CVB FINANCIAL CORP
Form 10-Q
November 05, 2009

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FORM 10-Q
UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

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

For the quarterly period ended September 30, 2009

or

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: 0-10140

CVB FINANCIAL CORP.

(Exact name of registrant as specified in its charter)

California	95-3629339
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
701 North Haven Ave, Suite 350, Ontario, California	91764
(Address of Principal Executive Offices)	(Zip Code)

(Registrant s telephone number, including area code) (909) 980-4030

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 þ 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, accelerated filer, non-accelerated filer or smaller reporting company. See definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ	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).
Yes o No þ

Number of shares of common stock of the registrant: 106,231,511 outstanding as of November 03, 2009.

CVB FINANCIAL CORP.
2009 QUARTERLY REPORT ON FORM 10-Q
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PART I FINANCIAL INFORMATION (UNAUDITED)
ITEM 1. FINANCIAL STATEMENTS
CVB FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(unaudited)
Dollar amounts in thousands

	September 30, 2009	December 31, 2008
ASSETS		
Cash and due from banks	$ 222,158	$ 95,297
Investment securities available-for-sale	2,285,456	2,493,476
Investment securities held-to-maturity	4,237	6,867
Federal Funds Sold and		
Interest-bearing balances due from depository institutions	150,285	285
Investment in stock of Federal Home Loan Bank (FHLB)	93,240	93,240
Loans and lease finance receivables	3,600,087	3,736,838
Allowance for credit losses	(87,316)	(53,960)
Net Loans and lease finance receivables	3,512,771	3,682,878
Total earning assets	6,045,989	6,276,746
Premises and equipment, net	42,285	44,420
Bank owned life insurance	108,744	106,366
Accrued interest receivable	27,430	28,519
Intangibles	8,763	11,020
Goodwill	55,097	55,097
Other assets	35,799	32,186
TOTAL ASSETS	$ 6,546,265	$ 6,649,651
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities:		
Deposits:		
Noninterest-bearing	$ 1,416,558	$ 1,334,248
Interest-bearing	2,623,213	2,173,908
Total deposits	4,039,771	3,508,156
Demand Note to U.S. Treasury	3,441	5,373
Repurchase agreements	710,326	607,813
Borrowings	955,000	1,737,660
Accrued interest payable	8,420	9,741
Deferred compensation	9,136	8,985
Junior subordinated debentures	115,055	115,055
Other liabilities	53,606	41,976

TOTAL LIABILITIES	5,894,755	6,034,759
COMMITMENTS AND CONTINGENCIES		
Stockholders Equity:		
Preferred stock, authorized, 20,000,000 shares without par; none issued or outstanding		121,508
Common stock, authorized, 122,070,312 shares without par; issued and outstanding 106,231,511 (2009) and 83,270,263 (2008)	492,014	364,469
Retained earnings	112,596	100,184
Accumulated other comprehensive income, net of tax	46,900	28,731
Total stockholders equity	651,510	614,892
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 6,546,265	$ 6,649,651

See accompanying notes to the consolidated financial statements.

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CVB FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EARNINGS
(unaudited)
Dollar amounts in thousands, except per share

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2009	2008	2009	2008
Interest income:				
Loans, including fees	$ 50,561	$ 52,954	$ 149,858	$ 159,211
Investment securities:				
Taxable	18,278	22,142	59,848	65,448
Tax-preferred	6,749	7,036	20,560	21,336
Total investment income	25,027	29,178	80,408	86,784
Dividends from FHLB stock	195	1,367	195	3,666
Federal funds sold and Interest bearing deposits with other institutions	136	8	195	34
Total interest income	75,919	83,507	230,656	249,695
Interest expense:				
Deposits	5,934	7,417	18,963	28,233
Borrowings	14,265	25,365	44,367	74,552
Junior subordinated debentures	914	1,713	3,133	5,286
Total interest expense	21,113	34,495	66,463	108,071
Net interest income before provision for credit losses	54,806	49,012	164,193	141,624
Provision for credit losses	13,000	4,000	55,000	8,700
Net interest income after provision for credit losses	41,806	45,012	109,193	132,924
Other operating income:				
Impairment loss on investment securities	(1,850)		(1,850)	
Less: Noncredit-related impairment loss recorded in other comprehensive income	1,618		1,618	
Net impairment loss on investment securities recognized in earnings	(232)		(232)	
Service charges on deposit accounts	3,720	3,829	11,080	11,381
Trust and Investment Services	1,682	2,019	4,948	5,906
Bankcard services	605	580	1,725	1,779
BOLI income	685	932	2,081	3,151
Other	1,744	1,013	3,120	2,999
Gain on sale of securities	6,898		28,446	
Total other operating income	15,102	8,373	51,168	25,216
Other operating expenses:				

Salaries and employee benefits	15,618	15,943	46,814	46,987
Occupancy and Equipment	4,330	4,811	13,199	14,430
Professional services	1,646	1,600	4,998	5,015
Amortization of intangibles	734	898	2,257	2,694
Other	7,517	5,805	26,953	18,708
Total other operating expenses	29,845	29,057	94,221	87,834
Earnings before income taxes	27,063	24,328	66,140	70,306
Income taxes	7,741	6,868	17,789	19,510
Net earnings	$ 19,322	$ 17,460	$ 48,351	$ 50,796
Preferred stock dividend and other reductions	8,838	23	12,879	67
Net earnings allocated to common shareholders	$ 10,484	$ 17,437	$ 35,472	$ 50,729
Comprehensive income	$ 41,749	$ 6,949	$ 66,520	$ 30,437
Basic earnings per common share	$ 0.10	$ 0.21	$ 0.40	$ 0.61
Diluted earnings per common share	$ 0.10	$ 0.21	$ 0.40	$ 0.61
Cash dividends per common share	$ 0.085	$ 0.085	$ 0.255	$ 0.255

See accompanying notes to the consolidated financial statements.

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CVB FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY
AND COMPREHENSIVE INCOME
(Unaudited)
Amounts and shares in thousands

	Common Shares Outstanding	Preferred Stock	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income	Comprehensive Income	Total
Balance January 1, 2009	83,270	$ 121,508	$ 364,469	$ 100,184	$ 28,731		$ 614,892
Repurchase of Preferred Stock		(130,000)					(130,000)
Amortization of preferred stock discount		8,492		(8,492)			
Issuance of Common Stock	22,655		126,066				126,066
Proceeds from exercise of stock options	307		280				280
Tax benefit from exercise of stock options			62				62
Stock-based Compensation Expense			1,137				1,137
Cash dividends declared							
Common ($0.255 per share)				(23,174)			(23,174)
Preferred				(4,273)			(4,273)
Comprehensive income:							0
Net earnings				48,351		$ 48,351	48,351
Other comprehensive gain:							0
Unrealized gain on securities							0
available-for-sale, net					19,107	19,107	19,107
Non-credit-related impairment loss on investment securities recorded in the current year, net					(938)	(938)	(938)
						$ 66,520	

Comprehensive income							
Balance September 30, 2009	106,232	$	$ 492,014	$ 112,596	$ 46,900		$ 651,510

	Common Shares Outstanding	Common Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Comprehensive Income	Total
Balance January 1, 2008	83,165	$ 354,249	$ 66,569	$ 4,130		$ 424,948
Issuance of common stock	176	606				606
Repurchase of common stock	(71)	(650)				(650)
Tax benefit from exercise of stock options		172				172
Stock-based Compensation Expense		1,117				1,117
Adoption of EITF 06-4 Split Dollar Life Insurance			(571)			(571)
Cash dividends ($0.255 per share)			(21,239)			(21,239)
Comprehensive income:						
Net earnings			50,796		$ 50,796	50,796
Other comprehensive loss:						
Unrealized loss on securities available-for-sale, net				(20,359)	(20,359)	(20,359)
Comprehensive income					$ 30,437	
Balance September 30, 2008	83,270	$ 355,494	$ 95,555	$ (16,229)		$ 434,820

	At September 30, 2009	2008
Disclosure of reclassification amount		
Unrealized gain/(loss) on securities arising during the period	$ 59,540	$ (35,101)
Tax (benefit)/expense	(25,007)	14,742
Less:		
Reclassification adjustment for net gain on securities included in net income	(28,214)	
Add:		
Tax expense on reclassification adjustments	11,850	
Net unrealized gain/(loss) on securities	$ 18,169	$ (20,359)

See accompanying notes to the consolidated financial statements.

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CVB FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
Dollar amounts in thousands

	For the Nine Months Ended September 30, 2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES:		
Interest and dividends received	$ 230,996	$ 247,921
Service charges and other fees received	22,407	25,195
Interest paid	(67,785)	(103,215)
Cash paid to vendors and employees	(81,618)	(84,264)
Income taxes paid	(34,586)	(19,346)
Net cash provided by operating activities	69,414	66,291
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sales of investment securities	459,092	
Proceeds from repayment of investment securities	296,052	262,540
Proceeds from maturity of investment securities	153,562	25,244
Purchases of investment securities	(790,231)	(328,089)
Purchases of FHLB stock		(12,371)
Net decrease/(increase) in loans and lease finance receivables	111,125	(98,568)
Proceeds from sales of premises and equipment	234	110
Proceeds from sales of other real estate owned	12,823	
Purchase of premises and equipment	(3,297)	(2,966)
Other, net	(410)	(293)
Net cash provided by/(used in) investing activities	238,950	(154,393)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase/(decrease) in transaction deposits	338,369	(93,208)
Net increase/(decrease) in time deposits	193,246	(75,600)
Advances from Federal Home Loan Bank		450,000
Repayment of advances from Federal Home Loan Bank	(600,000)	(100,000)
Net decrease in other borrowings	(184,592)	(93,708)
Net increase in repurchase agreements	102,513	24,664
Cash dividends on preferred stock	(4,273)	
Cash dividends on common stock	(23,174)	(21,239)
Repurchase of preferred stock	(130,000)	
Issuance of common stock	126,066	(650)
Proceeds from exercise of stock options	280	606
Tax benefit related to exercise of stock options	62	172
Net cash (used in)/provided by financing activities	(181,503)	91,037
NET INCREASE IN CASH AND CASH EQUIVALENTS	126,861	2,935
CASH AND CASH EQUIVALENTS, beginning of period	95,297	89,486

CASH AND CASH EQUIVALENTS, end of period	$ 222,158	$ 92,421

See accompanying notes to the consolidated financial statements.

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CVB FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
(unaudited)
Dollar amounts in thousands

	For the Nine Months Ended September 30, 2009	2008
RECONCILIATION OF NET EARNINGS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net earnings	$ 48,351	$ 50,796
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Gain on sale of investment securities	(28,446)	
Loss on sale of premises and equipment	53	169
Gain on sale of other real estate owned	(512)	
Credit-related impairment loss on investment securities held-to-maturity	232	
Increase from bank owned life insurance	(2,081)	(3,151)
Net amortization of premiums on investment securities	1,715	1,205
Provisions for credit losses	55,000	8,700
Stock-based compensation	1,137	1,117
Depreciation and amortization	7,401	8,290
Change in accrued interest receivable	1,089	934
Change in accrued interest payable	(1,320)	4,856
Change in other assets and liabilities	(13,205)	(6,625)
Total adjustments	21,063	15,495
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 69,414	$ 66,291
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING ACTIVITIES		
Transfer from loans to Other Real Estate Owned	$ 7,644	$ 1,927

See accompanying notes to the consolidated financial statements.

CVB FINANCIAL CORP. AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)
For the nine months ended September 30, 2009 and 2008

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying condensed consolidated unaudited financial statements and notes thereto have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission for Form 10-Q and conform to practices within the banking industry and include all of the information and disclosures required by accounting principles generally accepted in the United States of America for interim financial reporting. The results of operations for the nine months ended September 30, 2009 are not necessarily indicative of the results for the full year. These financial statements should be read in conjunction with the financial statements, accounting policies and financial notes thereto included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2008 filed with the Securities and Exchange Commission. In the opinion of management, the accompanying condensed consolidated unaudited financial statements reflect all adjustments (consisting only of normal recurring adjustments), which are necessary for a fair presentation of financial results for the interim periods presented. A summary of the significant accounting policies consistently applied in the preparation of the accompanying consolidated financial statements follows.

Principles of Consolidation The consolidated financial statements include the accounts of CVB Financial Corp. (the Company) and its wholly owned subsidiary: Citizens Business Bank (the Bank) after elimination of all intercompany transactions and balances. The Company also has three inactive subsidiaries: CVB Ventures, Inc.; Chino Valley Bancorp; and Orange National Bancorp. The Company is also the common stockholder of CVB Statutory Trust I, CVB Statutory Trust II, CVB Statutory Trust III and FCB Trust II. CVB Statutory Trusts I and II were created in December 2003 and CVB Statutory Trust III was created in January 2006 to issue trust preferred securities in order to raise capital for the Company. The Company acquired FCB Trust II through the acquisition of First Coastal Bancshares (FCB). These trusts do not meet the criteria for consolidation.

Nature of Operations The Company s primary operations are related to traditional banking activities, including the acceptance of deposits and the lending and investing of money through the operations of the Bank. The Bank also provides automobile and equipment leasing to customers through its Citizens Financial Services Division and trust services to customers through its CitizensTrust Division. The Bank s customers consist primarily of small to mid-sized businesses and individuals located in San Bernardino County, Riverside County, Orange County, Los Angeles County, Madera County, Fresno County, Tulare County, Kern County and San Joaquin County. The Bank operates 41 Business Financial Centers and 5 Commercial Banking Centers with its headquarters located in the city of Ontario.

The Company s operating business units have been combined into two main segments: (i) Business Financial and Commercial Banking Centers and (ii) Treasury. Business Financial and Commercial Banking Centers (branches) are comprised of loans, deposits, and products and services the Bank offers to the majority of its customers. The other segment is Treasury, which manages the investment portfolio of the Company. The Company s remaining centralized functions and eliminations of inter-segment amounts have been aggregated and included in Other.

The internal reporting of the Company considers all business units. Funds are allocated to each business unit based on its need to fund assets (use of funds) or its need to invest funds (source of funds). Net income is determined based on the actual net income of the business unit plus the allocated income or expense based on the sources and uses of funds for each business unit. Non-interest income and non-interest expense are those items directly attributable to a business unit.

FASB Accounting Standards Codification The FASB has issued FASB Statement No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles. Statement 168 establishes the FASB Accounting Standards Codification as the single source of authoritative U.S. generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission (SEC) under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. The Codification supersedes all existing non-SEC accounting and reporting standards. All other nongrandfathered, non-SEC accounting literature not included in the Codification will become nonauthoritative.

Following the Codification, the Board will not issue new standards in the form of Statements, FASB Staff Positions or Emerging Issues Task Force Abstracts. Instead, it will issue Accounting Standards Updates, which will serve to update the Codification, provide background information about the guidance and provide the basis for conclusions on the changes to the Codification.

GAAP is not intended to be changed as a result of the FASB s Codification project, but it will change the way the guidance is organized and presented. As a result, these changes will have a significant impact on how companies reference GAAP in their financial statements and in their accounting policies for financial statements issued for interim and annual periods ending after September 15, 2009.

Cash and due from banks Cash on hand, cash items in the process of collection, and amounts due from correspondent banks and the Federal Reserve Bank are included in Cash and due from banks.

Investment Securities The Company classifies as held-to-maturity those debt securities that the Company has the positive intent and ability to hold to maturity. Securities classified as trading are those securities that are bought and held principally for the purpose of selling them in the near term. All other debt and equity securities are classified as available-for-sale. Securities held-to-maturity are accounted for at cost and adjusted for amortization of premiums and accretion of discounts. Trading securities are accounted for at fair value with the unrealized gains and losses being included in current earnings. Available-for-sale securities are accounted for at fair value, with the net unrealized gains and losses, net of income tax effects, presented as a separate component of stockholders equity. Realized gains and losses on sales of securities are recognized in earnings at the time of sale and are determined on a specific-identification basis. Purchase premiums and discounts are recognized in interest income using the effective-yield method over the terms of the securities. For mortgage-backed securities (MBS), the amortization or accretion is based on estimated average lives of the securities. The lives of these securities can fluctuate based on the amount of prepayments received on the underlying collateral of the securities. The Company s investment in Federal Home Loan Bank (FHLB) stock is carried at cost.

At each reporting date, securities are assessed to determine whether there is an other-than-temporary impairment. Other-than-temporary impairment on investment securities is recognized in earnings when there are credit losses on a debt security for which management does not intend to sell and for which it is more-likely-than-not that the Company will not have to sell prior to recovery of the noncredit impairment. In those situations, the portion of the total impairment that is attributable to the credit loss would be recognized in earnings, and the remaining difference between the debt security s amortized cost and its fair value would be included in other comprehensive income.

Loans and Lease Finance Receivables Loans and lease finance receivables are reported at the principal amount outstanding, less deferred net loan origination fees. Interest on loans and lease finance receivables is credited to income based on the principal amount outstanding. Interest income is not recognized on loans and lease finance receivables when collection of interest is deemed by management to be doubtful. In the ordinary course of business, the Company enters into commitments to extend credit to its customers. These commitments are not reflected in the accompanying consolidated financial statements. As of September 30, 2009, the Company had entered into commitments with certain customers amounting to $559.5 million compared to $642.7 million at December 31, 2008. Letters of credit at September 30, 2009 and December 31, 2008, were $69.8 million and $63.1 million, respectively.

The Bank receives collateral to support loans, lease finance receivables, and commitments to extend credit for which collateral is deemed necessary. The most significant categories of collateral are real estate, principally commercial and industrial income-producing properties, real estate mortgages, and assets utilized in agribusiness.

Nonrefundable fees and direct costs associated with the origination or purchase of loans are deferred and netted against outstanding loan balances. The deferred net loan fees and costs are recognized in interest income over the loan term using the effective-yield method.

Provision and Allowance for Credit Losses The determination of the balance in the allowance for credit losses is based on an analysis of the loan and lease finance receivables portfolio using a systematic methodology and reflects an amount that, in management s judgment, is adequate to provide for probable credit losses inherent in the portfolio, after giving consideration to the character of the loan portfolio, current economic conditions, past credit loss experience, and such other factors that would deserve current recognition in estimating inherent credit losses. The estimate is reviewed quarterly by the Board of Directors and management and periodically by various regulatory entities and, as adjustments become necessary, they are reported in earnings in the periods in which they become known. The provision for credit losses is charged to expense. During the first nine months of 2009, we recorded a provision for credit losses of $55.0 million. The allowance for credit losses was $87.3 million as of September 30, 2009.

In addition to the allowance for credit losses, the Company also has a reserve for undisbursed commitments for loans and letters of credit. This reserve is carried in the liabilities section of the balance sheet in other liabilities. Provisions to this reserve are included in other expense. For the first nine months of 2009, the Company recorded an increase of $1.8 million in the reserve for undisbursed commitments. As of September 30, 2009, the balance in this reserve was $6.0 million.

A loan for which collection of principal and interest according to its original terms is not probable is considered to be impaired. The Company s policy is to record a specific valuation allowance, which is included in the allowance for credit losses, or charge off that portion of an impaired loan that exceeds its fair value. Fair value is usually based on the value of underlying collateral.

At September 30, 2009, the Company had impaired loans of $61.1 million. Of this amount, $15.7 million consisted of non-accrual residential construction and land loans, $19.6 million in non-accrual commercial construction loans, $8.1 million of non-accrual single family mortgage loans, $13.5 million of non-accrual commercial real estate loans, $1.1 million of non-accrual commercial and industrial loans, $100,000 of non-accrual consumer loans and $3.0 million of loans whose terms were modified in a troubled debt restructure. The impaired loans of $61.1 million, net of $16.2 million in charge-offs, are supported by collateral with a fair value less selling costs, net of prior liens. For the collateral-deficient loans, the amount of specific reserve was $2.0 million at September 30, 2009. At December 31, 2008, the Bank had classified as impaired, loans with a balance of $20.2 million.

Premises and Equipment Premises and equipment are stated at cost, less accumulated depreciation, which is provided for in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives using the straight-line method. Properties under capital lease and leasehold improvements are amortized over the shorter of estimated economic lives of 15 years or the initial terms of the leases. Estimated lives are 3 to 5 years for computer and equipment, 5 to 7 years for furniture, fixtures and equipment, and 15 to 40 years for buildings and improvements. Long-lived assets are reviewed periodically for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. The existence of impairment is based on undiscounted cash flows. To

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the extent impairment exists, the impairment is calculated as the difference in fair value of assets and their carrying value. The impairment loss, if any, would be recorded in noninterest expense.

Other Real Estate Owned Other real estate owned (OREO) represents real estate acquired through foreclosure in satisfaction of commercial and real estate loans and is stated at fair value, minus estimated costs to sell (fair value at time of foreclosure). Loan balances in excess of fair value of the real estate acquired at the date of acquisition are charged against the allowance for credit losses. Any subsequent operating expenses or income, reduction in estimated values, and gains or losses on disposition of such properties are charged to current operations. OREO is recorded in other assets on the consolidated balance sheets.

Business Combinations and Intangible Assets The Company has engaged in the acquisition of financial institutions and the assumption of deposits and purchase of assets from other financial institutions in its market area. The Company has paid premiums on certain transactions, and such premiums are recorded as intangible assets, in the form of goodwill or other intangible assets. Goodwill is not being amortized whereas identifiable intangible assets with finite lives are amortized over their useful lives. On an annual basis, the Company tests goodwill and intangible assets for impairment. The Company completed its annual impairment test as of July 1, 2009; there was no impairment of goodwill.

At September 30, 2009 goodwill was $55.1 million. As of September 30, 2009, intangible assets that continue to be subject to amortization include core deposit premiums of $8.8 million (net of $18.3 million of accumulated amortization). Amortization expense for such intangible assets was $2.3 million for the nine months ended September 30, 2009. Estimated amortization expense, for the remainder of 2009 is expected to be $733,000. Estimated amortization expense, for the succeeding five fiscal years is $2.9 million for year one, $2.8 million for year two, $1.6 million for year three, $627,000 for year four and $26,000 for year five. The weighted average remaining life of intangible assets is approximately 2.4 years.

Bank Owned Life Insurance The Bank invests in Bank-Owned Life Insurance (BOLI). BOLI involves the purchasing of life insurance by the Bank on a select group of employees. The Bank is the owner and beneficiary of these policies. BOLI is recorded as an asset at cash surrender value. Increases in the cash value of these policies, as well as insurance proceeds received, are recorded in other non-interest income and are not subject to income tax.

Income Taxes Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Future realization of deferred tax assets ultimately depends on the existence of sufficient taxable income of the appropriate character (for example, ordinary income or capital gain) within the carryback or carryforward periods available under the tax law. Based on historical and future expected taxable earnings and available strategies, the Company considers the future realization of these deferred tax assets more likely than not.

The tax effects from an uncertain tax position are recognized in the financial statements only if, based on its merits, the position is more likely than not to be sustained on audit by the taxing authorities. Interest and penalties related to uncertain tax positions are recorded as part of other operating expense.

Earnings per Common Share The Company calculates earnings per common share (EPS) using the two-class method. 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. All outstanding unvested share-based payment awards that contain rights to non-forfeitable dividends are considered participating securities. The Company grants restricted shares under the 2008 Equity Incentive Plan that qualify as participating securities. Restricted shares issued under this plan are entitled to dividends at the same rate as common stock.

Basic earnings per common share are computed by dividing income allocated to common stockholders by the weighted-average number of common shares outstanding during each period. The computation of diluted earnings per common share considers the number of tax-effected shares issuable upon the assumed exercise of outstanding common stock options. Share and per share amounts have been retroactively restated to give effect to all stock dividends and splits. The number of shares outstanding at September 30, 2009 was 106,231,511. The tables below presents the reconciliation of earnings per share for the periods indicated.

Earnings Per Share Reconciliation

(Dollars and shares in thousands, except per share amounts)

	For the nine months ended September 30,		For the three months ended September 30,	
	2009	2008	2009	2008
Earnings per common share				
Net earnings	$ 48,351	$ 50,796	$ 19,322	$ 17,460
Less: Dividends on preferred stock and discount amortization	12,765		8,804	
Net earnings available to common shareholders	$ 35,586	$ 50,796	$ 10,518	$ 17,460
Less: Net earnings allocated to restricted stock	114	67	34	23
Net earnings allocated to common shareholders (numerator)	$ 35,472	$ 50,729	$ 10,484	$ 17,437
Weighted Average Shares Outstanding (denominator)	88,601	83,106	99,242	83,148
Earnings per common share (1)	$ 0.40	$ 0.61	$ 0.10	$ 0.21
Diluted earnings per common share				
Net income allocated to common shareholders (numerator)	$ 35,472	$ 50,729	$ 10,484	$ 17,437
Weighted Average Shares Outstanding	88,601	83,106	99,242	83,148
Incremental shares from assumed exercise of outstanding options	97	223	90	225
Diluted Weighted Average Shares Outstanding (denominator)	88,698	83,329	99,332	83,373
Diluted earnings per common share (1)	$ 0.40	$ 0.61	$ 0.10	$ 0.21

(1) Substantially all of the decrease in earnings and diluted earnings per common share for each period presented is due to the preferred stock dividend and discount amortization

Stock-Based Compensation At September 30, 2009, the Company has three stock-based employee compensation plans, which are described more fully in Note 15 in the Company s Annual Report on Form 10-K.

There were 922,500 options and 250,000 restricted stock awards granted in September 2009. The options and stock awards will vest, in equal installments, over a five-year period. The options and restricted stock awards were issued at the stock price on the date of grant at $8.61. The fair value of each stock option granted was estimated on the date of grant using the following weighted-average assumptions:

	2009
Dividend Yield	3.95%
Volatility	47.3%
Risk-free interest rate	2.5%
Expected life	7.2years
Fair Value	$2.89

The expected volatility is solely based on the daily historical stock price volatility over the expected option life. The expected life of options granted is derived from the output of the option valuation model and represents the period of time an optionee will hold an option before exercising it. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury five-year constant maturity yield curve in effect at the time of the grant.

Option activity under the Company s stock compensation plans as of September 30, 2009 and changes for the nine months ended September 30, 2009 were as follows:

Options	Number of Stock Options Outstanding (000)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in Years)	Aggregate Intrinsic Value ($000)
Outstanding at January 1, 2009	2,249	$ 10.64		
Granted	931	$ 8.59		
Exercised	(56)	$ 4.97		
Forfeited or expired	(8)	$ 11.76		
Outstanding at September 30, 2009	3,116	$ 10.13	6.60	$ 862
Vested or expected to vest at September 30, 2009	2,921	$ 10.16	6.40	$ 861
Exercisable at September 30, 2009	1,598	$ 10.56	4.14	$ 855

As of September 30, 2009, there was $4.2 million of total unrecognized compensation costs related to non-vested options granted under the plans. The cost is expected to be recognized over a weighted-average period of approximately 3.9 years. The expense recognized for stock options was $270,000 and $913,000 for the three and nine months ended September 30, 2009.

A summary of the activity of the Company s non-vested restricted shares as of September 30, 2009 and changes during the nine months ended September 30, 2009, is presented below:

	2009	
Nonvested Restricted Shares	Shares (000)	Weighted Average Fair Value
Nonvested at January 1,	105	$ 10.55
Granted	250	$ 8.61
Vested	(25)	$ 10.98
Forfeited		$
Nonvested at September 30,	330	$ 9.04

As of September 30, 2009, there was $2.5 million of total unrecognized compensation costs related to non-vested shares granted under the plans. The cost is expected to be recognized over a weighted- average period of approximately 4.4 years. The expense recognized for restricted stock was $84,000 and $224,000 for the three and nine months ended September 30, 2009.

Derivative Financial Instruments All derivative instruments, including certain derivative instruments embedded in other contracts, are recognized on the consolidated balance sheet at fair value. For derivatives designated as fair value hedges, changes in the fair value of the derivative and the hedged item related to the hedged risk are recognized in earnings. Changes in fair value of derivatives designated and accounted for as cash flow hedges, to the extent they are effective as hedges, are recorded in Other Comprehensive Income, net of deferred taxes and are subsequently reclassified to earnings when the hedged transaction affects earnings. Any hedge ineffectiveness would be recognized in the income statement line item pertaining to the hedged item.

Statement of Cash Flows Cash and cash equivalents as reported in the statements of cash flows include cash and due from banks. Cash flows from loans and deposits are reported net.

CitizensTrust This division provides trust, investment and brokerage related services, as well as financial, estate and business succession planning services. The Company maintains funds in trust for customers. CitizensTrust has approximately $1.9 billion in assets under administration, including $991.9

million in assets under management. The amount of these funds and the related liability have not been recorded in the accompanying consolidated balance sheets because they are not assets or liabilities of the Bank or Company, with the exception of any funds held on deposit with the Bank.

Use of Estimates in the Preparation of Financial Statements The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. A material estimate that is particularly susceptible to significant change in the near term relates to the determination of the allowance for credit losses. Other significant estimates which may be subject to change include fair value disclosures, impairment of investments and goodwill, and valuation of deferred tax assets, other intangibles and OREO.

Recent Accounting Pronouncements In August 2009, the FASB issued Accounting Standards Update (ASU) 2009-05, Fair Value Measurements and Disclosures (Topic 820) - Measuring Liabilities at Fair Value. The update addresses practice difficulties caused by the tension between fair-value measurements based on the price that would be paid to transfer a liability to a new obligor and contractual or legal requirements that prevent such transfers from taking place. Companies determining the fair value of a liability may use the perspective of an investor that holds the related obligation as an asset. The new guidance is effective for interim and annual reporting periods beginning after August 27, 2009, and applies to all fair-value measurements of liabilities required by GAAP. The adoption of ASU 2009-05 did not have a material effect on the Company s consolidated financial position or results of operations.

Shareholder Rights Plan The Company has a shareholder rights plan designed to maximize long-term value and to protect shareholders from improper takeover tactics and takeover bids which are not fair to all shareholders. In accordance with the plan, preferred share purchase rights were distributed as a dividend at the rate of one right to purchase one one-thousandth of a share of the Company s Series A Participating Preferred Stock at an initial exercise price of $50.00 (subject to adjustment as described in the terms of the plan) upon the occurrence of certain triggering events. For additional information concerning this plan, see Note 11 to Consolidated Financial Statements, Commitments and Contingencies contained in the Company s Annual Report on Form 10-K for the year ended December 31, 2008.

Other Contingencies In the ordinary course of business, the Company becomes involved in litigation. Based upon the Company s internal records and discussions with legal counsel, the Company records reserves for estimates of the probable outcome of all cases brought against them. At September 30, 2009, the Company does not have any litigation reserves and is not aware of any material pending legal action or complaints asserted against the Company.

2. INVESTMENTS

The amortized cost and estimated fair value of investment securities are shown below. The majority of securities held are publicly traded, and the estimated fair values were obtained from an independent pricing service based upon market quotes.

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Table 3 Composition of Investment Securities

	September 30, 2009				
	Amortized Cost	Gross Unrealized Holding Gain	Gross Unrealized Holding Loss	Fair Value	Total Percent
	(Amounts in thousands)				
Investment Securities Available-for-Sale:					
Government agency & government-sponsored enterprises	$ 96,386	$ 253	$ (78)	$ 96,561	4.23%
Mortgage-backed securities	666,402	22,382		688,784	30.13%
CMO s / REMIC s	781,293	23,075	(1,002)	803,366	35.15%
Municipal bonds	658,896	38,121	(272)	696,745	30.49%
Total Investment Securities	$ 2,202,977	$ 83,831	$ (1,352)	$ 2,285,456	100.00%

	December 31, 2008				
	Amortized Cost	Gross Unrealized Holding Gain	Gross Unrealized Holding Loss	Fair Value	Total Percent
	(Amounts in thousands)				
Investment Securities Available-for-Sale:					
Government agency & government-sponsored enterprises	$ 27,105	$ 673	$	$ 27,778	1.11%
Mortgage-backed securities	1,150,650	33,836	(1)	1,184,485	47.50%
CMO s / REMIC s	591,531	9,855	(4,595)	596,791	23.94%
Municipal bonds	674,655	16,704	(6,937)	684,422	27.45%
Total Investment Securities	$ 2,443,941	$ 61,068	$ (11,533)	$ 2,493,476	100.00%

Approximately 68% of the available-for-sale portfolio represents securities issued by the U.S government or U.S. government-sponsored enterprises, which guarantee payment of principal and interest.

The remaining CMO/REMICs are backed by agency-pooled collateral or whole loan collateral. All non-agency available-for-sale CMO/REMIC issues held are rated investment grade or better by either Standard & Poor s or Moody s, as of September 30, 2009 and December 31, 2008.

Gross realized gains were $28.4 million and $6.9 million for the nine and three months ended September 30, 2009, respectively. There were no realized gains or losses during the same periods ended September 30, 2008.

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Composition of the Fair Value and Gross Unrealized Losses of Securities:

	September 30, 2009					
	Less than 12 months		12 months or longer		Total	
Description of Securities	**Fair Value**	**Gross Unrealized Holding Losses**	**Fair Value**	**Gross Unrealized Holding Losses**	**Fair Value**	**Gross Unrealized Holding Losses**
			(amounts in thousands)			
Held-To-Maturity						
CMO (1)	$	$	$ 4,237	$ 1,618	$ 4,237	$ 1,618
Available-for-Sale						
Government agency	$ 25,109	$ 78	$	$	$ 25,109	$ 78
CMO/REMICs	46,438	555	31,101	447	77,539	1,002
Municipal bonds	4,916	272			4,916	272
	$ 76,463	$ 905	$ 31,101	$ 447	$ 107,564	$ 1,352

(1) For the nine months ended September 30, 2009, the Company recorded $1.6 million, on a pre-tax basis, of the non-credit portion of OTTI for this security in other comprehensive income, which is included as gross unrealized losses.

	December 31, 2008					
	Less than 12 months		12 months or longer		Total	
Description of Securities	**Fair Value**	**Gross Unrealized Holding Losses**	**Fair Value**	**Gross Unrealized Holding Losses**	**Fair Value**	**Gross Unrealized Holding Losses**

			(amounts in thousands)			
Held-To-Maturity						
CMO	$ 4,770	$ 2,097	$	$	$ 4,770	$ 2,097
Available-for-Sale						
Mortgage-backed securities	$ 265	$	$ 13,903	$ 1	$ 14,168	$ 1
CMO/REMICs	163,036	4,542	1,853	53	164,889	4,595
Municipal bonds	159,370	5,341	37,994	1,596	197,364	6,937
	$ 322,671	$ 9,883	$ 53,750	$ 1,650	$ 376,421	$ 11,533

The tables above show the Company s investment securities gross unrealized losses and fair value by investment category and length of time that individual securities have been in a continuous unrealized loss position, at September 30, 2009 and December 31, 2008. The Company has reviewed individual securities to determine whether a decline in fair value below the amortized cost is other-than-temporary.

The following summarizes our analysis of these securities and the unrealized losses. This assessment was based on the following factors: i) the length of the time and the extent to which the fair value has been less than amortized cost; ii) adverse condition specifically related to the security, an industry, or a geographic area and whether or not the Company expects to recover the entire amortized cost, iii) historical and implied volatility of the fair value of the security; iv) the payment structure of the security and the likelihood of the issuer being able to make payments in the future; v.) failure of the issuer of the security to make scheduled interest or principal payments, vi) any changes to the rating of the security by a rating agency, and vii) recoveries or additional declines in fair value subsequent to the balance sheet date.

CMO Held-to-Maturity We have one investment security classified as held-to-maturity. This security was issued by Countrywide Financial and is collateralized by Alt-A mortgages. The mortgages are primarily fixed-rate, 30-year loans, originated in early 2006 with average FICO scores of 715 and an average LTV of 71% at origination. The security was a senior security in the securitization, was rated triple AAA at origination and was supported by subordinate securities. This security is classified as held-to-maturity as we have both the intent and ability to hold this debt security to maturity as the amount of the security, $4.2 million, is not significant to our liquidity needs. We acquired this security in February

2008 at a price of 98.25%. The significant decline in the fair value of the security first appeared in August 2008 as the current financial crisis in the markets occurred and the market for securities collateralized by Alt-A mortgages diminished.

As of September 30, 2009, the unrealized loss on this security was $1.8 million and the fair value on the security was 69% of the current par value. The security is rated non-investment grade. We evaluated the security for an other than temporary decline in fair value as of September 30, 2009. We assess for credit impairment using a cash flow model. The key assumptions include default rates, severities and prepayment rates. This security was determined to be credit impaired during the current quarter as opposed to prior quarters due to further degradation in expected cash flows primarily due to higher loss forecasts. We determined the amount of the credit impairment by discounting the expected future cash flows of the underlying collateral. We recognized an other-than-temporary impairment of $1.8 million reduced by $1.6 million for the non-credit portion which was reflected in other comprehensive income. The remaining loss of $232,000 was recognized in third quarter earnings.

The following table provides a roll-forward of credit-related other-than-temporary impairment recognized in earnings for the three and nine months ended September 30, 2009.

		Three and Nine Months Ended September 30, 2009
Balance, beginning of the period	$	
Addition of OTTI that was not previously recognized		232
Reduction for securities sold during the period		
Reduction for securities with OTTI recognized in earnings because the security might be sold before recovery of its amortized cost basis		
Addition of OTTI that was previously recognized because the security might not be sold before recovery of its amortized cost basis		
Reduction for increases in cash flows expected to be collected that are recognized over the remaining life of the security		
Balance, end of the period	$	232

Government Agency The government agency bonds are backed by the full faith and credit of Agencies of the U.S. Government. These securities are bullet securities, that is, they have a defined maturity date on which the principal is paid. The contractual term of these investments provides that the Bank will receive the face value of the bond at maturity which will equal the amortized cost of the bond. Interest is received throughout the life of the security. There was no loss greater than 12 months on these securities at September 30, 2009.

Mortgaged-Backed Securities and CMO/REMICs Almost all of the mortgage-backed and CMO/REMICs securities are issued by the government-sponsored enterprises such as Ginnie Mae, Fannie Mae and Freddie Mac. These securities are collateralized or backed by the underlying residential mortgages. All mortgage-backed securities are rated investment grade with an average life of approximately 3.8 years. The contractual cash flows of 97.9% of these investments are guaranteed by U.S. government-sponsored agencies. The remaining 2.1% are issued by banks. Accordingly, it is expected the securities would not be settled at a price less than the amortized cost of the bonds. The unrealized loss greater than 12 months on these securities at September 30, 2009 is $447,000. This loss is comprised of bonds issued by non-government sponsored enterprises such as financial institutions with a loss of $326,000 and two FHLMC securities with a loss of $121,000. Because we believe the decline in fair value is attributable to the changes in interest rates and not credit quality and because the Company does not intend to sell the investments and it is more likely than not that the Company will not be required

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to sell the investments before recovery of their amortized costs, which may be at maturity, management does not consider these investments to be other than temporarily impaired at September 30, 2009.

Municipal Bonds Ninety-four percent of our $696.7 million municipal bond portfolio contains securities which have an underlying rating of investment grade. The majority of our municipal bonds are insured by the largest bond insurance companies with maturities of approximately 5.1 years. There is no unrealized loss greater than 12 months on these securities at September 30, 2009. The Bank diversifies its holdings by owning selections of securities from different issuers and by holding securities from geographically diversified municipal issuers, thus reducing the Bank s exposure to any single adverse event.

We are continually monitoring the quality of our municipal bond portfolio in light of the current financial problems exhibited by certain monoline insurance companies. While most of our securities are insured by these companies, we feel that there is minimal risk of loss due to the problems these insurers are having. Many of the securities that would not be rated without insurance are pre-refunded and/or are general obligation bonds. Based on our monitoring of the municipal marketplace, to our knowledge, none of the municipalities are exhibiting financial problems that would lead us to believe there is a loss in any given security.

At September 30, 2009 and December 31, 2008, investment securities having an amortized cost of approximately $2.0 billion and $2.32 billion respectively, were pledged to secure public deposits, short and long-term borrowings, and for other purposes as required or permitted by law.

The amortized cost and fair value of debt securities at September 30, 2009, by contractual maturity, are shown below. Although mortgage-backed securities and CMO/REMICs have contractual maturities through 2039, expected maturities will differ from contractual maturities because borrowers may have the right to prepay such obligations without penalty. Mortgage-backed securities and CMO/REMICs are included in maturity categories based upon estimated prepayment speeds.

	Available-for-sale		
	Amortized Cost	Fair Value	Weighted-Average Yield
	(amounts in thousands)		
Due in one year or less	$ 220,431	$ 222,741	3.98%
Due after one year through five years	1,028,218	1,067,139	4.47%
Due after five years through ten years	900,220	939,536	4.36%
Due after ten years	54,108	56,040	4.04%
	$ 2,202,977	$ 2,285,456	4.36%

The investment in FHLB stock is periodically evaluated for impairment based on, among other things, the capital adequacy of the FHLB and its overall financial condition. No impairment losses have been recorded through September 30, 2009.

3. FAIR VALUE INFORMATION

The following disclosure provides fair value information for financial assets and liabilities as of September 30, 2009. The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels (Level 1, Level 2, and Level 3).

Level 1 Valuation is based upon quoted prices for identical instruments traded in active markets.

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Level 2 Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company s own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flows and similar techniques.

Determination of Fair Value

The following is a description of valuation methodologies used for assets and liabilities recorded at fair value and for estimating fair value for financial instruments not recorded at fair value.

Cash The carrying amount of cash and cash equivalents is considered to be a reasonable estimate of fair value.

Investment securities available-for-sale Investment securities available-for-sale are valued based upon quotes obtained from a reputable third-party pricing service. The service uses evaluated pricing applications and model processes. Market inputs, such as, benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data are considered as part of the evaluation. The inputs are related directly to the security being evaluated, or indirectly to a similarly situated security. Market assumptions and market data are utilized in the valuation models. Accordingly, the Company categorized its investment portfolio as a Level 2 valuation.

Investment security held-to-maturity Investment security held-to-maturity is carried at amortized cost-basis on the balance sheet. The fair value is determined using the same process described above for available-for-sale securities. During the third quarter ended, an other-than-temporary impairment loss was recognized and the carrying balance was reduced to fair value.

Loans The carrying amount of loans and lease finance receivables is their contractual amounts outstanding, reduced by deferred net loan origination fees and the allocable portion of the allowance for credit losses.

The fair value of loans, other than loans on non-accrual status, was estimated by discounting the remaining contractual cash flows using the estimated current rate at which similar loans would be made to borrowers with similar credit risk characteristics and for the same remaining maturities, reduced by deferred net loan origination fees and the allocable portion of the allowance for credit losses. Accordingly, in determining the estimated current rate for discounting purposes, no adjustment has been made for any change in borrowers credit risks since the origination of such loans. Rather, the allocable portion of the allowance for credit losses is considered to provide for such changes in estimating fair value.

The fair value of loans on non-accrual status has not been specifically estimated because it is not practicable to reasonably assess the credit risk adjustment that would be applied in the marketplace for such loans. As such, the estimated fair value of total loans at September 30, 2009 includes the carrying amount of non-accrual loans at each respective date, net of allowance for credit losses.

Impaired loans and OREO are generally measured using the fair value of the underlying collateral, which is determined based on the most recent appraisal information received, less costs to sell. These loans fall within Level 2 of the fair value hierarchy. Appraised values may be adjusted based on factors such as the changes in market conditions from the time of valuation. These loans fall within Level 3 of the fair value hierarchy.

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The fair value of commitments to extend credit and standby letters of credit were not significant at September 30, 2009 as these instruments predominantly have adjustable terms and are of a short-term nature.

Swaps The fair value of the interest rate swap contracts are provided by our counterparty using a system that constructs a yield curve based on cash LIBOR rates, Eurodollar futures contracts, and 3-year through 30-year swap rates. The yield curve determines the valuations of the interest rate swaps. Accordingly, the swap is categorized as a Level 2 valuation.

Deposits & Borrowings The amounts payable to depositors for demand, savings, and money market accounts, and the demand note to the U.S. Treasury, and short-term borrowings are considered to be stated at fair value. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities. The fair value of long-term borrowings and junior subordinated debentures is estimated using the rates currently offered for borrowings of similar remaining maturities.

Accrued Interest Receivable/Payable The amounts of accrued interest receivable on loans and lease finance receivables and investments and accrued interest payable on deposits and borrowings are considered to be stated at fair value.

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

Assets & Liabilities Measured at Fair Value on a Recurring Basis

(in thousands)	**Carrying Value at September 30, 2009**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Description of Assets				
Mortgage-backed securities	$ 688,784	$	$ 688,784	$
CMO s / REMIC s	803,366		803,366	
Government agency	96,561		96,561	
Municipal bonds	696,745		696,745	
Investment Securities-AFS	$ 2,285,456	$	$ 2,285,456	$
Interest Rate Swaps	5,761		5,761	
Total Assets	$ 2,291,217	$	$ 2,291,217	$
Description of Liability				
Interest Rate Swaps	$ 5,761	$	$ 5,761	$

We may be required to measure certain assets at fair value on a nonrecurring basis in accordance with GAAP. These adjustments to fair value usually result from application of lower-of-cost-or-market accounting or write-downs of individual assets. For assets measured at fair value on a nonrecurring basis that were still held in the balance sheet at quarter end, the following table provides the level of valuation assumptions used to determine each adjustment and the carrying value of the related assets at quarter end.

Assets & Liabilities Measured at Fair Value on a Non-Recurring Basis

(in thousands)	Carrying Value at September 30, 2009	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	For the nine months ended September 30, 2009 Total Losses
Description of Assets					
Investment Security-HTM	$ 4,237	$	$4,237	$	$ (232)
Impaired Loans (1)	$ 44,779	$	$3,319	$41,460	$(18,240)
OREO	$ 1,137	$	$	$ 1,137	$ (848)

(1) Impaired loans of $16.3 million have sufficient collateral value to cover losses and are recorded at carrying value.

The following table presents estimated fair value of financial instruments. The estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is required to develop the estimates of fair value. Accordingly, the estimates presented below are not necessarily indicative of the amounts the Company could have realized in a current market exchange as of September 30, 2009. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

FAIR VALUE INFORMATION

	September 30, 2009	
	Carrying Amount	Estimated Fair Value
	(amounts in thousands)	
Assets		
Cash and cash equivalents	$ 222,158	$ 222,158
Federal funds sold and Interest-bearing balances due from depository institutions	150,285	150,285
FHLB Stock	93,240	93,240
Investment securities available-for-sale	2,285,456	2,285,456
Investment securities held-to-maturity	4,237	4,237
Loans and lease finance receivables, net	3,512,771	3,546,141
Accrued interest receivable	27,430	27,430
Liabilities		
Deposits:		
Noninterest-bearing	$1,416,558	$1,416,558
Interest-bearing	2,623,213	2,626,464
Demand note to U.S. Treasury	3,441	3,441
Borrowings	1,665,326	1,721,518
Junior subordinated debentures	115,055	115,735
Accrued interest payable	8,420	8,420

The fair value estimates presented herein are based on pertinent information available to management as of September 30, 2009. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since that date, and therefore, current estimates of fair value may differ significantly from the amounts presented above.

4. BUSINESS SEGMENTS

The Company has identified two principal reportable segments: Business Financial and Commercial Banking Centers and the Treasury Department. The Company s subsidiary bank has 41 Business Financial Centers and 5 Commercial Banking Centers (branches), organized in 6 geographic regions, which are the focal points for customer sales and services. The Company utilizes an internal reporting

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system to measure the performance of various operating segments within the Bank which is the basis for determining the Bank s reportable segments. The Chief Operating Decision Maker (currently our CEO) regularly reviews the financial information of these segments in deciding how to allocate resources and assessing performance. The Bank s Business Financial and Commercial Banking Centers are considered one operating segment as their products and services are similar and are sold to similar types of customers, have similar production and distribution processes, have similar economic characteristics, and have similar reporting and organizational structures. The Treasury Department s primary focus is managing the Bank s investments, liquidity, and interest rate risk. Information related to the Company s remaining operating segments which include construction lending, dairy and livestock lending, SBA lending, leasing, and centralized functions have been aggregated and included in Other. In addition, the Company allocates internal funds transfer pricing to the segments using a methodology that charges users of funds interest expense and credits providers of funds interest income with the net effect of this allocation being recorded in administration.

The following table represents the selected financial information for these two business segments. Accounting principles generally accepted in the United States of America do not have an authoritative body of knowledge regarding the management accounting used in presenting segment financial information. The accounting policies for each of the business units is the same as those policies identified for the consolidated Company and identified in the footnote on the summary of significant accounting policies. The income numbers represent the actual income and expenses of each business unit. In addition, each segment has allocated income and expenses based on management s internal reporting system, which allows management to determine the performance of each of its business units. Loan fees, included in the Business Financial and Commercial Banking Centers category are the actual loan fees paid to the Company by its customers. These fees are eliminated and deferred in the Other category, resulting in deferred loan fees for the consolidated financial statements. All income and expense items not directly associated with the two business segments are grouped in the Other category. Future changes in the Company s management structure or reporting methodologies may result in changes in the measurement of operating segment results.

The following tables present the operating results and other key financial measures for the individual reportable segments for the three and nine months ended September 30, 2009 and 2008:

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	Three Months Ended September 30, 2009				
	Business Financial Centers	**Treasury**	**Other**	**Eliminations**	**Total**
Interest income, including loan fees	$ 38,632	$ 25,388	$ 11,899	$	**$ 75,919**
Credit for funds provided (1)	14,877		6,723	(21,600)	
Total interest income	53,509	25,388	18,622	(21,600)	**75,919**
Interest expense	6,920	13,286	907		**21,113**
Charge for funds used (1)	2,522	8,995	10,083	(21,600)	
Total interest expense	9,442	22,281	10,990	(21,600)	**21,113**
Net interest income	44,067	3,107	7,632		**54,806**
Provision for credit losses			13,000		**13,000**
Net interest income after provision for credit losses	$ 44,067	$ 3,107	($5,368)	$	**$ 41,806**
Non-interest income	5,058	6,667	3,377		**15,102**
Non-interest expense	12,236	383	17,226		**29,845**
Segment pretax profit (loss)	$ 36,889	$ 9,391	($19,217)	$	**$ 27,063**

	Three Months Ended September 30, 2008				
	Business Financial Centers	**Treasury**	**Other**	**Eliminations**	**Total**
Interest income, including loan fees	42,120	$ 30,620	$ 10,767	$	**$ 83,507**
Credit for funds provided (1)	18,306		4,458	(22,764)	
Total interest income	60,426	30,620	15,225	(22,764)	**83,507**
Interest expense	7,214	$ 24,712	2,569		**34,495**
Charge for funds used (1)	19,360	$ 856	2,548	(22,764)	
Total interest expense	26,574	25,568	5,117	(22,764)	**34,495**
Net interest income	33,852	5,052	10,108		**49,012**
Provision for credit losses			4,000		**4,000**
Net interest income after provision for credit losses	$ 33,852	$ 5,052	$ 6,108	$	**$ 45,012**

Non-interest income	5,471	$	1	2,901		**8,373**
Non-interest expense	12,173	$	342	16,542		**29,057**
Segment pretax profit (loss)	**$ 27,150**	**$**	**4,711**	**($7,533)**	$	**$ 24,328**

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	Nine Months Ended September 30, 2009				
	Business Financial Centers	**Treasury**	**Other**	**Eliminations**	**Total**
Interest income, including loan fees	$ 115,711	$ 80,877	$ 34,068	$	**$ 230,656**
Credit for funds provided (1)	37,526		16,457	(53,983)	
Total interest income	153,237	80,877	50,525	(53,983)	**230,656**
Interest expense	21,382	41,400	3,681		**66,463**
Charge for funds used (1)	9,325	20,167	24,491	(53,983)	
Total interest expense	30,707	61,567	28,172	(53,983)	**66,463**
Net interest income	122,530	19,310	22,353		**164,193**
Provision for credit losses			55,000		**55,000**
Net interest income after provision for credit losses	$ 122,530	$ 19,310	($32,647)	$	**$ 109,193**
Non-interest income	14,670	28,215	8,283		**51,168**
Non-interest expense	36,939	1,122	56,160		**94,221**
Segment pretax profit (loss)	$ 100,261	$ 46,403	($80,524)	$	**$ 66,140**
Segment assets as of September 30, 2009	$ 4,241,933	$ 2,724,010	$ 738,934	$ (1,158,612)	**$ 6,546,265**

	Nine Months Ended September 30, 2008				
	Business Financial Centers	**Treasury**	**Other**	**Eliminations**	**Total**
Interest income, including loan fees	$ 125,280	$ 90,545	$ 33,870	$	**$ 249,695**
Credit for funds provided (1)	39,224		6,421	(45,645)	
Total interest income	164,504	90,545	40,291	(45,645)	**249,695**
Interest expense	27,569	71,568	8,934		**108,071**
Charge for funds used (1)	27,519	6,596	11,530	(45,645)	
Total interest expense	55,088	78,164	20,464	(45,645)	**108,071**
Net interest income	109,416	12,381	19,827		**141,624**

Provision for credit losses			8,700			**8,700**
Net interest income after provision for credit losses	$ 109,416	$ 12,381	$ 11,127	$		**$ 132,924**
Non-interest income	16,068	7	9,141			**25,216**
Non-interest expense	36,135	950	50,749			**87,834**
Segment pretax profit (loss)	$ 89,349	$ 11,438	($30,481)	$		**$ 70,306**
Segment assets as of September 30, 2008	$ 3,300,145	$ 2,588,209	$ 609,060	$	(75,628)	**$ 6,421,786**

(1) Credit for funds provided and charge for funds used is eliminated in the consolidated presentation.

5. DERIVATIVE FINANCIAL INSTRUMENTS

The Bank is exposed to certain risks relating to its ongoing business operations. The primary risks managed by using derivative instruments are market risk and interest rate risk. As of September 30, 2009, the Bank entered into 28 interest-rate swap agreements with customers and 28 with a counterparty bank. The swaps are not designated as hedging instruments. The purpose of entering into offsetting derivatives not designated as a hedging instrument is to provide the Bank a variable-rate loan receivable and provide the customer the financial effects of a fixed-rate loan without creating volatility in the bank s earnings.

The structure of the swaps is as follows. The Bank enters into a swap with its customers to allow them to convert variable rate loans to fixed rate loans, and at the same time, the Bank enters into a swap with the counterparty bank to allow the Bank to pass on the interest-rate risk associated with fixed rate loans. The net effect of the transaction allows the Bank to receive interest on the loan from the customer at a variable rate based on LIBOR plus a spread. The changes in the market value of the swaps primarily offset each other and therefore do not have a significant impact on the Company s results of operations.

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As of September 30, 2009, the total notional amount of the Bank s swaps was $171.8 million. The following tables present the location of the asset and liability and the amount of gain recognized as of and for the nine months ended September 30, 2009.

Fair Value of Derivative Instruments

	Asset Derivatives September 30, 2009		**Liability Derivatives** September 30, 2009	
	(amounts in thousands)			
Derivatives Not Designated as Hedging Instruments	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Interest Rate Swaps	Other Assets	$ 5,761	Other Liabilities	$ 5,761
Total Derivatives		$ 5,761		$ 5,761

The Effect of Derivative Instruments on the Consolidated Statement of Earnings for the nine months ended September 30, 200