-term debt	(5,131)	(131,526)
Net proceeds from issuance of common stock	7,122	5,085
Excess tax benefits from stock-based compensation	237	25
Dividends paid	(31,138)	(40,117)
Acquisition of treasury stock	(90,927)	(20,360)
Net cash provided by (used in) financing activities	447,299	(221,611)
Net Increase (Decrease) in Cash and Due From Banks	6,638	(75,391)
Cash and Due From Banks at Beginning of Period	256,300	292,598
Cash and Due From Banks at End of Period	$262,938	$217,207
Supplemental Disclosures of Cash Flow Information:		
Cash paid during the period for:		
Interest	$65,663	$83,698

Income taxes	29,964	22,671

See Notes to Consolidated Financial Statements

FULTON FINANCIAL CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE A – Basis of Presentation

The accompanying unaudited consolidated financial statements of Fulton Financial Corporation (the Corporation) have been prepared in conformity with U.S. generally accepted accounting principles (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and notes required by U.S. GAAP for complete financial statements. The preparation of financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the amounts of assets and liabilities as of the date of the financial statements as well as revenues and expenses during the period. Actual results could differ from those estimates. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2013 are not necessarily indicative of the results that may be expected for the year ending December 31, 2013. The Corporation evaluates subsequent events through the filing date of this Form 10-Q with the Securities and Exchange Commission (SEC).

NOTE B – Net Income Per Share

Basic net income per share is calculated as net income divided by the weighted average number of shares outstanding. Diluted net income per share is calculated as net income divided by the weighted average number of shares outstanding plus the incremental number of shares added as a result of converting common stock equivalents, calculated using the treasury stock method. The Corporation's common stock equivalents consist of outstanding stock options and restricted stock.

A reconciliation of weighted average shares outstanding used to calculate basic net income per share and diluted net income per share follows:

	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
	(in thousands)			
Weighted average shares outstanding (basic)	192,251	198,956	193,926	199,371
Effect of dilutive securities	1,008	852	1,000	950
Weighted average shares outstanding (diluted)	193,259	199,808	194,926	200,321

For the three and nine months ended September 30, 2013, 3.2 million and 3.7 million shares issuable under stock options, respectively, were excluded from the diluted net income per share computation as their effect would have been anti-dilutive. For the three and nine months ended September 30, 2012, 5.2 million shares issuable under stock options were excluded from the diluted net income per share computation as their effect would have been anti-dilutive.

NOTE C – Accumulated Other Comprehensive Income (Loss)

The following table presents changes in other comprehensive income (loss):

	Before-Tax Amount (in thousands)	Tax Effect	Net of Tax Amount
Three months ended September 30, 2013			
Unrealized gain (loss) on securities	$(10,691)	$3,740	$(6,951)
Reclassification adjustment for securities gains included in net income (1)	(2,633)	922	(1,711)
Non-credit related unrealized gains (losses) on other-than-temporarily impaired debt securities	(163)	57	(106)
Unrealized gain on derivative financial instruments	52	(18)	34
Amortization of net unrecognized pension and postretirement items (2)	505	(176)	329
Total Other Comprehensive Income (Loss)	$(12,930)	$4,525	$(8,405)
Three months ended September 30, 2012			
Unrealized gain (loss) on securities	$16,667	$(5,833)	$10,834
Reclassification adjustment for securities gains included in net income (1)	(42)	14	(28)
Non-credit related unrealized gains (losses) on other-than-temporarily impaired debt securities	417	(146)	271
Unrealized gain on derivative financial instruments	52	(18)	34
Amortization of net unrecognized pension and postretirement items (2)	329	(115)	214
Total Other Comprehensive Income (Loss)	$17,423	$(6,098)	$11,325
Nine months ended September 30, 2013			
Unrealized gain (loss) on securities	$(67,357)	$23,573	$(43,784)
Reclassification adjustment for securities gains included in net income (1)	(7,971)	2,790	(5,181)
Non-credit related unrealized gains (losses) on other-than-temporarily impaired debt securities	2,049	(717)	1,332
Unrealized gain on derivative financial instruments	157	(55)	102
Amortization of net unrecognized pension and postretirement items (2)	1,515	(530)	985
Total Other Comprehensive Income (Loss)	$(71,607)	$25,061	$(46,546)
Nine months ended September 30, 2012			
Unrealized gain (loss) on securities	$7,252	$(2,538)	$4,714
Reclassification adjustment for securities gains included in net income (1)	(2,831)	991	(1,840)
Non-credit related unrealized gains (losses) on other-than-temporarily impaired debt securities	360	(126)	234
Unrealized gain on derivative financial instruments	157	(55)	102
Amortization of net unrecognized pension and postretirement items (2)	987	(345)	642
Total Other Comprehensive Income (Loss)	$5,925	$(2,073)	$3,852

(1) Amounts reclassified out of accumulated other comprehensive income. Before-tax amounts included within "Investment securities gains, net" on the consolidated statements of income. See Note D, "Investment Securities," for additional details.

(2) Amounts reclassified out of accumulated other comprehensive income. Before-tax amounts included within "Salaries and employee benefits" on the consolidated statements of income. See Note H, "Employee Benefit Plans," for additional details.

The following table presents changes in each component of accumulated other comprehensive income (loss), net of tax:

	Unrealized Gains (Losses) on Investment Securities Not Other-Than-Temporarily Impaired	Unrealized Non-Credit Gains (Losses) on Other-Than-Temporarily Impaired Debt Securities	Unrealized Effective Portions of Losses on Forward-Starting Interest Rate Swaps	Unrecognized Pension and Postretirement Plan Income (Costs)	Total
	(in thousands)				
Three months ended September 30, 2013					
Balance at June 30, 2013	$(12,941)	$ 1,050	$ (2,750)	$ (17,825)	$(32,466)
Other comprehensive income (loss) before reclassifications	(6,951)	(106)	—	—	(7,057)
Amounts reclassified from accumulated other comprehensive income (loss)	(1,774)	63	34	329	(1,348)
Balance at September 30, 2013	$(21,666)	$ 1,007	$ (2,716)	$ (17,496)	$(40,871)
Three months ended September 30, 2012					
Balance at June 30, 2012	$19,122	$ (1,048)	$ (2,886)	$ (14,706)	$482
Other comprehensive income (loss) before reclassifications	10,834	271	—	—	11,105
Amounts reclassified from accumulated other comprehensive income (loss)	(40)	12	34	214	220
Balance at September 30, 2012	$29,916	$ (765)	$ (2,852)	$ (14,492)	$11,807
Nine months ended September 30, 2013					
Balance at December 31, 2012	$26,361	$ 613	$ (2,818)	$ (18,481)	$5,675
Other comprehensive income (loss) before reclassifications	(43,784)	1,332	—	—	(42,452)
Amounts reclassified from accumulated other comprehensive income (loss)	(4,243)	(938)	102	985	(4,094)
Balance at September 30, 2013	$(21,666)	$ 1,007	$ (2,716)	$ (17,496)	$(40,871)
Nine months ended September 30, 2012					
Balance at December 31, 2011	$27,054	$ (1,011)	$ (2,954)	$ (15,134)	$7,955
Other comprehensive income (loss) before reclassifications	4,714	234	—	—	4,948
Amounts reclassified from accumulated other comprehensive income (loss)	(1,852)	12	102	642	(1,096)
Balance at September 30, 2012	$29,916	$ (765)	$ (2,852)	$ (14,492)	$11,807

NOTE D – Investment Securities

The following table presents the amortized cost and estimated fair values of investment securities:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Held to Maturity at September 30, 2013	(in thousands)			
Mortgage-backed securities	$206	$18	$—	$224
Available for Sale at September 30, 2013				
Equity securities	$123,111	$8,596	$(130)	$131,577
U.S. Government securities	2,250	—	—	2,250
U.S. Government sponsored agency securities	828	8	(1)	835
State and municipal securities	288,659	7,552	(2,698)	293,513
Corporate debt securities	108,272	5,115	(6,836)	106,551
Collateralized mortgage obligations	1,113,753	9,373	(40,149)	1,082,977
Mortgage-backed securities	909,292	15,209	(10,271)	914,230
Auction rate securities	172,052	36	(17,578)	154,510
	$2,718,217	$45,889	$(77,663)	$2,686,443

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Held to Maturity at December 31, 2012	(in thousands)			
Mortgage-backed securities	$292	$27	$—	$319
Available for Sale at December 31, 2012				
Equity securities	$118,465	$5,016	$(918)	$122,563
U.S. Government securities	325	—	—	325
U.S. Government sponsored agency securities	2,376	21	—	2,397
State and municipal securities	301,842	13,763	(86)	315,519
Corporate debt securities	112,162	7,858	(7,178)	112,842
Collateralized mortgage obligations	1,195,234	16,008	(123)	1,211,119
Mortgage-backed securities	847,790	31,831	—	879,621
Auction rate securities	174,026	—	(24,687)	149,339
	$2,752,220	$74,497	$(32,992)	$2,793,725

Securities carried at $1.8 billion as of September 30, 2013 and December 31, 2012 were pledged as collateral to secure public and trust deposits and customer repurchase agreements.

Available for sale equity securities include restricted investment securities issued by the Federal Home Loan Bank (FHLB) and the Federal Reserve Bank ($87.9 million at September 30, 2013 and $71.7 million at December 31, 2012), common stocks of financial institutions ($36.8 million at September 30, 2013 and $44.2 million at December 31, 2012) and other equity investments ($6.9 million at September 30, 2013 and $6.7 million at December 31, 2012).

As of September 30, 2013, the financial institutions stock portfolio had a cost basis of $28.5 million and a fair value of $36.8 million, including an investment in a single financial institution with a cost basis of $20.0 million and a fair value of $26.2 million. The fair value of this investment accounted for 71.1% of the fair value of the Corporation's investments in the common stocks of publicly traded financial institutions. No other investment within the financial institutions stock portfolio exceeded 5% of the portfolio's fair value.

The amortized cost and estimated fair values of debt securities as of September 30, 2013, by contractual maturity, are shown in the following table. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Held to Maturity		Available for Sale	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
	(in thousands)			
Due in one year or less	$—	$—	$45,346	$45,470
Due from one year to five years	—	—	63,113	66,924
Due from five years to ten years	—	—	197,964	201,552
Due after ten years	—	—	265,638	243,713
	—	—	572,061	557,659
Collateralized mortgage obligations	—	—	1,113,753	1,082,977
Mortgage-backed securities	206	224	909,292	914,230
	$206	$224	$2,595,106	$2,554,866

The following table presents information related to the gains and losses on the sales of equity and debt securities, and losses recognized for the other-than-temporary impairment of investments:

	Gross Realized Gains	Gross Realized Losses	Other-than-temporary Impairment Losses	Net Gains
Three months ended September 30, 2013		(in thousands)		
Equity securities	$2,135	$—	$—	$2,135
Debt securities	617	(22)	(97)	498
Total	$2,752	$(22)	$(97)	$2,633
Three months ended September 30, 2012				
Equity securities	$—	$—	$(24)	$(24)
Debt securities	85	—	(19)	66
Total	$85	$—	$(43)	$42
Nine months ended September 30, 2013				
Equity securities	$4,357	$(28)	$(27)	$4,302
Debt securities	3,788	(22)	(97)	3,669
Total	$8,145	$(50)	$(124)	$7,971
Nine months ended September 30, 2012				
Equity securities	$2,603	$—	$(81)	$2,522
Debt securities	328	—	(19)	309
Total	$2,931	$—	$(100)	$2,831

The other-than-temporary impairment charges for equity securities during the three and nine months ended September 30, 2013 and 2012 were for investments in stocks of financial institutions and were due to the severity and duration of the declines in the fair values of certain bank stock stocks, in conjunction with management's assessment of the near-term prospects of each specific issuer.

The credit related other-than-temporary impairment charges for debt securities during the three and nine months ended September 30, 2013 and 2012 were for investments in pooled trust preferred securities issued by financial institutions. The credit related other-than-temporary impairment charges for the pooled trust preferred securities were determined based on an expected cash flows model.

The following table presents a summary of the cumulative credit related other-than-temporary impairment charges, recognized as components of earnings, for debt securities held by the Corporation at September 30, 2013 and 2012:

	Three Months ended September 30		Nine Months ended September 30	
	2013	2012	2013	2012
	(in thousands)			
Balance of cumulative credit losses on debt securities, beginning of period	$(20,607)	$(22,692)	$(23,079)	$(22,781)
Reductions for securities sold during the period	—	—	2,468	—
Additions for credit losses recorded which were not previously recognized as components of earnings	(97)	(19)	(97)	(19)
Reductions for increases in cash flows expected to be collected that are recognized over the remaining life of the security	—	66	4	155
Balance of cumulative credit losses on debt securities, end of period	$(20,704)	$(22,645)	$(20,704)	$(22,645)

The following table presents the gross unrealized losses and estimated fair values of investments, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at September 30, 2013:

	Less than 12 months		12 months or longer		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
	(in thousands)					
U.S. Government sponsored agency securities	$—	$—	$59	$(1)	$59	$(1)
State and municipal securities	54,679	(2,698)	—	—	54,679	(2,698)
Corporate debt securities	6,889	(108)	42,989	(6,728)	49,878	(6,836)
Collateralized mortgage obligations	746,630	(40,149)	—	—	746,630	(40,149)
Mortgage-backed securities	499,406	(10,271)	—	—	499,406	(10,271)
Auction rate securities	87	(3)	153,245	(17,575)	153,332	(17,578)
Total debt securities	1,307,691	(53,229)	196,293	(24,304)	1,503,984	(77,533)
Equity securities	17	(1)	850	(129)	867	(130)
	$1,307,708	$(53,230)	$197,143	$(24,433)	$1,504,851	$(77,663)

The Corporation's collateralized mortgage obligations and mortgage-backed securities have contractual terms that generally do not permit the issuer to settle the securities at a price less than the amortized cost of the investment. Because the decline in market value of these securities is attributable to changes in interest rates and not credit quality, and because the Corporation does not have the intent to sell and does not believe it will more likely than not be required to sell any of these securities prior to a recovery of their fair value to amortized cost, the Corporation does not consider these investments to be other-than-temporarily impaired as of September 30, 2013.

The unrealized holding losses on auction rate securities, or auction rate certificates (ARCs), are attributable to liquidity issues resulting from the failure of periodic auctions. Fulton Financial Advisors (FFA) is the investment management and trust division of the Corporation's Fulton Bank, N.A. subsidiary. FFA had previously purchased ARCs for customers as short-term investments with fair values that could be derived based on periodic auctions under normal market conditions. During 2008 and 2009, the Corporation purchased ARCs from customers due to the failure of these periodic auctions, which made these previously short-term investments illiquid.

As of September 30, 2013, approximately $147 million, or 95%, of the ARCs were rated above investment grade, with approximately $8 million, or 5%, AAA rated and $100 million, or 65%, AA rated. Approximately $8 million, or 5%, of ARCs were either not rated or rated below investment grade by at least one ratings agency. Of this amount, approximately $6 million, or 72%, of the student loans underlying these ARCs have principal payments which are guaranteed by the federal government. In total, approximately $151 million, or 98%, of the student loans underlying the ARCs have principal payments which are guaranteed by the federal government. As of September 30, 2013, all ARCs were current and making scheduled interest payments. Based on management's evaluations, ARCs with a fair value of $154.5 million were not subject to any other-than-temporary impairment charges as of September 30, 2013. The Corporation does not have the intent to sell and does not believe it will more likely than not be required to sell any of these securities prior to a recovery of their fair value to amortized cost, which may be at maturity.

For its investments in equity securities, particularly its investments in stocks of financial institutions, management evaluates the near-term prospects of the issuers in relation to the severity and duration of the impairment. Based on that evaluation and the Corporation’s ability and intent to hold those investments for a reasonable period of time sufficient for a recovery of fair value, the Corporation does not consider those investments with unrealized holding losses as of September 30, 2013 to be other-than-temporarily impaired.

The majority of the Corporation's available for sale corporate debt securities are issued by financial institutions. The following table presents the amortized cost and estimated fair value of corporate debt securities:

	September 30, 2013		December 31, 2012	
	Amortized cost	Estimated fair value	Amortized cost	Estimated fair value
	(in thousands)			
Single-issuer trust preferred securities	$54,722	$48,368	$56,834	$51,656
Subordinated debt	47,375	50,493	47,286	51,747
Pooled trust preferred securities	3,676	5,191	5,530	6,927
Corporate debt securities issued by financial institutions	105,773	104,052	109,650	110,330
Other corporate debt securities	2,499	2,499	2,512	2,512
Available for sale corporate debt securities	$108,272	$106,551	$112,162	$112,842

The Corporation’s investments in single-issuer trust preferred securities had an unrealized loss of $6.4 million at September 30, 2013. The Corporation did not record any other-than-temporary impairment charges for single-issuer trust preferred securities during the three and nine months ended September 30, 2013 or 2012. The Corporation held six single-issuer trust preferred securities that were rated below investment grade by at least one ratings agency, with an amortized cost of $13.5 million and an estimated fair value of $11.6 million at September 30, 2013. The majority of the single-issuer trust preferred securities rated below investment grade were rated BB or Ba. Single-issuer trust preferred securities with an amortized cost of $4.7 million and an estimated fair value of $3.8 million at September 30, 2013 were not rated by any ratings agency.

As of September 30, 2013, the Corporation held eight pooled trust preferred securities with an amortized cost of $3.7 million and an estimated fair value of $5.2 million that were rated below investment grade by at least one ratings agency, with ratings ranging from C to Ca. The class of securities held by the Corporation was below the most senior tranche, with the Corporation’s interests being subordinate to other investors in the pool. The Corporation determines the fair value of pooled trust preferred securities based on quotes provided by third-party brokers.

The amortized cost of pooled trust preferred securities is the purchase price of the securities, net of cumulative credit related other-than-temporary impairment charges, determined using an expected cash flows model. The most significant input to the expected cash flows model is the expected payment deferral rate for each pooled trust preferred security. The Corporation evaluates the financial metrics, such as capital ratios and non-performing assets ratios, of the individual financial institution issuers that comprise each pooled trust preferred security to estimate its expected deferral rate.

Based on management’s evaluations, corporate debt securities with a fair value of $106.6 million were not subject to any additional other-than-temporary impairment charges as of September 30, 2013. The Corporation does not have the intent to sell and does not believe it will more likely than not be required to sell any of these securities prior to a recovery of their fair value to amortized cost, which may be at maturity.

NOTE E – Loans and Allowance for Credit Losses

Loans, Net of Unearned Income
Loans, net of unearned income are summarized as follows:

	September 30, 2013	December 31, 2012
	(in thousands)	
Real-estate - commercial mortgage	$5,063,373	$4,664,426
Commercial - industrial, financial and agricultural	3,645,270	3,612,065
Real-estate - home equity	1,773,554	1,632,390
Real-estate - residential mortgage	1,327,469	1,257,432
Real-estate - construction	577,342	584,118
Consumer	296,142	309,864
Leasing and other	89,819	75,521
Overdrafts	16,706	18,393
Loans, gross of unearned income	12,789,675	12,154,209
Unearned income	(8,776)	(7,238)
Loans, net of unearned income	$12,780,899	$12,146,971

Allowance for Credit Losses
The allowance for credit losses consists of the allowance for loan losses and the reserve for unfunded lending commitments. The allowance for loan losses represents management’s estimate of incurred losses in the loan portfolio as of the balance sheet date and is recorded as a reduction to loans. The reserve for unfunded lending commitments represents management’s estimate of incurred losses in its unfunded loan commitments and is recorded in other liabilities on the consolidated balance sheet. The allowance for credit losses is increased by charges to expense, through the provision for credit losses, and decreased by charge-offs, net of recoveries.
The Corporation’s allowance for credit losses includes: (1) specific allowances allocated to loans evaluated for impairment under the Financial Accounting Standards Board’s (FASB) Accounting Standards Codification (ASC) Section 310-10-35; and (2) allowances calculated for pools of loans measured for impairment under FASB ASC Subtopic 450-20.
The Corporation segments its loan portfolio by general loan type, or "portfolio segments," as presented in the table under the heading, "Loans, Net of Unearned Income," above. Certain portfolio segments are further disaggregated and evaluated collectively for impairment based on "class segments," which are largely based on the type of collateral underlying each loan. For commercial loans, class segments include loans secured by collateral and unsecured loans. Construction loan class segments include loans secured by commercial real estate, loans to commercial borrowers secured by residential real estate and loans to individuals secured by residential real estate. Consumer loan class segments include direct consumer installment loans and indirect automobile loans.
The following table presents the components of the allowance for credit losses:

	September 30, 2013	December 31, 2012
	(in thousands)	
Allowance for loan losses	$210,486	$223,903
Reserve for unfunded lending commitments	2,352	1,536
Allowance for credit losses	$212,838	$225,439

The following table presents the activity in the allowance for credit losses:

	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
	(in thousands)			
Balance at beginning of period	$217,626	$237,316	$225,439	$258,177
Loans charged off	(18,108)	(29,966)	(61,597)	(110,765)
Recoveries of loans previously charged off	3,820	4,918	10,996	11,356
Net loans charged off	(14,288)	(25,048)	(50,601)	(99,409)
Provision for credit losses	9,500	23,000	38,000	76,500
Balance at end of period	$212,838	$235,268	$212,838	$235,268

The following table presents the activity in the allowance for loan losses by portfolio segment:

	Real Estate - Commercial Mortgage	Commercial - Industrial, Financial and Agricultural	Real Estate - Home Equity	Real Estate - Residential Mortgage	Real Estate - Construction	Consumer	Leasing and other and overdrafts	Unallocated	Total
	(in thousands)								
Three months ended September 30, 2013									
Balance at June 30, 2013	$58,696	$ 57,557	$ 25,736	$ 32,684	$ 14,471	$ 2,497	$2,925	$ 21,865	$216,431
Loans charged off	(3,724)	(9,394)	(2,365)	(767)	(598)	(473)	(787)	—	(18,108)
Recoveries of loans previously charged off	185	2,295	198	245	379	294	224	—	3,820
Net loans charged off	(3,539)	(7,099)	(2,167)	(522)	(219)	(179)	(563)	—	(14,288)
Provision for loan losses (1)	3,470	1,437	4,451	1,595	(1,221)	610	620	(2,619)	8,343
Balance at September 30, 2013	$58,627	$ 51,895	$ 28,020	$ 33,757	$ 13,031	$ 2,928	$2,982	$ 19,246	$210,486
Three months ended September 30, 2012									
Balance at June 30, 2012	$69,868	$ 71,931	$ 14,444	$ 26,711	$ 25,559	$ 1,816	$3,243	$ 22,164	$235,736
Loans charged off	(7,463)	(10,471)	(1,688)	(670)	(8,364)	(685)	(625)	—	(29,966)
Recoveries of loans previously charged off	1,317	1,693	343	25	1,040	202	298	—	4,918

Net loans charged off	(6,146)	(8,778)	(1,345)	(645)	(7,324)	(483)	(327)	—	(25,048)
Provision for loan losses (1)	8,447	4,721	2,337	2,790	3,893	530	77	381	23,176
Balance at September 30, 2012	$72,169	$ 67,874	$ 15,436	$ 28,856	$ 22,128	$ 1,863	$ 2,993	$ 22,545	$233,864
Nine months ended September 30, 2013									
Balance at December 31, 2012	$62,928	$ 60,205	$ 22,776	$ 34,536	$ 17,287	$ 2,367	$ 2,752	$ 21,052	$223,903
Loans charged off	(13,050)	(24,856)	(6,735)	(8,282)	(5,181)	(1,456)	(2,037)	—	(61,597)
Recoveries of loans previously charged off	2,754	3,430	721	442	1,794	1,206	649	—	10,996
Net loans charged off	(10,296)	(21,426)	(6,014)	(7,840)	(3,387)	(250)	(1,388)	—	(50,601)
Provision for loan losses (1)	5,995	13,116	11,258	7,061	(869)	811	1,618	(1,806)	37,184
Balance at September 30, 2013	$58,627	$ 51,895	$ 28,020	$ 33,757	$ 13,031	$ 2,928	$ 2,982	$ 19,246	$210,486
Nine months ended September 30, 2012									
Balance at December 31, 2011	$85,112	$ 74,896	$ 12,841	$ 22,986	$ 30,066	$ 2,083	$ 2,397	$ 26,090	$256,471
Loans charged off	(43,053)	(29,157)	(6,683)	(3,009)	(25,377)	(1,790)	(1,696)	—	(110,765)
Recoveries of loans previously charged off	3,286	3,046	641	169	2,643	833	738	—	11,356
Net loans charged off	(39,767)	(26,111)	(6,042)	(2,840)	(22,734)	(957)	(958)	—	(99,409)
Provision for loan losses (1)	26,824	19,089	8,637	8,710	14,796	737	1,554	(3,545)	76,802
Balance at September 30, 2012	$72,169	$ 67,874	$ 15,436	$ 28,856	$ 22,128	$ 1,863	$ 2,993	$ 22,545	$233,864

(1) The provision for loan losses excluded a $1.2 million and $816,000 increase, respectively, in the reserve for unfunded lending commitments for the three and nine months ended September 30, 2013 and was gross of a $176,000 and $302,000 decrease, respectively, in the reserve for unfunded lending commitments for the three and

nine months ended September 30, 2012. The total provision for credit losses, comprised of allocations for both funded and unfunded loans, was $9.5 million and $38.0 million, respectively, for the three and nine months ended September 30, 2013 and $23.0 million and $76.5 million, respectively, for the three and nine months ended September 30, 2012.

The following table presents loans, net of unearned income and their related allowance for loan losses, by portfolio segment:

	Real Estate - Commercial Mortgage	Commercial - Industrial, Financial and Agricultural	Real Estate - Home Equity	Real Estate - Residential Mortgage	Real Estate - Construction	Consumer	Leasing and other and overdrafts	Unallocated (1)	Total
	(in thousands)								
Allowance for loan losses at September 30, 2013									
Measured for impairment under FASB ASC Subtopic 450-20	$43,262	$38,025	$18,482	$11,494	$8,648	$2,911	$2,982	$19,246	$145,050
Evaluated for impairment under FASB ASC Section 310-10-35	15,365	13,870	9,538	22,263	4,383	17	—	N/A	65,436
	$58,627	$51,895	$28,020	$33,757	$13,031	$2,928	$2,982	$19,246	$210,486
Loans, net of unearned income at September 30, 2013									
Measured for impairment under FASB ASC Subtopic 450-20	$5,001,851	$3,593,038	$1,758,492	$1,277,200	$543,268	$296,122	$97,749	N/A	$12,567,720
Evaluated for impairment under FASB ASC Section 310-10-35	61,522	52,232	15,062	50,269	34,074	20	—	N/A	213,179
	$5,063,373	$3,645,270	$1,773,554	$1,327,469	$577,342	$296,142	$97,749	N/A	$12,780,899
Allowance for loan losses at September 30, 2012									
Measured for impairment under FASB ASC Subtopic 450-20	$46,889	$44,169	$10,120	$8,306	$14,957	$1,858	$2,980	$22,545	$151,824
Evaluated for impairment under FASB ASC Section 310-10-35	25,280	23,705	5,316	20,550	7,171	5	13	N/A	82,040
	$72,169	$67,874	$15,436	$28,856	$22,128	$1,863	$2,993	$22,545	$233,864
Loans, net of unearned income at September 30, 2012									
Measured for impairment under FASB ASC Subtopic 450-20	$4,539,370	$3,430,724	$1,594,553	$1,165,504	$554,185	$301,710	$78,031	N/A	$11,664,077

Evaluated for impairment under FASB ASC Section 310-10-35	93,139	77,122	8,903	48,818	43,173	7	21	N/A	271,183
	$4,632,509	$3,507,846	$1,603,456	$1,214,322	$597,358	$301,717	$78,052	N/A	$11,935,260

(1) The unallocated allowance, which was approximately 9% and 10% of the total allowance for credit losses as of September 30, 2013 and September 30, 2012, respectively, was, in the opinion of management, reasonable and appropriate given that the estimates used in the allocation process are inherently imprecise.

N/A – Not applicable.

During the three and nine months ended September 30, 2013, the Corporation sold $16.4 million and $41.8 million, respectively, of non-accrual commercial mortgage, commercial and construction loans to investors. During the three and nine months ended September 30, 2013, total charge-offs associated with these transactions were $6.0 million and $18.0 million, respectively. The following table presents a summary of these transactions:

	Three months ended September 30, 2013				Nine months ended September 30, 2013			
	Real Estate - Commercial mortgage	Commercial - industrial, financial and agricultural	Real Estate - Construction	Total	Real Estate - Commercial mortgage	Commercial - industrial, financial and agricultural	Real Estate - Construction	Total
	(in thousands)							
Unpaid principal balance of loans sold	$4,840	$11,950	$ 1,490	$18,280	$21,760	$23,600	$ 9,930	$55,290
Charge-offs prior to sale	—	(1,860)	—	(1,860)	(4,890)	(3,890)	(4,680)	(13,460)
Net recorded investment in loans sold	4,840	10,090	1,490	16,420	16,870	19,710	5,250	41,830
Proceeds from sale, net of selling expenses	3,310	6,020	1,050	10,380	10,410	10,050	3,400	23,860
Total charge-off upon sale	$(1,530)	$(4,070)	$ (440)	$(6,040)	$(6,460)	$(9,660)	$ (1,850)	$(17,970)
Existing allocation for credit losses on sold loans	$(320)	$(450)	$ —	$(770)	$(6,620)	$(5,780)	$ (1,320)	$(13,720)

The $16.4 million of loans sold during the third quarter of 2013 were primarily larger balance impaired commercial loans which were secured by commercial real estate. The estimated fair value of the collateral underlying these commercial loans exceeded their unpaid principal balance and, as a result, for a number of the loans sold no specific loan loss allocations under FASB ASC

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Section 310-10-35 were necessary prior to the date the loans were designated for sale. The $6.0 million charge-off recorded upon this sale occurred based on the third party's purchase offer, which was based on economic return expectations relative to the perceived lending risk of the acquired loans, and the Corporation's view of the acceptability of that purchase price in relationship to other recent loan sale transactions and the desire to eliminate these impaired loans from the portfolio.

In June 2012, the Corporation sold $44.1 million of non-accrual commercial mortgage, commercial and construction loans to an investor, resulting in a total increase to charge-offs of $21.2 million during the nine months ended September 30, 2012. The following table presents a summary of this transaction:

	Real Estate - Commercial mortgage	Commercial - industrial, financial and agricultural	Real Estate - Construction	Total
	(in thousands)			
Unpaid principal balance of loans sold	$38,450	$15,270	$ 6,280	$60,000
Charge-offs prior to sale	(8,600)	(3,750)	(3,540)	(15,890)
Net recorded investment in loans sold	29,850	11,520	2,740	44,110
Proceeds from sale, net of selling expenses	15,910	5,170	1,850	22,930
Total charge-off upon sale	$(13,940)	$(6,350)	$ (890)	$(21,180)
Existing allocation for credit losses on sold loans	$(15,090)	$(7,510)	$ (1,520)	$(24,120)

Impaired Loans

A loan is considered to be impaired if it is probable that all amounts will not be collected according to the contractual terms of the loan agreement. Impaired loans consist of all loans on non-accrual status and accruing troubled debt restructurings (TDRs). An allowance for loan losses is established for an impaired loan if its carrying value exceeds its estimated fair value. Impaired loans with balances greater than $1.0 million are evaluated individually for impairment. Impaired loans with balances less than $1.0 million are pooled and measured for impairment collectively. All loans evaluated for impairment under FASB ASC Section 310-10-35 are measured for losses on a quarterly basis. As of September 30, 2013 and December 31, 2012, substantially all of the Corporation's individually evaluated impaired loans with balances greater than $1.0 million were measured based on the estimated fair value of each loan's collateral. Collateral could be in the form of real estate, in the case of impaired commercial mortgages and construction loans, or business assets, such as accounts receivable or inventory, in the case of commercial loans. Commercial loans may also be secured by real property.

As of September 30, 2013 and 2012, approximately 79% and 78%, respectively, of impaired loans with principal balances greater than $1.0 million, whose primary collateral is real estate, were measured at estimated fair value using state certified third-party appraisals that had been updated within the preceding 12 months.

When updated certified appraisals are not obtained for loans evaluated for impairment under FASB ASC Section 310-10-35 that are secured by real estate, fair values are estimated based on the original appraisal values, as long as the original appraisal indicated a strong loan-to-value position and, in the opinion of the Corporation's internal loan evaluation staff, there has not been a significant deterioration in the collateral value since the original appraisal was performed. Original appraisals are typically used only when the estimated collateral value, as adjusted appropriately for the age of the appraisal, results in a current loan-to-value ratio that is lower than the Corporation's loan-to-value requirements for new loans, generally less than 70%.

The following table presents total impaired loans by class segment:

	September 30, 2013			December 31, 2012		
	Unpaid Principal Balance	Recorded Investment	Related Allowance	Unpaid Principal Balance	Recorded Investment	Related Allowance
	(in thousands)					
With no related allowance recorded:						
Real estate - commercial mortgage	$29,656	$24,117	$—	$44,649	$34,189	$—
Commercial - secured	35,102	28,665	—	40,409	30,112	—
Commercial - unsecured	—	—	—	132	131	—
Real estate - home equity	399	300	—	300	300	—
Real estate - residential mortgage	—	—	—	486	486	—
Construction - commercial residential	24,389	18,836	—	40,432	23,548	—
Construction - commercial	2,992	2,014	—	6,294	5,685	—
	92,538	73,932		132,702	94,451	
With a related allowance recorded:						
Real estate - commercial mortgage	45,568	37,405	15,365	69,173	55,443	21,612
Commercial - secured	28,438	22,322	12,972	52,660	39,114	17,187
Commercial - unsecured	1,303	1,245	898	2,142	2,083	1,597
Real estate - home equity	20,730	14,762	9,538	12,843	12,843	8,380
Real estate - residential mortgage	62,534	50,269	22,263	53,610	53,610	24,108
Construction - commercial residential	23,490	12,351	3,941	21,336	9,831	4,787
Construction - commercial	857	374	157	2,602	2,350	1,146
Construction - other	665	499	285	576	576	326
Consumer - direct	18	18	15	29	29	25
Consumer - indirect	2	2	2	—	—	—
Leasing and other and overdrafts	—	—	—	10	10	7
	183,605	139,247	65,436	214,981	175,889	79,175
Total	$276,143	$213,179	$65,436	$347,683	$270,340	$79,175

As of September 30, 2013 and December 31, 2012, there were $73.9 million and $94.5 million, respectively, of impaired loans that did not have a related allowance for loan loss. The estimated fair values of the collateral for these loans exceeded their carrying amount, or were previously charged down to collateral values. Accordingly, no specific valuation allowance was considered to be necessary.

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The following table presents average impaired loans by class segment:

	Three months ended September 30				Nine months ended September 30			
	2013		2012		2013		2012	
	Average Recorded Investment	Interest Income Recognized (1)	Average Recorded Investment	Interest Income Recognized (1)	Average Recorded Investment	Interest Income Recognized (1)	Average Recorded Investment	Interest Income Recognized (1)
	(in thousands)							
With no related allowance recorded:								
Real estate - commercial mortgage	$27,120	$ 113	$43,197	$ 172	$29,630	$ 394	$43,422	370
Commercial - secured	33,644	49	25,992	13	32,528	131	25,526	30
Commercial - unsecured	—	—	59	—	33	—	33	—
Real estate - home equity	300	—	583	1	253	1	466	1
Real estate - residential mortgage	747	4	1,984	17	869	25	1,115	30
Construction - commercial residential	20,809	66	25,768	60	21,730	200	28,315	128
Construction - commercial	2,021	—	2,666	6	3,500	2	2,943	12
	84,641	232	100,249	269	88,543	753	101,820	571
With a related allowance recorded:								
Real estate - commercial mortgage	37,962	158	59,239	240	46,213	563	67,064	523
Commercial - secured	22,771	34	43,420	32	29,317	115	46,743	65
Commercial - unsecured	1,260	1	2,555	2	1,502	4	2,735	4
Real estate - home equity	14,761	17	8,045	7	14,031	49	6,810	11
Real estate - residential mortgage	51,365	290	45,022	384	52,581	924	42,555	1,144
Construction - commercial residential	12,053	39	16,232	37	11,774	121	21,647	94
Construction - commercial	525	—	2,373	5	1,641	3	2,204	11
Construction - other	501	—	997	2	517	1	1,073	4
Consumer - direct	18	—	7	—	21	—	98	—
Consumer - indirect	3	—	—	—	1	—	—	—
Leasing and other and overdrafts	—	—	158	—	14	—	101	—
	141,219	539	178,048	709	157,612	1,780	191,030	1,856
Total	$225,860	$ 771	$278,297	$ 978	$246,155	$ 2,533	$292,850	2,427

(1) All impaired loans, excluding accruing TDRs, were non-accrual loans. Interest income recognized for the three and nine months ended September 30, 2013 and 2012 represents amounts earned on accruing TDRs.

Credit Quality Indicators and Non-performing Assets

The following table presents internal credit risk ratings for commercial loans, commercial mortgages and construction loans to commercial borrowers by class segment:

Pass	Special Mention	Substandard or Lower	Total

	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012
	(dollars in thousands)							
Real estate - commercial mortgage	$4,682,593	$4,255,334	$169,811	$157,640	$210,969	$251,452	$5,063,373	$4,664,426
Commercial - secured	3,183,136	3,081,215	103,085	137,277	153,313	194,952	3,439,534	3,413,444
Commercial -unsecured	197,932	187,200	3,988	5,421	3,816	6,000	205,736	198,621
Total commercial - industrial, financial and agricultural	3,381,068	3,268,415	107,073	142,698	157,129	200,952	3,645,270	3,612,065
Construction - commercial residential	145,823	156,537	41,776	52,434	57,458	79,581	245,057	288,552
Construction - commercial	247,350	211,470	2,370	2,799	9,121	12,081	258,841	226,350
Total construction (excluding Construction - other)	393,173	368,007	44,146	55,233	66,579	91,662	503,898	514,902
	$8,456,834	$7,891,756	$321,030	$355,571	$434,677	$544,066	$9,212,541	$8,791,393
% of Total	91.8 %	89.8 %	3.5 %	4.0 %	4.7 %	6.2 %	100.0 %	100.0 %

The following is a summary of the Corporation's internal risk rating categories:

- Pass: These loans do not currently pose undue credit risk and can range from the highest to average quality, depending on the degree of potential risk.

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- Special Mention: These loans constitute an undue and unwarranted credit risk, but not to a point of justifying a classification of substandard. Loans in this category are currently acceptable, but are nevertheless potentially weak.
- Substandard or Lower: These loans are inadequately protected by current sound worth and paying capacity of the borrower. There exists a well-defined weakness or weaknesses that jeopardize the normal repayment of the debt.

The Corporation believes that internal risk ratings are the most relevant credit quality indicator for the class segments presented above. The migration of loans through the various internal risk rating categories is a significant component of the allowance for credit loss methodology, which bases the probability of default on this migration. Assigning risk ratings involves judgment. Risk ratings are initially assigned to loans by loan officers and are reviewed on a regular basis by credit administration staff. The Corporation's loan review officers provide a separate assessment of risk rating accuracy. Ratings may be changed based on the ongoing monitoring procedures performed by loan officers or credit administration staff, or if specific loan review activities identify a deterioration or an improvement in the loan. The risk rating process allows management to identify riskier credits in a timely manner and to allocate resources to managing troubled accounts.

The Corporation does not assign internal risk ratings for smaller balance, homogeneous loans, such as home equity, residential mortgage, consumer, leasing and other and construction loans to individuals secured by residential real estate. For these loans, the most relevant credit quality indicator is delinquency status. The migration of these loans through the various delinquency status categories is a significant component of the allowance for credit losses methodology, which bases the probability of default on this migration.

The following table presents a summary of delinquency and non-performing status for home equity, residential mortgages, construction loans to individuals and consumer, leasing and other loans by class segment:

	Performing		Delinquent (1)		Non-performing (2)		Total	
	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012	September 30, 2013	December 31, 2012
	(dollars in thousands)							
Real estate - home equity	$1,736,645	$1,602,541	$18,218	$12,645	$18,691	$17,204	$1,773,554	$1,632,390
Real estate - residential mortgage	1,269,058	1,190,873	24,102	32,123	34,309	34,436	1,327,469	1,257,432
Construction - other	71,520	67,447	1,425	865	499	904	73,444	69,216
Consumer - direct	138,373	159,616	4,057	3,795	2,891	3,170	145,321	166,581
Consumer - indirect	147,741	140,868	2,958	2,270	122	145	150,821	143,283
Total consumer	286,114	300,484	7,015	6,065	3,013	3,315	296,142	309,864
Leasing and other and overdrafts	97,160	85,946	522	711	67	19	97,749	86,676
	$3,460,497	$3,247,291	$51,282	$52,409	$56,579	$55,878	$3,568,358	$3,355,578
% of Total	97.0 %	96.7 %	1.4 %	1.6 %	1.6 %	1.7 %	100.0 %	100.0 %

(1) Includes all accruing loans 31 days to 89 days past due.
(2) Includes all accruing loans 90 days or more past due and all non-accrual loans.

The following table presents non-performing assets:

	September 30, 2013	December 31, 2012
	(in thousands)	
Non-accrual loans	$143,012	$184,832
Accruing loans greater than 90 days past due	25,271	26,221
Total non-performing loans	168,283	211,053
Other real estate owned (OREO)	18,173	26,146
Total non-performing assets	$186,456	$237,199

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The following table presents TDRs, by class segment:

	September 30, 2013	December 31, 2012
	(in thousands)	
Real-estate - residential mortgage	$27,820	$32,993
Real-estate - commercial mortgage	22,644	34,672
Construction - commercial residential	9,841	10,564
Commercial - secured	8,060	5,624
Real estate - home equity	1,667	1,518
Commercial - unsecured	124	121
Consumer - other	11	—
Consumer - direct	—	16
Total accruing TDRs	70,167	85,508
Non-accrual TDRs (1)	30,501	31,245
Total TDRs	$100,668	$116,753

(1) Included within non-accrual loans in the preceding table detailing non-performing assets.

As of September 30, 2013 and December 31, 2012, there were $12.0 million and $7.4 million, respectively, of commitments to lend additional funds to borrowers whose loans were modified under TDRs.

The following table presents TDRs, by class segment, as of September 30, 2013 and 2012 that were modified during the three and nine months ended September 30, 2013 and 2012:

	Three months ended September 30				Nine months ended September 30			
	2013		2012		2013		2012	
	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment
	(dollars in thousands)							
Construction - commercial residential	2	$ 4,427	2	$ 741	6	$ 9,542	8	$ 11,178
Real estate - commercial mortgage	4	3,774	2	1,404	13	8,428	15	18,004
Real estate - home equity	14	1,071	1	132	42	2,928	7	692
Real estate - residential mortgage	5	836	9	3,350	44	6,861	33	11,465
Construction - commercial	—	—	1	957	—	—	1	957
Commercial - secured	—	—	7	737	7	592	14	3,944
Commercial - unsecured	—	—	—	—	1	15	—	—
Construction - other	—	—	1	335	—	—	1	335
Consumer - direct	—	—	—	—	7	2	—	—
	25	$ 10,108	23	$ 7,656	120	$ 28,368	79	$ 46,575

The following table presents TDRs, by class segment, as of September 30, 2013 and 2012 that were modified within the previous 12 months and had a payment default during the three and nine months ended September 30, 2013 and 2012:

	Three months ended September 30				Nine months ended September 30			
	2013		2012		2013		2012	
	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment
	(dollars in thousands)							
Real estate - residential mortgage	29	$ 7,224	15	$ 2,977	55	$ 14,808	26	$ 6,763
Real estate - commercial mortgage	3	1,299	6	6,358	9	3,712	7	7,442
Real estate - home equity	7	507	3	273	20	1,609	8	653
Commercial - secured	2	217	3	1,267	5	690	4	1,294
Consumer - other	—	—	1	335	—	—	1	335
Construction - commercial	—	—	1	957	—	—	1	957
Construction - commercial residential	—	—	3	836	2	608	4	2,691
	41	$ 9,247	32	$ 13,003	91	$ 21,427	51	$ 20,135

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The following table presents past due status and non-accrual loans by portfolio segment and class segment:

	September 30, 2013							
	31-59 Days Past Due	60-89 Days Past Due	≥ 90 Days Past Due and Accruing	Non-accrual	Total ≥ 90 Days	Total Past Due	Current	Total
	(in thousands)							
Real estate - commercial mortgage	$17,060	$2,951	$3,745	$38,878	$42,623	$62,634	$5,000,739	$5,063,373
Commercial - secured	9,603	1,333	1,136	42,927	44,063	54,999	3,384,535	3,439,534
Commercial - unsecured	524	308	—	1,121	1,121	1,953	203,783	205,736
Total commercial - industrial, financial and agricultural	10,127	1,641	1,136	44,048	45,184	56,952	3,588,318	3,645,270
Real estate - home equity	14,176	4,042	5,296	13,395	18,691	36,909	1,736,645	1,773,554
Real estate - residential mortgage	17,468	6,634	11,860	22,449	34,309	58,411	1,269,058	1,327,469
Construction - commercial residential	233	339	163	21,346	21,509	22,081	222,976	245,057
Construction - commercial	308	—	—	2,388	2,388	2,696	256,145	258,841
Construction - other	1,425	—	—	499	499	1,924	71,520	73,444
Total real estate - construction	1,966	339	163	24,233	24,396	26,701	550,641	577,342
Consumer - direct	2,852	1,205	2,884	7	2,891	6,948	138,373	145,321
Consumer - indirect	2,505	453	120	2	122	3,080	147,741	150,821
Total consumer	5,357	1,658	3,004	9	3,013	10,028	286,114	296,142
Leasing and other and overdrafts	294	228	67	—	67	589	97,160	97,749
	$66,448	$17,493	$25,271	$143,012	$168,283	$252,224	$12,528,675	$12,780,899

	December 31, 2012							
	31-59 Days Past Due	60-89 Days Past Due	≥ 90 Days Past Due and Accruing	Non-accrual	Total ≥ 90 Days	Total Past Due	Current	Total
	(in thousands)							
Real estate - commercial mortgage	$12,993	$8,473	$2,160	$54,960	$57,120	$78,586	$4,585,840	$4,664,426
Commercial - secured	8,013	8,030	1,060	63,602	64,662	80,705	3,332,739	3,413,444
Commercial - unsecured	461	12	199	2,093	2,292	2,765	195,856	198,621
Total commercial - industrial, financial and agricultural	8,474	8,042	1,259	65,695	66,954	83,470	3,528,595	3,612,065
Real estate - home equity	9,579	3,066	5,579	11,625	17,204	29,849	1,602,541	1,632,390
Real estate - residential mortgage	21,827	10,296	13,333	21,103	34,436	66,559	1,190,873	1,257,432
Construction - commercial residential	466	—	251	22,815	23,066	23,532	265,020	288,552
	—	—	—	8,035	8,035	8,035	218,315	226,350

Construction - commercial								
Construction - other	865	—	328	576	904	1,769	67,447	69,216
Total real estate - construction	1,331	—	579	31,426	32,005	33,336	550,782	584,118
Consumer - direct	2,842	953	3,157	13	3,170	6,965	159,616	166,581
Consumer - indirect	1,926	344	145	—	145	2,415	140,868	143,283
Total consumer	4,768	1,297	3,302	13	3,315	9,380	300,484	309,864
Leasing and other and overdrafts	662	49	9	10	19	730	85,946	86,676
	$59,634	$31,223	$26,221	$184,832	$211,053	$301,910	$11,845,061	$12,146,971

NOTE F – Mortgage Servicing Rights

The following table summarizes the changes in mortgage servicing rights (MSRs), which are included in other assets on the consolidated balance sheets:

	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
	(in thousands)			
Amortized cost:				
Balance at beginning of period	$41,750	$37,003	$39,737	$34,666
Originations of mortgage servicing rights	2,909	4,341	10,371	11,177
Amortization	(2,031)	(2,711)	(7,480)	(7,210)
Balance at end of period	$42,628	$38,633	$42,628	$38,633
Valuation allowance:				
Balance at beginning of period	$(1,690)	$(1,550)	$(3,680)	$(1,550)
Reversals (additions)	1,690	(2,130)	3,680	(2,130)
Balance at end of period	$—	$(3,680)	$—	$(3,680)
Net MSRs at end of period	$42,628	34,953	$42,628	$34,953

MSRs represent the economic value of existing contractual rights to service mortgage loans that have been sold. Accordingly, actual and expected prepayments of the underlying mortgage loans can impact the value of MSRs.

The Corporation estimates the fair value of its MSRs by discounting the estimated cash flows from servicing income, net of expense, over the expected life of the underlying loans at a discount rate commensurate with the risk associated with these assets. Expected life is based on the contractual terms of the loans, as adjusted for prepayment projections. As of September 30, 2013, the estimated fair value of MSRs was $44.9 million, resulting in the reversal of the remaining $1.7 million valuation allowance during the third quarter of 2013. An increase to the valuation allowance of $2.1 million was recorded for three and nine months ended September 30, 2012. As a result, the fair value of MSRs as of September 30, 2012 was equal to their book value.

NOTE G – Stock-Based Compensation

The fair value of equity awards granted to employees is recognized as compensation expense over the period during which employees are required to provide service in exchange for such awards. The Corporation grants equity awards to employees, consisting of stock options and restricted stock, under its Amended and Restated Equity and Cash Incentive Compensation Plan (Employee Option Plan). In addition, employees may purchase stock under the Corporation's Employee Stock Purchase Plan.

The Corporation also grants restricted stock to non-employee members of the board of directors under its 2011 Directors' Equity Participation Plan (Directors' Plan). Under the Directors' Plan, the Corporation can grant equity awards to non-employee holding company and subsidiary bank directors in the form of stock options, restricted stock or common stock.

The following table presents compensation expense and the related tax benefits for equity awards recognized in the consolidated statements of income:

	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
	(in thousands)			
Stock-based compensation expense	$979	$913	$4,186	$3,963
Tax benefit	(272)	(245)	(1,183)	(1,061)
Stock-based compensation expense, net of tax	$707	$668	$3,003	$2,902

Stock option fair values are estimated through the use of the Black-Scholes valuation methodology as of the date of grant. Stock options carry terms of up to ten years. Restricted stock fair values are equal to the average trading price of the Corporation’s stock on the date of grant. Restricted stock awards earn dividends during the vesting period, which are forfeitable if the awards do not vest. Stock options and restricted stock under the Employee Option Plan have historically been granted annually and become fully vested over or after a three year vesting period. Restricted stock awards under the Directors' Plan generally vest one year from the date of grant. Certain events, as defined in the Employee Option Plan and the Directors' Plan, result in the acceleration of the vesting of both stock options and restricted stock. As of September 30, 2013, the Employee Option Plan had 11.4 million shares reserved for future grants through 2023. As of September 30, 2013, the Directors’ Plan had 450,000 shares reserved for future grants through 2021.

NOTE H – Employee Benefit Plans

The Corporation maintains a defined benefit pension plan (Pension Plan) for certain employees, which was curtailed effective January 1, 2008. Contributions to the Pension Plan are actuarially determined and funded annually, if required. Pension Plan assets are invested in: money markets; fixed income securities, including corporate bonds, U.S. Treasury securities and common trust funds; and equity securities, including common stocks and common stock mutual funds.

The Corporation currently provides medical and life insurance benefits under a postretirement benefits plan (Postretirement Plan) to certain retired full-time employees who were employees of the Corporation prior to January 1, 1998. Certain full-time employees may become eligible for these discretionary benefits if they reach retirement age while working for the Corporation.

The Corporation recognizes the funded status of its Pension Plan and Postretirement Plan on the consolidated balance sheets and recognizes the change in that funded status through other comprehensive income.

The net periodic benefit cost for the Corporation’s Pension Plan, as determined by consulting actuaries, consisted of the following components:

	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
	(in thousands)			
Service cost (1)	$51	$39	$153	$117
Interest cost	772	806	2,316	2,418
Expected return on plan assets	(800)	(808)	(2,400)	(2,424)
Net amortization and deferral	596	420	1,788	1,260
Net periodic benefit cost	$619	$457	$1,857	$1,371

(1) The Pension Plan service cost recorded for the three and nine months ended September 30, 2013 and 2012, respectively, was related to administrative costs associated with the plan and was not due to the accrual of additional participant benefits.

The net periodic benefit cost for the Corporation’s Postretirement Plan, as determined by consulting actuaries, consisted of the following components:

	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
	(in thousands)			
Service cost	$57	$53	$171	$159
Interest cost	81	87	243	261
Expected return on plan assets	—	(1)	—	(3)
Net accretion and deferral	(91)	(91)	(273)	(273)
Net periodic benefit cost	$47	$48	$141	$144

NOTE I – Derivative Financial Instruments

The Corporation manages its exposure to certain interest rate and foreign currency price risks through the use of derivatives. None of the Corporation's outstanding derivative contracts are designated as hedges and they are not entered into for speculative purposes. Derivative instruments are carried at fair value, with changes in fair values recognized directly in earnings.

Derivative contracts create counterparty credit risk with both the Corporation's customers and with institutional derivative counterparties. The Corporation manages credit risk through its credit approval processes, monitoring procedures and obtaining adequate collateral, when appropriate.

Mortgage Banking Derivatives

In connection with its mortgage banking activities, the Corporation enters into commitments to originate certain fixed rate residential mortgage loans for customers, also referred to as interest rate locks. In addition, the Corporation enters into forward commitments for the future sales or purchases of mortgage-backed securities to or from third-party counterparties to hedge the effect of changes in interest rates on the values of both the interest rate locks and mortgage loans held for sale. Forward sales commitments may also be in the form of commitments to sell individual mortgage loans or interest rate locks at a fixed price at a future date. The amount necessary to settle each interest rate lock is based on the price that secondary market investors would pay for loans with similar characteristics, including interest rate and term, as of the date fair value is measured. Gross derivative assets and liabilities are recorded within other assets and other liabilities, respectively, on the consolidated balance sheets, with changes in fair values during the period recorded within mortgage banking income on the consolidated statements of income.

Interest Rate Swaps

The Corporation executes interest rate swaps with certain qualifying commercial loan customers to meet their interest rate risk management needs. The Corporation simultaneously enters into interest rate swaps with dealer counterparties, with identical notional amounts and terms. The net result of these interest rate swaps is that the customer pays a fixed rate of interest and the Corporation receives a floating rate. These interest rate swaps are derivative financial instruments that are recorded at their fair values within other assets and liabilities on the consolidated balance sheets. Changes in fair values during the period are recorded within other expense on the consolidated statements of income.

Foreign Exchange Contracts

The Corporation enters into foreign exchange contracts to accommodate the needs of its customers. Foreign exchange contracts are commitments to buy or sell foreign currency on a future date at a contractual price. The Corporation offsets its foreign exchange contract exposure with customers by entering into contracts with third-party correspondent financial institutions to mitigate its exposure to fluctuations in foreign currency exchange rates. The Corporation also holds certain amounts of foreign currency with international correspondent banks. The Corporation's policy limits the total net foreign currency open position, which includes all outstanding contracts and foreign account balances, to less than $500,000. Gross derivative assets and liabilities are recorded within other assets and other liabilities, respectively, on the consolidated balance sheets, with changes in fair values during the period recorded within other service charges and fees on the consolidated statements of income.

The following table presents a summary of the notional amounts and fair values of derivative financial instruments:

	September 30, 2013		December 31, 2012	
	Notional Amount	Asset (Liability) Fair Value	Notional Amount	Asset (Liability) Fair Value
	(in thousands)			
Interest Rate Locks with Customers				
Positive fair values	$120,547	$3,100	$314,416	$6,912
Negative fair values	5,790	(50)	9,714	(155)
Net interest rate locks with customers		3,050		6,757
Forward Commitments				
Positive fair values	6,002	16	79,152	707
Negative fair values	130,498	(2,193)	236,500	(915)
Net forward commitments		(2,177)		(208)
Interest Rate Swaps with Customers				
Positive fair values	115,409	3,460	130,841	7,090
Negative fair values	84,625	(1,640)	—	—
Net interest rate swaps with customers		1,820		7,090
Interest Rate Swaps with Dealer Counterparties				
Positive fair values	84,625	1,640	—	—
Negative fair values	115,409	(3,460)	130,841	(7,090)
Net Interest rate swaps with dealer counterparties		(1,820)		(7,090)
Foreign Exchange Contracts with Customers				
Positive fair values	4,362	64	1,810	137
Negative fair values	16,770	(450)	9,851	(348)
Net foreign exchange contracts with customers		(386)		(211)
Foreign Exchange Contracts with Correspondent Banks				
Positive fair values	25,418	1,013	59,368	1,064
Negative fair values	10,805	(160)	37,865	(1,121)
Net foreign exchange contracts with correspondent banks		853		(57)
Net derivative fair value asset		$1,340		$6,281

The following table presents a summary of the fair value gains and losses on derivative financial instruments:

	Three months ended September 30		Nine months ended September 30	
	2013	2012	2013	2012
	(in thousands)			
Interest rate locks with customers	$4,717	$3,933	$(3,707)	$8,985
Forward commitments	(12,244)	(3,255)	(1,969)	(5,068)
Interest rate swaps with customers	1,009	1,189	(5,270)	4,229
Interest rate swaps with dealer counterparties	(1,009)	(1,189)	5,270	(4,229)
Foreign exchange contracts with customers	(344)	1,654	(175)	2,523
Foreign exchange contracts with correspondent banks	(50)	(1,331)	910	(1,717)
Net fair value gains (losses) on derivative financial instruments	$(7,921)	$1,001	$(4,941)	$4,723

NOTE J – Balance Sheet Offsetting

Certain financial assets and liabilities may be eligible for offset on the consolidated balance sheets as they are subject to master netting arrangements or similar agreements. The Corporation elects to not offset assets and liabilities subject to such arrangements on the consolidated financial statements.

The Corporation is a party to interest rate swap transactions with financial institution counterparties and customers, discussed in detail within Note I, "Derivative Financial Instruments." Under these agreements, the Corporation has the right to net settle multiple contracts with the same counterparty in the event of default on, or termination of, any one contract. Cash collateral is posted by the party with a net liability position in accordance with contract thresholds and can be used to settle the fair value of the interest rate swap agreements in the event of default.

The Corporation also enters into agreements with customers in which it sells securities subject to an obligation to repurchase the same or similar securities, referred to as repurchase agreements. Under these agreements, the Corporation may transfer legal control over the assets but still maintain effective control through agreements that both entitle and obligate the Corporation to repurchase the assets. Therefore, repurchase agreements are reported as secured borrowings, classified within short-term borrowings on the consolidated balance sheets, while the securities underlying the repurchase agreements remain classified with investment securities on the consolidated balance sheets. The Corporation has no intention of setting off these amounts, therefore, these repurchase agreements are not eligible for offset.

The following table presents the Corporation's financial instruments that are eligible for offset, and the effects of offsetting, on the consolidated balance sheets:

	Gross Amounts Recognized on the Consolidated Balance Sheets	Gross Amounts Not Offset on the Consolidated Balance Sheets		
		Financial Instruments (1)	Cash Collateral (2)	Net Amount
	(in thousands)			
September 30, 2013				
Interest rate swap assets	$5,100	$(1,837)	$—	$3,263
Interest rate swap liabilities	$5,100	$(1,837)	$(1,800)	$1,463
December 31, 2012				
Interest rate swap assets	$7,090	$—	$—	$7,090
Interest rate swap liabilities	$7,090	$—	$(7,090)	$—

(1) For interest rate swap assets, amounts represent any derivative liability fair values that could be offset in the event of counterparty or customer default. For interest rate swap liabilities, amounts represent any derivative asset fair values that could be offset in the event of counterparty or customer default.

(2) Amounts represent cash collateral posted on interest rate swap transactions with financial institution counterparties. Interest rate swaps with customers are collateralized by the underlying loans to those borrowers.

NOTE K – Commitments and Contingencies

Commitments

The Corporation is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers.

Those financial instruments include commitments to extend credit and letters of credit, which involve, to varying degrees, elements of credit risk and interest rate risk in excess of the amounts recognized on the Corporation’s consolidated balance sheets. Exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and letters of credit is represented by the outstanding amount of those instruments.

The outstanding amounts of commitments to extend credit and letters of credit were as follows:

	September 30, 2013	December 31, 2012
	(in thousands)	
Commitments to extend credit	$4,301,326	$4,011,741
Standby letters of credit	393,023	425,095
Commercial letters of credit	35,036	26,191

The Corporation records a reserve for unfunded lending commitments, which represents management’s estimate of losses associated with unused commitments to extend credit. See Note E, "Loans and Allowance for Credit Losses," for additional details.

Residential Lending

Residential mortgages are originated and sold by the Corporation and consist primarily of conforming, prime loans sold to government sponsored agencies, such as the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac). The Corporation also sells a portion of prime loans to non-government sponsored agency investors.

The Corporation provides customary representations and warranties to investors that specify, among other things, that the loans have been underwritten to the standards established by the investor. The Corporation may be required to repurchase a loan or reimburse the investor for a credit loss incurred on a loan if it is determined that the representations and warranties have not been met. This generally results from an underwriting or documentation deficiency. As of September 30, 2013 and December 31, 2012, the reserves for losses on these loans were approximately $4.9 million and $2.4 million, respectively.

From 2000 to 2011, the Corporation sold loans to the FHLB under its Mortgage Partnership Finance Program (MPF Program). No loans were sold under this program in 2013 or 2012. The Corporation provided a "credit enhancement" for residential mortgage loans sold under the MPF Program whereby it would assume credit losses in excess of a defined "First Loss Account" (FLA) balance, up to specified amounts. The FLA is funded by the FHLB based on a percentage of the outstanding principal balance of loans sold. As of September 30, 2013, the unpaid principal balance of loans sold under the MPF Program was approximately $186 million. As of September 30, 2013 and December 31, 2012, the reserve for estimated credit losses related to loans sold under the MPF Program was $2.9 million and $3.6 million, respectively. Required reserves are calculated based on delinquency status and estimated loss rates established through the Corporation's existing allowance for credit losses methodology.

As of September 30, 2013 and December 31, 2012, the total reserve for losses on residential mortgage loans sold was $7.8 million and $6.0 million, respectively, including both reserves for credit losses under the MPF Program and reserves for representation and warranty exposures. Management believes that the reserves recorded as of September 30, 2013 are adequate. However, declines in collateral values, the identification of additional loans to be repurchased, or a deterioration in the credit quality of loans sold under the MPF Program could necessitate additional reserves in the future.

Other Contingencies

The Corporation and its subsidiaries are involved in various legal proceedings in the ordinary course of business. The Corporation evaluates the possible impact of pending litigation based on, among other factors, the advice of counsel, available insurance coverage and recorded liabilities and reserves for probable legal liabilities and costs. As of the date of this report, the Corporation believes that any liabilities, individually or in the aggregate, which may result from the final outcomes of pending proceedings will not have a material adverse effect on the financial position, the operating results and/or the liquidity of the Corporation. However, litigation is often unpredictable, and the actual results of litigation cannot be determined with certainty.

NOTE L – Fair Value Option

FASB ASC Subtopic 825-10 permits entities to measure many financial instruments and certain other items at fair value and requires certain disclosures for amounts for which the fair value option is applied. The Corporation has elected to measure mortgage loans held for sale at fair value to more accurately reflect the financial results of its mortgage banking activities in its consolidated financial statements. Derivative financial instruments related to these activities are also recorded at fair value, as noted within Note I, "Derivative Financial Instruments." The Corporation determines fair value for its mortgage loans held for sale based on the price that secondary market investors would pay for loans with similar characteristics, including interest rate and term, as of the date fair value is measured. Changes in fair values during the period are recorded as components of mortgage banking income on the consolidated statements of income. Interest income earned on mortgage loans held for sale is recorded within interest income on the consolidated statements of income.

The following table presents a summary of the Corporation’s mortgage loans held for sale:

	September 30, 2013	December 31, 2012
	(in thousands)	

Cost	$37,903	$65,745
Fair value	39,273	67,899

During the three months ended September 30, 2013, the Corporation recorded gains related to changes in fair values of mortgage loans held for sale of $2.6 million. During the nine months ended September 30, 2013, the Corporation recorded losses related to changes in fair values of mortgage loans held for sale of $784,000. During the three and nine months ended September 30, 2012, the Corporation recorded gains related to changes in fair values of mortgage loans held for sale of $1.5 million and $2.5 million, respectively.

NOTE M – Fair Value Measurements

FASB ASC Topic 820 establishes a fair value hierarchy for the inputs to valuation techniques used to measure fair value into the following three categories (from highest to lowest priority):

- Level 1 – Inputs that represent quoted prices for identical instruments in active markets.
- Level 2 – Inputs that represent quoted prices for similar instruments in active markets, or quoted prices for identical instruments in non-active markets. Also includes valuation techniques whose inputs are derived principally from observable market data other than quoted prices, such as interest rates or other market-corroborated means.
- Level 3 – Inputs that are largely unobservable, as little or no market data exists for the instrument being valued.

The Corporation has categorized all assets and liabilities measured at fair value on both a recurring and nonrecurring basis into the above three levels.

The following tables present summaries of the Corporation’s assets and liabilities measured at fair value on a recurring basis and reported on the consolidated balance sheets:

	September 30, 2013			
	Level 1	Level 2	Level 3	Total
	(in thousands)			
Mortgage loans held for sale	$—	$39,273	$—	$39,273
Available for sale investment securities:				
Equity securities	43,728	—	—	43,728
U.S. Government securities	—	2,250	—	2,250
U.S. Government sponsored agency securities	—	835	—	835
State and municipal securities	—	293,513	—	293,513
Corporate debt securities	—	97,580	8,971	106,551
Collateralized mortgage obligations	—	1,082,977	—	1,082,977
Mortgage-backed securities	—	914,230	—	914,230
Auction rate securities	—	—	154,510	154,510
Total available for sale investments	43,728	2,391,385	163,481	2,598,594
Other assets	15,815	8,216	—	24,031
Total assets	$59,543	$2,438,874	$163,481	$2,661,898
Other liabilities	$15,348	$7,342	$—	$22,690

	December 31, 2012			
	Level 1	Level 2	Level 3	Total
	(in thousands)			
Mortgage loans held for sale	$—	$67,899	$—	$67,899
Available for sale investment securities:				
Equity securities	50,873	—	—	50,873
U.S. Government securities	—	325	—	325
U.S. Government sponsored agency securities	—			