CITY NATIONAL CORP
Form 10-Q
November 09, 2009
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2009

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NUMBER: 1-10521

CITY NATIONAL CORPORATION

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

Delaware	**95-2568550**
(State of Incorporation)	(I.R.S. Employer Identification No.)

City National Plaza

555 South Flower Street, Los Angeles, California, 90071

(Address of principal executive offices)(Zip Code)

(213) 673-7700

(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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 the filing requirements for at least the past 90 days. Yes x No o

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No o

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). o Yes x No

As of October 30, 2009, there were 51,503,312 shares of Common Stock outstanding.

Table of Contents

TABLE OF CONTENTS

PART I		
Item 1.	Financial Statements	3
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	40
Item 3.	Quantitative and Qualitative Disclosures about Market Risk	66
Item 4.	Controls and Procedures	68
PART II		
Item 1A.	Risk Factors	70
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	70
Item 4.	Submission of Matters to a Vote of Security Holders	71
Item 6.	Exhibits	71

Table of Contents

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CITY NATIONAL CORPORATION

CONSOLIDATED BALANCE SHEETS

(in thousands, except share amounts)		September 30, 2009 (Unaudited)		December 31, 2008		September 30, 2008 (Unaudited)
Assets						
Cash and due from banks	$	348,958	$	279,921	$	428,557
Due from banks - interest-bearing		767,362		144,344		95,993
Federal funds sold		240,000				
Securities available-for-sale - cost $3,480,659, $2,239,184, and $2,230,192 at September 30, 2009, December 31, 2008 and September 30, 2008, respectively:						
Securities pledged as collateral		226,497		223,506		214,762
Held in portfolio		3,285,575		1,921,364		1,945,156
Trading securities		188,904		295,598		310,251
Loans and leases		12,168,490		12,444,259		12,278,517
Less: Allowance for loan and lease losses		265,005		224,046		208,046
Net loans and leases		11,903,485		12,220,213		12,070,471
Premises and equipment, net		126,097		131,294		127,361
Deferred tax asset		173,752		226,854		152,445
Goodwill		491,501		459,418		460,137
Customer-relationship intangibles, net		41,866		40,619		52,160
Bank-owned life insurance		76,155		74,575		73,930
Affordable housing investments		92,170		74,577		72,453
Customers acceptance liability		3,476		1,714		2,954
Other real estate owned		43,969		11,388		2,279
Other assets		390,837		350,130		321,959
Total assets	$	18,400,604	$	16,455,515	$	16,330,868
Liabilities						
Demand deposits	$	7,441,898	$	6,140,619	$	5,744,863
Interest checking deposits		1,776,643		988,313		847,921
Money market deposits		4,220,737		3,699,900		3,822,418
Savings deposits		276,087		146,590		143,252
Time deposits-under $100,000		210,344		234,669		233,173
Time deposits-$100,000 and over		1,182,734		1,442,033		1,376,033
Total deposits		15,108,443		12,652,124		12,167,660
Federal funds purchased and securities sold under repurchase agreements		231,903		908,157		1,272,359
Other short-term borrowings		720		124,500		630,673
Subordinated debt		341,587		161,595		157,769
Long-term debt		233,536		246,554		231,321
Reserve for off-balance sheet credit commitments		19,576		22,703		23,384
Acceptances outstanding		3,476		1,714		2,954
Other liabilities		192,974		262,923		144,348
Total liabilities		16,132,215		14,380,270		14,630,468
Redeemable noncontrolling interest		49,897		44,811		52,556
Commitments and contingencies						

Equity			
Preferred Stock; 5,000,000 shares authorized; 400,000 shares issued; aggregate liquidation preference of $400,000 as of September 30, 2009 and December 31, 2008, respectively	391,593	390,089	
Common Stock, par value $1.00 per share; 75,000,000 shares authorized; 53,885,886, 50,961,457, and 50,966,264 shares issued at September 30, 2009, December 31, 2008 and September 30, 2008, respectively	53,886	50,961	50,966
Additional paid-in capital	514,904	389,077	371,279
Accumulated other comprehensive income (loss)	24,329	(48,022)	(38,071)
Retained earnings	1,363,176	1,379,624	1,396,400
Treasury shares, at cost - 2,386,899, 2,413,039 and 2,434,941 shares at September 30, 2009, December 31, 2008 and September 30, 2008, respectively	(154,245)	(156,736)	(158,193)
Total common shareholders equity	1,802,050	1,614,904	1,622,381
Total shareholders equity	2,193,643	2,004,993	1,622,381
Noncontrolling interest	24,849	25,441	25,463
Total equity	2,218,492	2,030,434	1,647,844
Total liabilities and equity	$ 18,400,604	$ 16,455,515	$ 16,330,868

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents

CITY NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(in thousands, except per share amounts)	For the three months ended September 30, 2009	2008	For the nine months ended September 30, 2009	2008
Interest Income				
Loans and leases	$ 145,756	$ 168,824	$ 433,636	$ 514,293
Securities available-for-sale	34,243	25,760	90,835	79,601
Trading securities	31	557	465	1,533
Due from banks - interest-bearing	259	440	705	1,491
Federal funds sold and securities purchased under resale agreements	130	25	145	147
Total interest income	180,419	195,606	525,786	597,065
Interest Expense				
Deposits	12,854	26,689	48,483	92,811
Federal funds purchased and securities sold under repurchase agreements	2,016	7,767	6,279	25,009
Subordinated debt	3,220	1,489	5,294	5,304
Other long-term debt	988	2,154	3,803	7,440
Other short-term borrowings		4,703	113	15,364
Total interest expense	19,078	42,802	63,972	145,928
Net interest income	161,341	152,804	461,814	451,137
Provision for credit losses	85,000	35,000	205,000	87,000
Net interest income after provision for credit losses	76,341	117,804	256,814	364,137
Noninterest Income				
Trust and investment fees	32,289	33,457	83,342	103,993
Brokerage and mutual fund fees	6,041	19,470	22,443	55,601
Cash management and deposit transaction charges	13,142	12,392	39,143	35,712
International services	7,895	8,202	22,416	24,065
Bank-owned life insurance	639	824	2,373	2,107
Loss on sale of other assets	(173)	(198)	(130)	(390)
Gain (loss) on sale of securities	3,445	(536)	3,795	16
Other	6,345	8,403	21,366	22,190
Impairment loss on securities:				
Total other-than-temporary impairment loss on securities	(20,588)	(31,936)	(34,161)	(31,936)
Less: Portion of loss recognized in other comprehensive income	19,810		19,810	
Net impairment loss recognized in earnings	(778)	(31,936)	(14,351)	(31,936)
Total noninterest income	68,845	50,078	180,397	211,358
Noninterest Expense				
Salaries and employee benefits	80,937	89,373	235,023	267,072
Net occupancy of premises	12,613	12,719	37,433	36,693
Legal and professional fees	8,545	8,332	24,014	24,423
Information services	7,342	6,576	20,814	19,170
Depreciation and amortization	6,472	5,502	18,417	16,464
Marketing and advertising	4,615	5,653	14,034	16,608
Office services and equipment	3,610	3,683	11,136	11,468
Amortization of intangibles	1,726	2,238	5,237	6,197
Other real estate owned	2,231	23	4,481	343

FDIC assessments		5,308		2,188		22,237		4,358
Other operating		10,366		9,910		28,058		24,989
Total noninterest expense		143,765		146,197		420,884		427,785
Income before income taxes		1,421		21,685		16,327		147,710
Income taxes		(6,966)		3,974		(6,320)		44,960
Net income	$	8,387	$	17,711	$	22,647	$	102,750
Less: Net income attributable to noncontrolling interest		348		1,160		375		6,728
Net income attributable to City National Corporation	$	8,039	$	16,551	$	22,272	$	96,022
Less: Dividends on preferred stock		5,502				16,504		
Net income available to common shareholders	$	2,537	$	16,551	$	5,768	$	96,022
Net income per common share, basic	$	0.05	$	0.34	$	0.11	$	1.99
Net income per common share, diluted	$	0.05	$	0.34	$	0.11	$	1.98
Shares used to compute income per common share, basic		51,482		47,934		49,855		47,871
Shares used to compute income per common share, diluted		51,660		48,207		49,987		48,178
Dividends per common share	$	0.10	$	0.48	$	0.45	$	1.44

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents

CITY NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)	For the nine months ended September 30, 2009	2008
Cash Flows From Operating Activities		
Net income attributable to City National Corporation	$ 22,272	$ 96,022
Adjustments to net income:		
Provision for credit losses	205,000	87,000
Amortization of intangibles	5,237	6,197
Depreciation and amortization	18,417	16,464
Amortization of cost and discount on long-term debt	436	457
Share-based employee compensation expense	10,786	10,862
Loss on sale of other assets	130	390
Gain on sale of securities	(3,795)	(16)
Impairment loss on securities	14,351	31,936
Other, net	2,460	27,938
Net change in:		
Trading securities	113,094	(16,896)
Deferred income tax benefit	(470)	(23,042)
Other assets and other liabilities, net	(143,336)	(101,692)
Net cash provided by operating activities	244,582	135,620
Cash Flows From Investing Activities		
Purchase of securities available-for-sale	(2,440,987)	(218,445)
Sales of securities available-for-sale	554,834	94,076
Maturities and paydowns of securities	618,141	346,583
Loan originations, net of principal collections	73,617	(699,027)
Net payments for premises and equipment	(10,432)	(25,758)
Acquisition of Lee Munder Capital Group, LLC, net of cash acquired	(18,328)	
Other investing activities, net	(894)	18,410
Net cash used in investing activities	(1,224,049)	(484,161)
Cash Flows From Financing Activities		
Net increase in deposits	2,456,319	345,155
Net decrease in federal funds purchased and securities sold under repurchase agreements	(676,254)	(272,052)
Net (decrease) increase in short-term borrowings, net of transfers from long-term debt	(123,780)	530,673
Net increase (decrease) in other borrowings	170,900	(116,854)
Proceeds from exercise of stock options	1,150	19,555
Tax benefit from exercise of stock options	141	3,821
Stock repurchases		(21,655)
Issuance of common stock	119,929	
Cash dividends paid	(36,883)	(69,621)
Net cash provided by financing activities	1,911,522	419,022
Net increase in cash and cash equivalents	932,055	70,481
Cash and cash equivalents at beginning of year	424,265	454,069

Cash and cash equivalents at end of period	$	1,356,320	$	524,550
Supplemental Disclosures of Cash Flow Information:				
Cash paid during the period for:				
Interest	$	63,804	$	159,427
Income taxes		17,689		93,015
Non-cash investing activities:				
Transfer of loans to other real estate owned		47,715		14,891
Transfer from securities available-for-sale to trading securities		6,400		

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents

CITY NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

AND COMPREHENSIVE INCOME

(Unaudited)

	City National Corporation Shareholders Equity								
(in thousands, except share amounts)	**Shares issued**	**Preferred stock**	**Common stock**	**Additional paid-in capital**	**Accumulated other comprehensive income (loss)**	**Retained earnings**	**Treasury shares**	**Non-controlling interest**	**Total equity**
Balance, January 1, 2008	50,824,178	$	$ 50,824	$ 374,700	$ (9,349)	$ 1,369,999	$ (176,035)	$ 25,583	$ 1,635,722
Net income						96,022		1,806	97,828
Other comprehensive loss, net of tax:									
Amortization of prior service cost					(39)				(39)
Net unrealized loss on securities available-for-sale, net of taxes of $20.2 million and reclassification of $0.1 million net gain included in net income					(27,937)				(27,937)
Net unrealized loss on cash flow hedges, net of taxes of $0.5 million and reclassification of $2.3 million net gain included in net income					(746)				(746)
Total comprehensive income								1,806	69,106
Dividends and distributions to noncontrolling interest								(1,926)	(1,926)
Issuance of shares under share-based compensation plans	142,086		142	(20,084)			39,497		19,555
Share-based employee compensation expense				10,698					10,698
Tax benefit from share-based compensation plans				3,821					3,821
Cash dividends paid						(69,621)			(69,621)
Repurchased shares, net							(21,655)		(21,655)
Net change in deferred compensation plans				745					745
Change in redeemable noncontrolling interest				1,399					1,399
Balance, September 30, 2008	50,966,264	$	$ 50,966	$ 371,279	$ (38,071)	$ 1,396,400	$ (158,193)	$ 25,463	$ 1,647,844
Balance, January 1, 2009	50,961,457	$ 390,089	$ 50,961	$ 389,077	$ (48,022)	$ 1,379,624	$ (156,736)	$ 25,441	$ 2,030,434
Net income						22,272		1,625	23,897
Other comprehensive income, net of tax:									
Amortization of prior service cost					119				119
Non-credit related impairment loss on investment securities, net of taxes of $8.3 million					(11,523)				(11,523)
Net unrealized gain on securities available-for-sale, net of taxes of $60.9 million and reclassification of $2.0 million net loss included in net income					84,657				84,657
Net unrealized loss on cash flow hedges, net of taxes of $0.6 million and reclassification of $5.2 million net gain included in net income					(902)				(902)

Total comprehensive income								1,625	96,248
Dividends and distributions to noncontrolling interest								(1,717)	(1,717)
Issuance of common stock	3,220,000		3,220	116,409					119,629
Issuance of shares under share-based compensation plans	(295,571)		(295)	(1,814)			2,491		382
Preferred stock accretion		1,504				(1,504)			
Share-based employee compensation expense				10,693					10,693
Tax benefit from share-based compensation plans				(714)					(714)
Cash dividends:									
Preferred						(15,000)			(15,000)
Common						(22,216)			(22,216)
Net change in deferred compensation plans				492					492
Change in redeemable noncontrolling interest				761					761
Other								(500)	(500)
Balance, September 30, 2009	53,885,886	$ 391,593	$ 53,886	$ 514,904	$ 24,329	$ 1,363,176	$ (154,245)	$ 24,849	$ 2,218,492

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents

CITY NATIONAL CORPORATION

NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Summary of Significant Accounting Policies

Organization

City National Corporation (the Corporation) is the holding company for City National Bank (the Bank). The Bank delivers banking, trust and investment services through 63 offices in Southern California, the San Francisco Bay area, Nevada and New York City. Additionally, the Corporation delivers investment and wealth advisory services through its wealth advisory affiliates. The Corporation also has an unconsolidated subsidiary, Business Bancorp Capital Trust I. The Corporation is approved as a financial holding company pursuant to the Gramm-Leach-Bliley Act of 1999. References to the Company mean the Corporation, Bank, all subsidiaries and affiliates together.

Consolidation

The consolidated financial statements of the Company include the accounts of the Corporation, its non-bank subsidiaries, the Bank and the Bank s wholly owned subsidiaries, after the elimination of all material intercompany transactions. Preferred stock and equity ownership of others are reflected as Redeemable noncontrolling interest and Noncontrolling interest in the consolidated balance sheets. The related noncontrolling share of earnings is shown as Net income attributable to noncontrolling interest in the consolidated statements of income.

The Company s investment management and wealth advisory affiliates are organized as limited liability companies. The Corporation generally owns a majority position in each affiliate and certain management members of each affiliate own the remaining shares. The Corporation has contractual arrangements with its affiliates whereby a percentage of revenue is allocable to fund affiliate operating expenses (operating share) while the remaining portion of revenue (distributable revenue) is allocable to the Corporation and the noncontrolling owners. All majority-owned affiliates are consolidated. The Corporation s interest in one investment management affiliate in which it holds a noncontrolling share is accounted for using the equity method. Additionally, the Company has various interests in variable interest entities that are not required to be consolidated. See Note 13 for a more detailed discussion on variable interest entities.

Use of Estimates

The Company s accounting and reporting policies conform to generally accepted accounting principles (GAAP) and practices in the financial services industry. To prepare the financial statements in conformity with GAAP, management must make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, and income and expenses during the reporting period.

Circumstances and events that differ significantly from those underlying the Company s estimates and assumptions could cause actual financial results to differ from those estimates. The material estimates included in the financial statements relate to the allowance for loan and lease losses, the reserve for off-balance sheet credit commitments, valuation of stock options and restricted stock, income taxes, goodwill and intangible asset impairment, available-for-sale securities impairment and the valuation of financial assets and liabilities reported at fair value. The Company has applied its critical accounting policies and estimation methods consistently in all periods presented in these financial statements. The allowance for loan and lease losses reflects management s ongoing assessment of the credit quality of the Company s portfolio, which is affected by a broad range of economic factors, including weak valuations in commercial real estate. Additional factors affecting the provision include net loan charge-offs, nonaccrual loans, specific reserves, risk-rating migration and changes in the portfolio size. The Company s estimates and assumptions are expected to change as changes in market conditions and the Company s portfolio occur in subsequent periods.

Basis of Presentation

The Company is on the accrual basis of accounting for income and expense. The results of operations reflect any interim adjustments, all of which are of a normal recurring nature, unless otherwise disclosed in this Form 10-Q, and which, in the opinion of management, are necessary for a fair presentation of the results for the interim periods presented. In accordance with the usual practice of banks, assets and liabilities of individual trust, agency and fiduciary funds have not been included in the financial statements. These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2008.

Table of Contents

Note 1. Summary of Significant Accounting Policies (continued)

The results for the 2009 interim period are not necessarily indicative of the results expected for the full year. The Company has not made any significant changes in its critical accounting policies or in its estimates and assumptions from those disclosed in its 2008 Annual Report other than the adoption of new accounting pronouncements and other authoritative guidance that became effective for the Company on January 1, 2009. Refer to *Accounting Pronouncements* below for discussion of accounting pronouncements adopted in 2009.

Certain prior period amounts have been reclassified or restated to conform to the current period presentation.

On July 1, 2009, the Financial Accounting Standards Board Accounting Standards Codification (ASC) became the official source of nongovernmental authoritative U.S. GAAP other than guidance issued by the Securities and Exchange Commission (SEC). The ASC organizes GAAP by Topic-Subtopic-Section-Paragraph. References to GAAP contained in this Form 10-Q reflect the ASC reference structure.

During the nine months ended September 30, 2009, the Company made certain changes to the following accounting policies as a result of the Company s adoption of new accounting pronouncements and other considerations:

Goodwill and Customer-Relationship Intangible Assets

The Company applies the acquisition method of accounting for acquisitions in accordance with the revised guidance under ASC Topic 805, *Business Combinations*, which became effective January 1, 2009. Previously, acquisitions were accounted for under the purchase method. Under the acquisition method, the acquiring entity in a business combination recognizes 100 percent of the assets acquired and liabilities assumed, including contingent consideration, in the transaction at their acquisition date fair values. Management utilizes valuation techniques based on discounted cash flow analysis to determine these fair values. Any excess of the purchase price over amounts allocated to acquired assets, including identifiable intangible assets, and liabilities assumed is recorded as goodwill. Intangible assets include core deposit intangibles and client advisory contract intangibles (combined, customer-relationship intangibles) originating from acquisitions of financial services firms. Core deposit intangibles are amortized over a range of four to eight years and client advisory contract intangibles are amortized over various periods ranging from four to 20 years. The weighted-average amortization period for the contract intangibles is 17.2 years.

Goodwill and customer-relationship intangibles are evaluated for impairment at least annually or more frequently if events or circumstances, such as changes in economic or market conditions, indicate that potential impairment exists. Given the volatility in the current economic environment, goodwill and customer-relationship intangibles are evaluated for impairment on a quarterly basis. Goodwill is tested for impairment at the reporting unit level. A reporting unit is an operating segment or one level below an operating segment for which discrete financial information is available and regularly reviewed by management. Fair values of reporting units are determined using methods consistent with current market practices for valuing similar types of businesses. Valuations are generally based on market multiples of net income or gross revenue combined with an analysis of expected near and long-term financial performance. Management utilizes market information including market comparables and recent merger and acquisition transactions to validate the reasonableness of its valuations. If the fair value of the reporting unit, including goodwill, is determined to be less than the carrying amount of the reporting unit, a further test is required to measure the amount of impairment. If an impairment loss exists, the carrying amount of the goodwill is adjusted to a new cost basis. Subsequent reversal of a previously recognized goodwill impairment loss is prohibited.

Impairment testing of customer-relationship intangibles is performed at the individual asset level. Impairment exists when the carrying amount of an intangible asset is not recoverable and exceeds its fair value. The carrying amount of an intangible asset is not recoverable when the carrying amount of the asset exceeds the sum of undiscounted cash flows (cash inflows less cash outflows) associated with the use and/or disposition of the asset. An impairment loss is measured as the amount by which the carrying amount of the asset exceeds its fair value. The fair value of core deposit intangibles is determined using market-based core deposit premiums from recent deposit sale transactions. The fair value of client advisory contracts is based on discounted expected future cash flows. Management makes certain estimates and assumptions in determining the expected future cash flows from customer-relationship intangibles including account attrition, expected lives, discount rates, interest rates, servicing costs and other factors. Significant changes in these estimates and assumptions could adversely impact the valuation of these intangible assets. If an impairment loss exists, the carrying amount of the intangible asset is adjusted to a new cost basis. The new cost basis is amortized over the remaining useful life of the asset.

Table of Contents

Note 1. Summary of Significant Accounting Policies (Continued)

Earnings per Common Share

The Company calculates earnings per common share (EPS) using the two-class method in accordance with ASC Topic 260, *Earnings per Share* (ASC 260), effective January 1, 2009 with retrospective application to all prior-period earnings per share data presented. Refer to *Accounting Pronouncements* below. The two-class method requires the Company to present EPS as if all of the earnings for the period are distributed to common shareholders and any participating securities, regardless of whether any actual dividends or distributions are made. Under ASC Topic 260, all outstanding unvested share-based payment awards that contain rights to nonforfeitable dividends are considered participating securities. The Company grants restricted shares under a share-based compensation plan that qualify as participating securities. Restricted shares issued under the Company s share-based compensation plan are entitled to dividends at the same rate as common stock.

Basic EPS are computed by dividing distributed and undistributed earnings available to common shareholders by the weighted average number of common shares outstanding for the period. Distributed and undistributed earnings available to common shareholders represent net income reduced by preferred stock dividends and distributed and undistributed earnings available to participating securities. Common shares outstanding include common stock and vested restricted stock awards. Diluted EPS reflect the assumed conversion of all potential dilutive securities. Adoption of the two-class method resulted in a 2 cent per share reduction in basic EPS for the nine-month period ended September 30, 2008. Diluted EPS for 2008 were not impacted by the adoption. Prior-period EPS data presented has been restated retrospectively for comparability.

Accounting Pronouncements

During the nine months ended September 30, 2009, the following accounting pronouncements applicable to the Company were issued or became effective:

- The Company adopted the new guidance in ASC Topic 805, *Business Combinations* (ASC 805), and ASC Topic 810, *Consolidation* (ASC 810), effective January 1, 2009. ASC 805 requires the acquiring entity in a business combination to recognize 100 percent of the assets acquired and liabilities assumed in the transaction; establishes acquisition date fair value as the measurement objective for the assets acquired and liabilities assumed; requires recognition of contingent consideration arrangements at their acquisition date fair values; and expands required disclosures regarding the nature and financial effect of the business combination. It also requires that acquisition-related costs be expensed when incurred. The provisions of ASC 805 are to be applied for business combination transactions consummated after January 1, 2009. ASC 810 requires that noncontrolling interests in subsidiaries be initially measured at fair value and classified as a separate component of equity in the consolidated financial statements. Following adoption, the Company reports noncontrolling interests in subsidiaries, with the exception of certain redeemable noncontrolling interests, as a separate component of equity in the consolidated balance sheets, and noncontrolling interests share of subsidiary earnings is no longer recognized as an expense in the computation of consolidated net income. The expanded presentation and disclosure requirements of ASC 810 have been applied for the current period and retrospectively for prior periods presented. Redeemable noncontrolling interest continues to be reported in the mezzanine section of the consolidated balance sheets.

- On January 1, 2009, ASC Topic 820, *Fair Value Measurements and Disclosures* (ASC 820), became effective for the Company s non-financial assets and non-financial liabilities measured at fair value on a nonrecurring basis. The Company s non-financial assets within the

scope of ASC 820, which include goodwill and customer-relationship intangible assets, are reported at fair value on a nonrecurring basis (generally as the result of an impairment assessment) during the period in which the remeasurement at fair value is recorded. The Company currently has no non-financial liabilities required to be reported at fair value.

• Effective January 1, 2009, the Company adopted the expanded disclosure requirements for derivative instruments and hedging activities under ASC Section 815-10-50, *Derivatives and Hedging - Disclosures* (ASC 815-50). The expanded disclosures address how derivative instruments are used, how derivatives and the related hedged items are accounted for, and how derivative instruments and related hedged items affect an entity s financial position, financial performance and cash flows. In addition, companies are required to disclose the fair values of derivative instruments and their gains and losses in a tabular format. The disclosure requirements of ASC 815-50 have been applied for the current period and retrospectively for prior periods presented.

Table of Contents

Note 1. Summary of Significant Accounting Policies (continued)

- The new guidance in ASC Section 350-30-35, *Intangibles Goodwill and Other Subsequent Measurement* (ASC 350-35), pertaining to the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset became effective for the Company on January 1, 2009. The intent of the revised guidance is to improve the consistency between the useful life of a recognized intangible asset and the period of expected cash flows used to measure the fair value of the asset under ASC Topic 805 when the underlying arrangement includes renewal or extension terms. ASC 350-35 permits an entity to use its own assumptions, based on its historical experience, about the renewal or extension of an arrangement to determine the useful life of an intangible asset. Adoption of the new guidance did not have a significant impact on the Company s consolidated financial statements.

- ASC Section 260-10-55, *Earnings per Share Implementation* (ASC 260-55), requires that all outstanding unvested share-based payment awards that contain rights to nonforfeitable dividends are considered to be participating securities, and the issuing entity is required to apply the two-class method of computing basic and diluted EPS. This guidance became effective for the Company on January 1, 2009. The Company grants restricted shares under a share-based compensation plan that qualify as participating securities. Accordingly, the Company calculates EPS using the two-class method. Prior period EPS and share data presented have been restated for comparability. The adoption of ASC 260-55 resulted in a 2 cent per share reduction in basic EPS for the nine-month period ended September 30, 2008. Diluted EPS for 2008 were not impacted.

- ASC Subtopic 815-40*, Derivatives and Hedging - Contracts in Entity s Own Equity* (ASC 815-40), requires an entity to evaluate an instrument s contingency provisions and the factors that affect its ultimate settlement amount (i.e., the payoff to the holder) when determining whether the instrument is indexed to the entity s own stock. This guidance became effective for the Company on January 1, 2009. Adoption of the new guidance did not have a significant impact on the Company s consolidated financial statements.

- On November 13, 2008, the Financial Accounting Standards Board (FASB) ratified a consensus on new guidance in ASC Subtopic 323-10, *Investments Equity Method and Joint Ventures - Overall* (ASC 323-10), that clarifies the accounting for certain transactions and impairment considerations involving equity method investments. The guidance applies to all investments accounted for under the equity method and became effective for the Company, on a prospective basis, for annual and interim reporting periods beginning January 1, 2009. Adoption of the new guidance in ASC 323-10 did not have a significant impact on the Company s consolidated financial statements.

- On April 1, 2009, the FASB revised the guidance in ASC Subtopic 805-20, *Business Combinations Identifiable Assets and Liabilities, and Any Noncontrolling Interest* (ASC 805-20), to amend the requirements associated with the initial recognition and measurement, subsequent measurement and accounting, and disclosure of assets and liabilities arising from contingencies in a business combination. Under the revised guidance, an asset or liability assumed in a business combination that arises from a contingency is to be initially measured at fair value if fair value can be determined. If fair value cannot be determined, an asset or liability is to be recognized if it is probable that an asset existed or a liability had been incurred at the acquisition date and the amount can be reasonably estimated. An acquiring entity should develop a systematic and rational basis for subsequently measuring and accounting for assets and liabilities arising from contingencies. An acquirer is required to disclose information that enables users of its financial statements to evaluate the nature and financial effects of a business combination. The new guidance in ASC 805-20 is effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The Company has applied the revised guidance to the acquisition completed subsequent to January 1, 2009.

- On April 9, 2009, the FASB revised ASC Section 825-10-50, *Financial Instruments Disclosures* (ASC 825-50), to require disclosures about fair value of financial instruments in interim financial statements of publicly traded companies as well as in annual financial statements. ASC 825-50 requires entities to disclose the methods and significant assumptions used to estimate the fair value of financial instruments in interim financial statements and any changes in these methods and assumptions from prior periods. The requirement to provide interim disclosures became effective for the Company for June 30, 2009 reporting. In periods after initial adoption, the Company is required to provide comparative disclosures only for periods ending after initial adoption. The disclosure requirements of ASC 825-50 have been applied for the current period.

Table of Contents

Note 1. Summary of Significant Accounting Policies (continued)

• On April 9, 2009, the FASB revised ASC Section 320-10-35, *Investments Debt and Equity Securities Subsequent Measurement* (ASC 320-35) to amend the other-than-temporary impairment guidance for debt securities. The intent and ability indicator for recognizing other-than-temporary impairment was modified, and the trigger used to assess the collectibility of cash flows changed from probable that the investor will be unable to collect all amounts due to the entity does not expect to recover the entire amortized cost basis of the security. The new guidance changes the total amount recognized in earnings when there are credit losses associated with an impaired debt security and management asserts that it does not have the intent to sell the security and it is more likely than not that it will not have to sell the security before recovery of its cost basis. In those situations, impairment shall be separated into (a) the amount representing a credit loss and (b) the amount related to non-credit factors. The amount of impairment related to credit losses shall be recognized in earnings. The credit loss component of an other-than-temporary impairment, representing an increase in credit risk, shall be determined by the reporting entity using its best estimate of the present value of cash flows expected to be collected from the debt security. The amount of impairment related to non-credit factors shall be recognized in other comprehensive income. The previous cost basis less impairment recognized in earnings becomes the new cost basis of the security and shall not be adjusted for subsequent recoveries in fair value. However, the difference between the new amortized cost basis and the cash flows expected to be collected should be accreted as interest income. The total other-than-temporary impairment is presented in the consolidated statements of income with a reduction for the amount of the other-than-temporary impairment that is recognized in other comprehensive income, if any.

The cumulative effect of initial adoption is recorded as an adjustment to the opening balance of retained earnings with a corresponding adjustment to accumulated other comprehensive income. The amortized cost basis of a security for which an other-than-temporary impairment was previously recognized shall be adjusted by the amount of the cumulative effect adjustment before taxes. The difference between the new amortized cost basis and the cash flows expected to be collected shall be accreted as interest income. The new guidance became effective for the Company on April 1, 2009. The Company did not hold any available-for-sale debt securities on April 1, 2009 with previously recognized other-than-temporary impairment. Therefore, the Company was not required to record a cumulative effect adjustment upon adoption.

• On April 9, 2009, the FASB revised ASC Subtopic 820-10, *Fair Value Measurements and Disclosures - Overall* (ASC 820-10), to provide additional guidance for estimating fair value when the volume and level of activity for an asset or liability have significantly decreased, and identifying transactions that are not orderly. Several factors are identified that a reporting entity should evaluate to determine whether there has been a significant decrease in the volume and level of activity for an asset or liability. If the reporting entity concludes there has been a significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity, transactions or quoted prices may not be determinative of fair value (for example, there may be increased instances of transactions that are not orderly), further analysis of the transactions or quoted prices is needed, and a significant adjustment to the transactions or quoted prices may be necessary to estimate fair value. The expanded guidance reiterates that even in circumstances where there has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation technique(s) used, the objective of a fair value measurement remains the same. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. The new guidance became effective for the Company for the June 30, 2009 reporting period. Adoption of the new guidance did not have a significant impact on the consolidated financial statements.

• On May 28, 2009, the FASB issued ASC Topic 855, *Subsequent Events* (ASC 855). ASC 855 provides authoritative accounting literature for a topic that was previously addressed only in the auditing literature. ASC 855 is similar to the current guidance with some

modifications that are not intended to result in significant changes in practice. Under ASC 855, subsequent events are categorized as recognized (currently type I) or nonrecognized (currently type II). The definition of subsequent events is modified to refer to events or transactions that occur after the balance sheet date, but before the financial statements are issued (for public entities) or available to be issued (for nonpublic entities). Entities are required to disclose the date through which an entity has evaluated subsequent events and the basis for that date. ASC 855 is effective on a prospective basis for interim or annual financial periods ending after June 15, 2009 and became effective for the Company for the June 30, 2009 reporting period. Adoption of ASC 855 did not have a significant impact on the Company s consolidated financial statements.

Table of Contents

Note 1. Summary of Significant Accounting Policies (continued)

- On June 29, 2009, the FASB issued ASC Topic 105, *Generally Accepted Accounting Principles* (ASC 105). ASC 105 establishes the FASB Accounting Standards Codification (Codification) as the source of authoritative principles and standards recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with GAAP. Rules and interpretive releases of the SEC under the authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. The Codification represents a major reorganization of GAAP but is not intended to change GAAP. ASC 105 became effective for the Company on July 1, 2009. Adoption of the Codification did not have a significant impact on the Company s consolidated financial statements.

The following accounting pronouncements were issued prior to or during the first nine months of 2009, but are not effective for the company until after September 30, 2009:

- On June 12, 2009, the FASB revised ASC Topic 860-10, *Transfers and Servicing* (ASC 860), to expand required disclosures about transfers of financial assets and a transferor s continuing involvement with transferred assets. It also removes the concept of qualifying special-purpose entity from U.S. GAAP. The new guidance is effective for financial asset transfers occurring after the beginning of an entity s first fiscal year that begins after November 15, 2009. Adoption of the new guidance is not expected to have a material effect on the Company s consolidated financial statements.

- On June 12, 2009, the FASB revised ASC 810-10-25, *Consolidation Recognition (Variable Interest Entities)* (ASC 810-25). The revised guidance requires, among other things: that an entity perform a qualitative analysis to determine if it is the primary beneficiary of a variable interest entity (VIE), consideration of related party relationships in the determination of the primary beneficiary of a VIE, and enhanced disclosures about an enterprise s involvement with a VIE. The new guidance is effective as of the beginning of the first annual reporting period that begins after November 15, 2009, for interim reporting periods within that first annual reporting period and for interim and annual reporting periods thereafter. The Company is evaluating the impact of adoption on its consolidated financial statements.

- In August 2009, the FASB issued Accounting Standards Update (ASU) 2009-05 to provide guidance on measuring the fair value of liabilities under ASC Subtopic 820-10, *Fair Value Measurements and Disclosures-Overall.* ASU 2009-05 reaffirms that fair value measurement of a liability assumes the transfer of a liability to a market participant as of the measurement date; that is, the liability is presumed to continue and is not settled with the counterparty. In addition, ASU 2009-05 reemphasizes that a fair value measurement of a liability includes nonperformance risk and that such risk does not change after the transfer of the liability. The guidance clarifies that in circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity is required to measure fair value using either (1) a valuation technique that uses the quoted price of the identical liability when traded as an asset, or quoted prices for similar liabilities or similar liabilities when traded as assets, or (2) another valuation technique that is consistent with ASC Topic 820 such as an income or market approach. ASU 2009-05 also states that a separate adjustment for the impact of a restriction on the transfer of a liability should not be made in the fair value measurement of a liability. The effect of a restriction on the transfer of a liability is presumed to be already factored into the transaction price of the liability at inception. ASU 2009-05 is effective for the Company on October 1, 2009. Adoption of the new guidance is not expected to have a significant impact on the Company s consolidated financial statements.

- In September 2009, the FASB issued ASU 2009-12 to provide guidance on measuring the fair value of investments in certain entities, such as hedge funds, private equity funds, venture capital funds, funds of funds and real estate funds that calculate net asset value per share. ASU 2009-12 amends ASC Topic 820, *Fair Value Measurements and Disclosures.* The guidance applies to investments that are required or permitted to be measured at fair value on a recurring or nonrecurring basis that do not have readily determinable fair values. If an investment is within scope of the ASU, a reporting entity is permitted but not required to use the investment s net asset value (NAV) or its equivalent to estimate its fair value, provided that the NAV is calculated as of the reporting entity s measurement date. ASU 2009-12 also requires enhanced disclosures about the nature and risks of investments within its scope that are measured at fair value on a recurring or nonrecurring basis. The ASU is effective for interim and annual periods ending after December 15, 2009. The Company does not expect adoption of the new guidance to have a significant impact on its consolidated financial statements.

Table of Contents

Note 2. Business Combination

On July 21, 2009, the Company acquired an approximate 57 percent majority interest in Lee Munder Capital Group, LLC (LMCG), a Boston-based investment firm that manages assets for corporations, pensions, endowments and affluent households. LMCG had approximately $3.4 billion of assets under management at the date of acquisition. LMCG was merged with Independence Investments, a Boston-based institutional asset management firm in which the Company held a majority interest. The combined entity is the Company s primary institutional asset management affiliate, with more than $4 billion of assets under management at acquisition date. It is operated under the Lee Munder Capital Group name and as an affiliate of Convergent Capital Management LLC, the Chicago-based asset management holding company that the Company acquired in 2003.

The Company recorded $36.0 million of goodwill and a $2.8 million client advisory contract intangible in association with its acquisition of LMCG. Although the Company only acquired an interest of approximately 57 percent, ASC Topic 805 requires the Company to account for the acquisition of 100 percent of LMCG. Under ASC Topic 805, the assets acquired, liabilities assumed and remaining noncontrolling interests are recognized at their full acquisition-date fair values. The $36.0 million of goodwill recognized includes the $14.7 million fair value of noncontrolling interest recorded at the acquisition date. The noncontrolling interest is recorded in Redeemable noncontrolling interest in the mezzanine section of the consolidated balance sheets.

Note 3. Fair Value Measurements

ASC 820, *Fair Value Measurements and Disclosures*, defines fair value for financial reporting purposes as the price that would be received to sell an asset or paid to transfer a liability in an orderly market transaction between market participants at the measurement date (reporting date). Fair value is based on an exit price in the principal market or most advantageous market in which the reporting entity could transact.

Fair Value Hierarchy

Management employs market standard valuation techniques in determining the fair value of assets and liabilities. Inputs used in valuation techniques are based on assumptions that market participants would use in pricing an asset or liability. The inputs used in valuation techniques are prioritized as follows:

Level 1 Quoted market prices in an active market for identical assets and liabilities.

Level 2 Observable inputs including quoted prices (other than Level 1) in active markets for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability such as interest rates, yield curves, volatilities and default rates, and inputs that are derived principally from or corroborated by observable market data.

Level 3 Unobservable inputs reflect the reporting entity s own assumptions about the assumptions market participants would use in pricing the asset or liability based on the best information available.

If the determination of fair value measurement for a particular asset or liability is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. Management s assessment of the significance of a particular input to the fair value measurement requires judgment and considers factors specific to the asset or liability measured.

The Company records securities available-for-sale, trading securities and derivative contracts at fair value on a recurring basis. Certain other assets such as impaired loans, other real estate owned (OREO), goodwill, customer-relationship intangibles and private equity investments are recorded at fair value on a nonrecurring basis. Nonrecurring fair value measurements typically involve assets that are periodically evaluated for impairment and for which any impairment is recorded in the period in which the remeasurement is performed.

Table of Contents

Note 3. Fair Value Measurements (continued)

A distribution of asset and liability fair values according to the fair value hierarchy at September 30, 2009 is provided in the table below:

		Fair Value Measurements at Reporting Date Using		
(in thousands)	Balance as of September 30, 2009	Quoted Prices in Active Markets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Measured on a Recurring Basis				
Assets				
Securities available-for-sale				
Debt securities	$ 3,491,347	$ 13,554	$ 3,450,820	$ 26,973
Equity securities and mutual funds	20,725	20,725		
Trading securities	188,904	175,035	13,040	829
Mark-to-market derivatives (1)	64,414	5,337	59,077	
Total assets at fair value	$ 3,765,390	$ 214,651	$ 3,522,937	$ 27,802
Liabilities				
Mark-to-market derivatives (2)	$ 19,315	$ 624	$ 18,691	$
Total liabilities at fair value	$ 19,315	$ 624	$ 18,691	$
Measured on a Nonrecurring Basis				
Assets				
Collateral dependent impaired loans (3)	$ 224,684	$	$ 224,684	$
Other real estate owned (4)	32,758		32,758	
Private equity investments	4,954			4,954
Total assets at fair value	$ 262,396	$	$ 257,442	$ 4,954

(1) Reported in Other assets in the consolidated balance sheets.

(2) Reported in Other liabilities in the consolidated balance sheets.

(3) Impaired loans for which fair value was calculated using the collateral valuation method.

(4) Includes other real estate owned that was measured at fair value during the nine months ended September 30, 2009.

For assets measured at fair value on a nonrecurring basis, the following table presents the total losses recognized in the three months and nine months ended September 30, 2009:

(in thousands)	Three months ended September 30, 2009	Nine months ended September 30, 2009
Impaired loans	$ 51,844	$ 106,606
Other real estate owned	4,199	9,537

Private equity investments		1,396		1,799
Total losses recognized	$	57,439	$	117,942

Level 3 assets measured at fair value on a recurring basis are CDO senior notes, included in available-for-sale debt securities, and CDO income notes, included in trading securities, for which the market is inactive. The fair value of these securities is determined using an internal cash flow model that incorporates management s assumptions about risk-adjusted discount rates, prepayment expectations, projected cash flows and collateral performance. These assumptions are not directly observable in the market. Unrealized gains and losses on available-for-sale securities are reported as a component of Accumulated other comprehensive income in the consolidated balance sheets. Unrealized gains and losses on trading securities are reported in earnings.

Table of Contents

Note 3. Fair Value Measurements (continued)

Activity in Level 3 assets measured on a recurring basis for the nine-months ended September 30, 2009 is summarized in the following table:

Level 3 Assets Measured on a Recurring Basis

(in thousands)	Securities Available-for-Sale	Trading Securities	Total Level 3 Assets
Balance of recurring Level 3 assets at January 1, 2009	$ 32,419	$	$ 32,419
Total realized/unrealized gains (losses):			
Included in earnings	(9,281)	(1,618)	(10,899)
Included in other comprehensive income	7,068		7,068
Purchases, sales, issuances and settlements, net	(786)		(786)
Transfers between categories	(2,447)	2,447	
Balance of recurring Level 3 assets at September 30, 2009	$ 26,973	$ 829	$ 27,802

Level 3 assets measured at fair value on a nonrecurring basis include private equity investments. Private equity investments do not have readily determinable fair values. These investments are carried at cost and evaluated for impairment on a quarterly basis. Due to the lack of readily determinable fair values for these investments, the impairment assessment was based primarily on a review of investment performance and the likelihood that the capital invested would be recovered. The Company recorded an impairment loss of $1.4 million on two private equity investments for the three months ended September 30, 2009. This impairment is included in Other noninterest income in the consolidated statements of income.

There were no purchases or sales of Level 3 assets in 2009.

Note 4. Fair Value of Financial Instruments

A financial instrument is broadly defined as cash, evidence of an ownership interest in another entity, or a contract that imposes a contractual obligation on one entity and conveys a corresponding right to a second entity to require delivery or exchange of a financial instrument. The table below summarizes the estimated fair values for the Company s financial instruments as of September 30, 2009 and December 31, 2008. The disclosure does not include estimated fair value amounts for assets and liabilities which are not defined as financial instruments but which have significant value. These assets and liabilities include the value of customer-relationship intangibles, goodwill, private equity and affordable housing investments carried at cost, other assets, deferred taxes and other liabilities. Accordingly, the total of the fair values presented does not represent the underlying value of the Company.

Following is a description of the methods and assumptions used in estimating the fair values for each class of financial instrument:

Cash and due from banks, Due from banks interest bearing and Federal funds sold For these short-term instruments, the carrying amount is a reasonable estimate of fair value.

Securities available-for-sale and Trading securities For securities held as available-for-sale, the fair value is determined by quoted market prices, where available, or on observable market inputs appropriate for the type of security. If quoted market prices or observable market inputs are not available, discounted cash flows may be used to determine an appropriate fair value. See Note 3, *Fair Value Measurements*. Fair values for trading securities, with the exception of CDO income notes, are based on quoted market prices or dealer quotes. The fair value of CDO income notes is determined using a discounted cash flow model.

Loans and leases Loans are not recorded at fair value on a recurring basis. Nonrecurring fair value adjustments are periodically recorded on impaired loans that are measured for impairment based on the fair value of collateral. See Note 3, *Fair Value Measurements*. Due to the lack of activity in the secondary market for the types of loans in the Company s portfolio, a model-based approach is used for determining the fair value of loans for purposes of the disclosures in the table below. The fair value of loans is estimated by discounting future cash flows using discount rates that incorporate assumptions concerning current market yields, credit risk and liquidity premiums. Loan cash flow projections are based on contractual loan terms adjusted for the impact of current interest rate levels on borrower behavior, including prepayments. Loan prepayment assumptions are based on industry standards for the type of loans being valued. Projected cash flows are discounted using yield curves based on current market conditions. Yield curves are constructed by product type using the Bank s loan pricing model for like-quality credits.

Note 4. Fair Value of Financial Instruments (continued)

Derivative Contracts The fair value of non-exchange traded (over-the-counter) derivatives are obtained from third party market sources. The Company provides client data to the third party source for purposes of calculating the credit valuation component of the fair value measurement of client derivative contracts. The fair values of interest rate contracts include interest receivable and payable and cash collateral, if any.

Deposits The fair value of demand and interest checking deposits, savings deposits, and certain money market accounts is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is determined by discounting expected future cash flows using the rates offered by the Bank for deposits of similar type and remaining maturity at the measurement date. This value is compared to the termination value of each CD given the bank s standard early withdrawal penalties. The fair value reported is the higher of the discounted present value of each CD and the termination value after the recovery of prepayment penalties. The Bank reviews pricing for its CD products weekly. This review gives consideration to market pricing for products of similar type and maturity offered by other financial institutions.

Federal funds purchased, Securities sold under repurchase agreements and Other short-term borrowings The carrying amount is a reasonable estimate of fair value.

Structured securities sold under repurchase agreements The fair value of structured repurchase agreements is based on market pricing for synthetic instruments with the same term and structure. These values are validated against dealer quotes for similar instruments.

Subordinated and long-term debt The fair value of subordinated and long-term debt is obtained through third-party pricing sources.

Commitments to extend credit The fair value of these commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. The Company does not make fixed-rate loan commitments. The fair value of commitments to extend credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date.

Commitments to private equity and affordable housing funds The fair value of commitments to invest in private equity and affordable housing funds is based on the estimated cost to terminate them or otherwise settle the obligation.

Table of Contents

Note 4. Fair Value of Financial Instruments (continued)

The estimated fair values of financial instruments of the Company are as follows:

(in millions)	September 30, 2009 Carrying Amount	September 30, 2009 Fair Value	December 31, 2008 Carrying Amount	December 31, 2008 Fair Value
Financial Assets:				
Cash and due from banks	$ 349.0	$ 349.0	$ 279.9	$ 279.9
Due from banks - interest bearing	767.4	767.4	144.3	144.3
Federal funds sold	240.0	240.0		
Securities available-for-sale	3,512.1	3,512.1	2,144.9	2,144.9
Trading securities	188.9	188.9	295.6	295.6
Loans and leases, net of allowance	11,903.5	12,058.1	12,220.2	12,515.8
Derivative contracts	64.4	64.4	48.2	48.2
Financial Liabilities:				
Deposits	$ 15,108.4	$ 15,112.5	$ 12,652.1	$ 12,663.7
Federal funds purchased and securities sold under repurchase agreements	31.9	31.9	708.2	708.2
Structured securities sold under repurchase agreements	200.0	210.1	200.0	218.0
Other short-term borrowings	0.7	0.7	124.5	124.5
Subordinated and long-term debt	575.1	571.8	408.1	369.6
Derivative contracts	19.3	19.3	21.0	21.0
Commitments to extend credit		(13.7)		(13.1)
Commitments to private equity and affordable housing funds		36.1		44.0

Note 5. Investment Securities

Securities are classified as trading, available-for-sale or held-to-maturity based on the Company s intent for holding a particular instrument. At September 30, 2009, all securities held other than trading securities were classified as available-for-sale and valued at fair value. Unrealized gains or losses on securities available-for-sale are excluded from net income, to the extent they are considered temporary, but are included as separate components of other comprehensive income, net of taxes. Premiums or discounts on securities available-for-sale are amortized or accreted into income using the interest method over the expected lives of the individual securities. For most of the Company s investments, fair values are determined based upon externally verifiable quoted prices or other observable inputs. Realized gains or losses on sales of securities available-for-sale are recorded using the specific identification method.

Table of Contents

Note 5. Investment Securities (continued)

The following is a summary of amortized cost and estimated fair value for the major categories of securities available-for-sale:

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2009				
U.S. Treasury	$ 13,543	$ 11	$	$ 13,554
Federal agency - Debt	358,928	1,464	(108)	360,284
Federal agency - MBS	564,193	17,804	(23)	581,974
CMOs - Federal agency	1,750,790	32,139	(1,263)	1,781,666
CMOs - Non-agency	314,583	88	(33,815)	280,856
State and municipal	384,999	18,476	(211)	403,264
Other debt securities	76,069	873	(7,193)	69,749
Total debt securities	3,463,105	70,855	(42,613)	3,491,347
Equity securities and mutual funds	17,554	3,171		20,725
Total securities	$ 3,480,659	$ 74,026	$ (42,613)	$ 3,512,072
December 31, 2008				
U.S. Treasury	$ 45,709	$ 488	$	$ 46,197
Federal agency - Debt	29,939	241		30,180
Federal agency - MBS	644,594	10,206	(886)	653,914
CMOs - Federal agency	563,310	6,966	(907)	569,369
CMOs - Non-agency	393,150		(87,434)	305,716
State and municipal	404,787	9,729	(1,486)	413,030
Other debt securities	98,419	139	(24,215)	74,343
Total debt securities	2,179,908	27,769	(114,928)	2,092,749
Equity securities and mutual funds	59,276	1,154	(8,309)	52,121
Total securities	$ 2,239,184	$ 28,923	$ (123,237)	$ 2,144,870
September 30, 2008				
U.S. Treasury	$ 45,784	$ 156	$	$ 45,940
Federal agency - Debt	29,933	202		30,135
Federal agency - MBS	650,616	1,414	(9,952)	642,078
CMOs - Federal agency	533,920	765	(5,668)	529,017
CMOs - Non-agency	418,417	76	(35,217)	383,276
State and municipal	370,118	2,024	(7,809)	364,333
Other debt securities	109,403	3,270	(15,942)	96,731
Total debt securities	2,158,191	7,907	(74,588)	2,091,510
Equity securities and mutual funds	72,001	271	(3,864)	68,408
Total securities	$ 2,230,192	$ 8,178	$ (78,452)	$ 2,159,918

Proceeds from sales of securities were $108.8 million and $554.8 million for the three months and nine months ended September 30, 2009, respectively, compared to $6 thousand and $0.1 million for the three months and nine months ended September 30, 2008, respectively. The following table shows the gross realized gains and losses on the sales of securities available-for-sale:

(in thousands)	For the three months ended September 30, 2009	2008	For the nine months ended September 30, 2009	2008
Gross realized gains	$ 3,555	$ 337	$ 12,218	$ 2,318
Gross realized losses	(109)	(873)	(8,423)	(2,302)
Net realized gains (losses)	$ 3,446	$ (536)	$ 3,795	$ 16

Table of Contents

Note 5. Investment Securities (continued)

Impairment Assessment

Impairment exists when the fair value of a security is less than its cost. Cost includes adjustments made to the cost basis of a security for accretion, amortization and previous other-than-temporary impairments recognized in earnings. The Company performs a quarterly assessment of the debt and equity securities in its investment portfolio that have an unrealized loss to determine whether the decline in the fair value of these securities below their cost is other-than-temporary. Impairment is considered other-than-temporary when it becomes probable that an investor will be unable to recover the cost of an investment. The Company s impairment assessment takes into consideration factors such as the length of time and the extent to which the market value has been less than cost; the financial condition and near-term prospects of the issuer including events specific to the issuer or industry; defaults or deferrals of scheduled interest, principal or dividend payments; external credit ratings and recent downgrades; and the Company does not intend to sell the security and it is not more likely than not it will be required to sell the security prior to recovery of its amortized cost basis. If a decline in fair value is judged to be other than temporary, the cost basis of the individual security is written down to fair value which then becomes the new cost basis. The new cost basis is not adjusted for subsequent recoveries in fair value.

In accordance with ASC 320-35, when there are credit losses associated with an impaired debt security and the Company does not have the intent to sell the security and it is more likely than not that it will not have to sell the security before recovery of its cost basis, the Company will separate the amount of the impairment into the amount that is credit related and the amount related to non-credit factors. The credit-related impairment is recognized in Net impairment loss recognized in earnings in the consolidated statements of income. The non-credit-related impairment is recognized in Accumulated other comprehensive income (loss) (AOCI).

Securities Deemed to be Other-Than-Temporarily Impaired

Through the impairment assessment process, the Company determined that certain investments were other-than-temporarily impaired at September 30, 2009. The Company recorded credit loss impairment in earnings on available-for-sale securities of $0.8 million and $14.4 million for the three months and nine months ended September 30, 2009, respectively. The $19.8 million non-credit portion of impairment recognized at September 30, 2009 was recorded in AOCI. The Company recorded a $31.9 million impairment loss on available-for-sale securities for the three months and nine months ended September 30, 2008.

(in thousands) Impairment Losses on Other-Than-Temporarily Impaired Securities	**For the three months ended September 30,**		**For the nine months ended September 30,**	
	2009	**2008**	**2009**	**2008**
Non-agency CMOs	$ 778	$	$ 2,315	$
Collateralized debt obligation income notes		7,159	9,282	7,159
Perpetual preferred stock		21,884	1,124	21,884
Equity securities and mutual funds		2,893	1,630	2,893
Total	$ 778	$ 31,936	$ 14,351	$ 31,936

The following table provides a rollforward of credit related other than-temporary impairment recognized in earnings for the three months and nine months ended September 30, 2009. Credit related other-than-temporary impairment that was recognized in earnings during the three months and nine months ending September 30, 2009 is reflected as an Initial credit-related impairment if the current period is the first time the security had a credit impairment. A credit related other-than-temporary impairment is reflected as a Subsequent credit-related impairment if the current period is not the first time the security had a credit impairment.

(in thousands)	**Three months ended September 30, 2009**	**Nine months ended September 30, 2009**
Balance, beginning of period	$ 14,835	$ 8,083
Subsequent credit-related impairment	696	5,215
Initial credit-related impairment	82	2,315
Balance, end of period	$ 15,613	$ 15,613

Table of Contents

Note 5. Investment Securities (continued)

Non-Agency CMOs

The Company identified seven non-agency collateralized mortgage obligation securities (CMOs) that had other than temporary impairment at September 30, 2009. These CMOs had an adjusted cost basis of $65.1 million at September 30, 2009 and a fair value of $45.3 million. The fair value of the CMOs is based on prices provided by an external pricing service. These securities are classified as Level 2 in the fair value hierarchy. The CMOs analyzed for impairment have a fixed interest rate for an initial period after which they become variable-rate instruments with annual rate resets. For purposes of projecting future cash flows, the current fixed coupon was used through the reset date for each security. The prevailing LIBOR/Treasury curve as of September 30, 2009 was used to project all future floating-rate cash flows based on the characteristics of each security. Other factors considered in the projection of future cash flows include the current level of subordination from other CMO classes, anticipated prepayment rates, cumulative defaults and loss given default. The present value of expected cash flows was less than cost by a total of $0.8 million for the securities analyzed. The Company concluded that the $0.8 million shortfall in expected cash flows represented a credit loss and recognized an impairment loss in earnings for this amount at September 30, 2009. The Company has recognized credit losses totaling $2.3 million on its investments in non-agency CMOs year-to-date. The remaining other-than-temporary impairment of $19.8 million was recognized in AOCI. This non-credit portion of other-than-temporary impairment is attributed to external market conditions, primarily the lack of liquidity in these securities, and risks of additional declines in the housing markets.

Collateralized Debt Obligation Income Notes

Collateralized debt obligation income notes (Income Notes) are equity interests in a multi-class, cash flow collateralized bond obligation backed by a collection of Trust Preferred securities issued by financial institutions. The equity interests represent ownership of all residual cash flow from the asset pools after all fees have been paid and debt issues have been serviced. Income Notes are collateralized by debt securities with stated maturities. Income Notes are classified as Level 3 in the fair value hierarchy. Refer to Note 3, *Fair Value Measurements*, for further discussion of fair value.

In response to unprecedented volatility in the credit markets, the Company reevaluated its investment strategy and risk tolerance with respect to its investments in Income Notes. Based on this reassessment, the Company determined that its intent was to sell these securities when the market recovers rather than hold them for the long term. The change in intent resulted in the Company transferring its holdings of Income Notes from available-for-sale to trading securities on April 1, 2009, at their fair value of $2.4 million. There were no gross gains and gross losses included in earnings from the transfer of these securities. Trading securities are carried at fair value and unrealized holding gains and losses are included in earnings.

The Company recorded a $9.3 million impairment loss, of which $5.2 million represented a credit loss recognized in earnings, on its investment in Income Notes in the first quarter of 2009 prior to their transfer to trading securities. The Income Notes were evaluated for impairment under the guidance applicable to certain debt securities which are beneficial interests in securitized financial assets and not considered to be of high credit quality. For these securities, other-than-temporary impairment exists when it is probable there has been an adverse change in estimated cash flows since the date of acquisition. Due to lack of activity in the market for Income Notes, the fair value of these securities was determined using an internal cash flow model that incorporated management s assumptions about risk-adjusted discount rates, prepayment expectations, projected cash flows and collateral performance. The Company considered a number of factors in determining the discount rate used in the cash flow valuation model including the implied rate of return at the last date the market for Income Notes and similar securities was active, rates of return that market participants would consider in valuing the securities and indicative quotes from dealers.

Perpetual Preferred Stock

The adjusted cost basis of the Company s investment in perpetual preferred stock issued by Freddie Mac and Fannie Mae was $0.6 million at September 30, 2009, compared with a fair value of $1.6 million, indicating that these securities were not impaired at quarter end. The Company previously recorded impairment losses totaling $23.0 million on these securities. Impairment losses of $1.1 million and $21.9 million were recognized for the quarters ending March 31, 2009 and September 30, 2008, respectively, following the action taken by the Federal Housing Finance Agency in September 2008 of placing these Government-Sponsored Agencies into conservatorship and eliminating the dividends on their preferred shares.

Table of Contents

Note 5. Investment Securities (continued)

Mutual Funds

The adjusted cost basis of available-for-sale mutual funds was $16.9 million at September 30, 2009, compared with a fair value of $19.1 million, indicating that these investments were not impaired at quarter end. The Company previously recognized a $1.6 million impairment loss on its investment in one high-yield bond fund in the quarter ended March 31, 2009.

The following table provides a summary of the gross unrealized losses and fair value of investment securities aggregated by investment category and length of time that the securities have been in a continuous unrealized loss position as of September 30, 2009. The table includes investments for which an other-than-temporary impairment has not been recognized in earnings, along with investments that had a non-credit related impairment recognized in AOCI:

	Less than 12 months		12 months or greater		Total	
(in thousands)	Fair Value	Estimated Unrealized Loss	Fair Value	Estimated Unrealized Loss	Fair Value	Estimated Unrealized Loss
Federal agency - Debt	$ 25,819	$ 108	$	$	$ 25,819	$ 108
Federal agency - MBS	9,937	23			9,937	23
CMOs - Federal agency	129,042	1,263			129,042	1,263
CMOs - Non-agency			257,400	33,815	257,400	33,815
State and municipal	1,611	31	5,865	180	7,476	211
Other debt securities			45,089	7,193	45,089	7,193
Total securities	$ 166,409	$ 1,425	$ 308,354	$ 41,188	$ 474,763	$ 42,613

At September 30, 2009, total securities available-for-sale had a fair value of $3.51 billion, which included the $474.8 million of securities available-for-sale in an unrealized loss position as of September 30, 2009. This balance consists of $429.5 million of temporarily impaired securities and $45.3 million of securities that had non-credit related impairment recognized in AOCI. At September 30, 2009, the Company had 55 debt securities in an unrealized loss position. The debt securities in an unrealized loss position include 2 Federal agency debt securities, 1 Federal agency MBS, 7 Federal agency CMOs, 29 private label CMOs, 10 state and municipal securities and 6 other debt securities. The largest component of the unrealized loss at September 30, 2009 was $33.8 million related to non-agency collateralized mortgage obligations. The Company monitors the performance of the mortgages underlying these bonds. Although there has been some deterioration in collateral performance during 2009 due to declines in the housing market, the Company only holds the most senior tranches of each issue which provides protection against defaults. The Company attributes the unrealized loss on CMOs held largely to the current absence of liquidity in the credit markets and not to deterioration in credit quality. The unrealized loss on the Company s holdings of non-agency CMOs decreased from $57.0 million at June 30, 2009 to $33.8 million at September 30, 2009 largely due to government-backed investment programs which have modestly increased demand and liquidity in these markets. Other than the $2.3 million credit loss discussed in *Non-Agency CMOs* above, the Company expects to receive all contractual principal and interest payments due on its CMO debt securities. Additionally, the Company does not intend to sell the securities, and it is not more likely than not that it will be required to sell the securities before it recovers the cost basis of its investment. The mortgages in these asset pools are relatively large and have been made to borrowers with strong credit history and significant equity invested in their homes. They are well diversified geographically. Nonetheless, significant further weakening of economic fundamentals coupled with significant increases in unemployment and substantial deterioration in the value of high-end residential properties could extend distress to this borrower population. This could increase default rates and put additional pressure on property values. Should these conditions occur, the value of these securities could decline and trigger the recognition of further other-than-temporary impairment charges.

Other debt securities include the Company s investments in highly rated corporate debt and collateralized bond obligations backed by trust preferred securities (CDOs) issued by a geographically diverse pool of small- and medium-sized financial institutions. Liquidity pressures in 2008 and in 2009 caused a general decline in the value of corporate debt. The CDOs held in available-for-sale securities at September 30, 2009 are the most senior tranches of each issue. The market for CDOs was inactive in 2008 and 2009, therefore, the fair values of these securities were determined using an internal pricing model that incorporates assumptions about discount rates in an illiquid market, projected cash flows and collateral performance. The Company attributes the $4.7 million unrealized loss on CDOs at September 30, 2009 to the illiquid credit markets. The senior notes have collateral that exceeds the outstanding debt by approximately 35 percent. Security valuations

Table of Contents

Note 5. Investment Securities (continued)

reflect the current and prospective performance of the issuers whose debt is contained in these asset pools. The Company expects to receive all contractual principal and interest payments due on its CDOs. Additionally, the Company does not intend to sell the securities, and it is not more likely than not that it will be required to sell the securities before it recovers the cost basis of its investment.

Excluding the investments which had non-credit related impairment, the Company does not consider the debt securities in the above table to be other than temporarily impaired at September 30, 2009.

The following table provides a summary of the gross unrealized losses and fair value of investment securities that are not deemed to be other-than-temporarily impaired aggregated by investment category and length of time that the securities have been in a continuous unrealized loss position as of December 31, 2008:

	Less than 12 months		12 months or greater		Total	
(in thousands)	Fair Value	Estimated Unrealized Loss	Fair Value	Estimated Unrealized Loss	Fair Value	Estimated Unrealized Loss
Federal agency - MBS	$ 63,634	$ 719	$ 12,925	$ 167	$ 76,559	$ 886
CMOs - Federal agency	29,133	111	41,041	796	70,174	907
CMOs - Non-agency	172,899	50,631	132,818	36,803	305,717	87,434
State and municipal	39,974	1,275	4,769	211	44,743	1,486
Other debt securities	43,844	17,661	25,910	6,554	69,754	24,215
Total debt securities	349,484	70,397	217,463	44,531	566,947	114,928
Equity securities and mutual funds	36,129	8,309			36,129	8,309
Total securities	$ 385,613	$ 78,706	$ 217,463	$ 44,531	$ 603,076	$ 123,237

At December 31, 2008, total securities available-for-sale had a fair value of $2.14 billion, which included the temporarily impaired securities of $603.1 million in the table above. As of December 31, 2008, the Company had 109 debt securities in an unrealized loss position, including 29 CMO securities, 10 mortgage-backed securities, 55 state and municipal securities and 15 other debt securities. As of December 31, 2008, the Company had 2,012 equity securities and 5 mutual funds in an unrealized loss position.