

FULTON FINANCIAL CORP
Form 10-Q
August 09, 2012

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2012, or

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

For the transition period from _____ to _____

Commission File No. 0-10587

FULTON FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

PENNSYLVANIA

(State or other jurisdiction of incorporation or organization)

23-2195389

(I.R.S. Employer Identification No.)

One Penn Square, P.O. Box 4887, Lancaster, Pennsylvania
(Address of principal executive offices)

17604

(Zip Code)

(717) 291-2411

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Common Stock, \$2.50 Par Value – 200,389,000 shares outstanding as of July 31, 2012.

FULTON FINANCIAL CORPORATION
 FORM 10-Q FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2012
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Item 1. Financial Statements

FULTON FINANCIAL CORPORATION
CONSOLIDATED BALANCE SHEETS

(in thousands, except per-share data)

| | June 30, 2012 (unaudited) | December 31, 2011 |
|--|---------------------------------|----------------------|
| ASSETS | | |
| Cash and due from banks | \$242,811 | \$292,598 |
| Interest-bearing deposits with other banks | 118,468 | 175,336 |
| Loans held for sale | 71,406 | 47,009 |
| Investment securities: | | |
| Held to maturity (estimated fair value of \$6,571 in 2012 and \$6,669 in 2011) | 6,562 | 6,669 |
| Available for sale | 2,864,270 | 2,673,298 |
| Loans, net of unearned income | 11,982,833 | 11,968,970 |
| Less: Allowance for loan losses | (235,737) | (256,471) |
| Net Loans | 11,747,096 | 11,712,499 |
| Premises and equipment | 222,083 | 212,274 |
| Accrued interest receivable | 48,283 | 51,098 |
| Goodwill | 535,980 | 536,005 |
| Intangible assets | 6,642 | 8,204 |
| Other assets | 474,149 | 655,518 |
| Total Assets | \$16,337,750 | \$16,370,508 |
| LIABILITIES | | |
| Deposits: | | |
| Noninterest-bearing | \$2,748,269 | \$2,588,034 |
| Interest-bearing | 9,484,215 | 9,937,705 |
| Total Deposits | 12,232,484 | 12,525,739 |
| Short-term borrowings: | | |
| Federal funds purchased | 566,167 | 253,470 |
| Other short-term borrowings | 365,514 | 343,563 |
| Total Short-Term Borrowings | 931,681 | 597,033 |
| Accrued interest payable | 23,725 | 25,686 |
| Other liabilities | 199,867 | 189,362 |
| Federal Home Loan Bank advances and long-term debt | 908,809 | 1,040,149 |
| Total Liabilities | 14,296,566 | 14,377,969 |
| SHAREHOLDERS' EQUITY | | |
| Common stock, \$2.50 par value, 600 million shares authorized, 216.6 million shares issued in 2012 and 216.2 million shares issued in 2011 | 541,587 | 540,386 |
| Additional paid-in capital | 1,425,037 | 1,423,727 |
| Retained earnings | 313,970 | 264,059 |
| Accumulated other comprehensive income | 482 | 7,955 |
| Treasury stock, at cost, 15.8 million shares in 2012 and 16.0 million shares in 2011 | (239,892) | (243,588) |
| Total Shareholders' Equity | 2,041,184 | 1,992,539 |
| Total Liabilities and Shareholders' Equity | \$16,337,750 | \$16,370,508 |

See Notes to Consolidated Financial Statements

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

(in thousands, except per-share data)

| | Three Months Ended | | Six Months Ended | |
|---|--------------------|------------|------------------|------------|
| | June 30 | | June 30 | |
| | 2012 | 2011 | 2012 | 2011 |
| INTEREST INCOME | | | | |
| Loans, including fees | \$ 141,541 | \$ 149,751 | \$ 285,887 | \$ 299,247 |
| Investment securities: | | | | |
| Taxable | 18,624 | 20,749 | 37,285 | 42,556 |
| Tax-exempt | 2,596 | 3,146 | 5,297 | 6,321 |
| Dividends | 641 | 696 | 1,340 | 1,379 |
| Loans held for sale | 538 | 492 | 969 | 992 |
| Other interest income | 45 | 101 | 98 | 134 |
| Total Interest Income | 163,985 | 174,935 | 330,876 | 350,629 |
| INTEREST EXPENSE | | | | |
| Deposits | 14,743 | 21,775 | 30,993 | 45,061 |
| Short-term borrowings | 411 | 168 | 692 | 422 |
| Long-term debt | 11,301 | 12,347 | 22,966 | 24,938 |
| Total Interest Expense | 26,455 | 34,290 | 54,651 | 70,421 |
| Net Interest Income | 137,530 | 140,645 | 276,225 | 280,208 |
| Provision for credit losses | 25,500 | 36,000 | 53,500 | 74,000 |
| Net Interest Income After Provision for Credit Losses | 112,030 | 104,645 | 222,725 | 206,208 |
| NON-INTEREST INCOME | | | | |
| Service charges on deposit accounts | 15,367 | 14,332 | 30,209 | 27,637 |
| Other service charges and fees | 11,507 | 12,709 | 22,062 | 24,191 |
| Mortgage banking income | 11,143 | 6,049 | 21,193 | 11,512 |
| Investment management and trust services | 9,822 | 9,638 | 19,199 | 18,842 |
| Other | 3,987 | 3,386 | 9,592 | 7,108 |
| Investment securities gains (losses), net: | | | | |
| Other-than-temporary impairment losses | (57) | (71) | (57) | (1,092) |
| Less: Portion of gain recognized in other comprehensive income (before taxes) | — | (322) | — | (592) |
| Net other-than-temporary impairment losses | (57) | (393) | (57) | (1,684) |
| Net gains on sales of investment securities | 1,595 | 58 | 2,846 | 3,634 |
| Investment securities gains (losses), net | 1,538 | (335) | 2,789 | 1,950 |
| Total Non-Interest Income | 53,364 | 45,779 | 105,044 | 91,240 |
| NON-INTEREST EXPENSES | | | | |
| Salaries and employee benefits | 60,091 | 56,070 | 120,451 | 110,378 |
| Net occupancy expense | 11,205 | 10,874 | 22,140 | 22,240 |
| Data processing | 3,759 | 3,214 | 7,447 | 6,586 |
| Equipment expense | 3,185 | 3,377 | 6,554 | 6,509 |
| FDIC insurance expense | 3,002 | 3,264 | 6,023 | 8,018 |
| Professional fees | 2,984 | 3,102 | 5,566 | 5,951 |
| Other real estate owned and repossession expense | 2,823 | 982 | 5,751 | 2,253 |
| Marketing | 2,583 | 1,863 | 5,055 | 4,699 |
| Software | 2,272 | 1,973 | 4,447 | 4,004 |
| Operating risk loss | 2,055 | (8) | 5,423 | (470) |
| Intangible amortization | 761 | 1,172 | 1,562 | 2,350 |

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| | | | | |
|-----------------------------|----------|----------|----------|----------|
| Other | 17,423 | 15,002 | 32,435 | 29,231 |
| Total Non-Interest Expenses | 112,143 | 100,885 | 222,854 | 201,749 |
| Income Before Income Taxes | 53,251 | 49,539 | 104,915 | 95,699 |
| Income taxes | 13,360 | 13,154 | 26,892 | 25,529 |
| Net Income | \$39,891 | \$36,385 | \$78,023 | \$70,170 |

PER SHARE:

| | | | | |
|----------------------|--------|--------|--------|--------|
| Net Income (Basic) | \$0.20 | \$0.18 | \$0.39 | \$0.35 |
| Net Income (Diluted) | 0.20 | 0.18 | 0.39 | 0.35 |
| Cash Dividends | 0.07 | 0.05 | 0.14 | 0.09 |

See Notes to Consolidated Financial Statements

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

(in thousands)

| | Three Months Ended June 30 | | Six Months Ended June 30 | |
|--|-------------------------------|----------|-----------------------------|----------|
| | 2012 | 2011 | 2012 | 2011 |
| Net Income | \$39,891 | \$36,385 | \$78,023 | \$70,170 |
| Other Comprehensive Income (Loss), net of tax: | | | | |
| Unrealized (loss) gain on securities | (10,704) | 13,451 | (6,120) | 17,019 |
| Reclassification adjustment for securities (gains) losses included in net income | (999) | 218 | (1,812) | (1,267) |
| Non-credit related unrealized gain (loss) on other-than-temporarily impaired debt securities | (172) | 480 | (37) | 729 |
| Unrealized gain on derivative financial instruments | 34 | 34 | 68 | 68 |
| Amortization (accretion) of net unrecognized pension and postretirement items | 214 | (12) | 428 | (24) |
| Other Comprehensive Income (Loss) | (11,627) | 14,171 | (7,473) | 16,525 |
| Total Comprehensive Income | \$28,264 | \$50,556 | \$70,550 | \$86,695 |

See Notes to Consolidated Financial Statements

FULTON FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (UNAUDITED)
SIX MONTHS ENDED JUNE 30, 2012 AND 2011

(in thousands, except per-share data)

| | Common Stock | | Additional Paid-in Capital | Retained Earnings | Accumulated Other Comprehensive Income | Treasury Stock | Total |
|--|-----------------------|-----------|----------------------------------|----------------------|---|-------------------|-------------|
| | Shares Outstanding | Amount | | | | | |
| Balance at December 31, 2011 | 200,164 | \$540,386 | \$1,423,727 | \$264,059 | \$ 7,955 | \$(243,588) | \$1,992,539 |
| Net income | | | | 78,023 | | | 78,023 |
| Other comprehensive loss | | | | | (7,473) | | (7,473) |
| Stock issued, including related tax benefits | 716 | 1,201 | (1,740) | | | 3,696 | 3,157 |
| Stock-based compensation awards | | | 3,050 | | | | 3,050 |
| Common stock cash dividends - \$0.14 per share | | | | (28,112) | | | (28,112) |
| Balance at June 30, 2012 | 200,880 | \$541,587 | \$1,425,037 | \$313,970 | \$ 482 | \$(239,892) | \$2,041,184 |
| Balance at December 31, 2010 | 199,050 | \$538,492 | \$1,420,127 | \$158,453 | \$ 12,495 | \$(249,178) | \$1,880,389 |
| Net income | | | | 70,170 | | | 70,170 |
| Other comprehensive income | | | | | 16,525 | | 16,525 |
| Stock issued, including related tax benefits | 320 | 431 | 398 | | | 2,247 | 3,076 |
| Stock-based compensation awards | | | 1,101 | | | | 1,101 |
| Common stock cash dividends - \$0.09 per share | | | | (17,952) | | | (17,952) |
| Balance at June 30, 2011 | 199,370 | \$538,923 | \$1,421,626 | \$210,671 | \$ 29,020 | \$(246,931) | \$1,953,309 |

See Notes to Consolidated
Financial Statements

FULTON FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(in thousands)

| | Six Months Ended | |
|---|------------------|-----------|
| | June 30 | |
| | 2012 | 2011 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net Income | \$78,023 | \$70,170 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for credit losses | 53,500 | 74,000 |
| Depreciation and amortization of premises and equipment | 10,845 | 10,462 |
| Net amortization of investment securities premiums | 5,251 | 1,999 |
| Investment securities gains, net | (2,789) | (1,950) |
| Net (increase) decrease in loans held for sale | (24,397) | 36,807 |
| Amortization of intangible assets | 1,562 | 2,350 |
| Stock-based compensation | 3,050 | 1,101 |
| Excess tax benefits from stock-based compensation | (14) | — |
| Decrease in accrued interest receivable | 2,815 | 2,454 |
| Decrease in other assets | 3,829 | 22,955 |
| Decrease in accrued interest payable | (1,961) | (3,889) |
| Increase (decrease) in other liabilities | 5,910 | (11,566) |
| Total adjustments | 57,601 | 134,723 |
| Net cash provided by operating activities | 135,624 | 204,893 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Proceeds from sales of securities available for sale | 210,804 | 416,480 |
| Proceeds from maturities of securities held to maturity | 121 | 160 |
| Proceeds from maturities of securities available for sale | 371,176 | 279,841 |
| Purchase of securities held to maturity | (14) | (14) |
| Purchase of securities available for sale | (602,642) | (356,323) |
| Decrease (increase) in short-term investments | 56,868 | (91,670) |
| Net increase in loans | (88,224) | (49) |
| Net purchases of premises and equipment | (20,654) | (9,623) |
| Net cash (used in) provided by investing activities | (72,565) | 238,802 |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Net (decrease) increase in demand and savings deposits | (13,950) | 229,071 |
| Net decrease in time deposits | (279,305) | (354,757) |
| Increase (decrease) in short-term borrowings | 334,648 | (127,496) |
| Repayments of long-term debt | (131,340) | (93,913) |
| Net proceeds from issuance of stock | 3,143 | 3,076 |
| Excess tax benefits from stock-based compensation | 14 | — |
| Dividends paid | (26,056) | (13,939) |
| Net cash used in financing activities | (112,846) | (357,958) |
| Net (Decrease) Increase in Cash and Due From Banks | (49,787) | 85,737 |
| Cash and Due From Banks at Beginning of Period | 292,598 | 198,954 |
| Cash and Due From Banks at End of Period | \$242,811 | \$284,691 |

Supplemental Disclosures of Cash Flow Information:

Cash paid during the period for:

| | | |
|--|----------|----------|
| Interest | \$56,612 | \$74,310 |
| Income taxes | 22,646 | 7,469 |
| See Notes to Consolidated Financial Statements | | |

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FULTON FINANCIAL CORPORATION
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE A – Basis of Presentation

The accompanying unaudited consolidated financial statements of Fulton Financial Corporation (the Corporation) have been prepared in conformity with U.S. generally accepted accounting principles (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and notes required by U.S. GAAP for complete financial statements. The preparation of financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the amounts of assets and liabilities as of the date of the financial statements as well as revenues and expenses during the period. Actual results could differ from those estimates. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and six-month periods ended June 30, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012. The Corporation evaluates subsequent events through the date of filing with the Securities and Exchange Commission (SEC).

NOTE B – Net Income Per Share

Basic net income per common share is calculated as net income divided by the weighted average number of common shares outstanding.

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

A reconciliation of weighted average common shares outstanding used to calculate basic net income per common share and diluted net income per common share follows for the three and six months ended June 30:

| | Three Months Ended | | Six Months Ended | |
|---|--------------------|---------|------------------|---------|
| | June 30 | | June 30 | |
| | 2012 | 2011 | 2012 | 2011 |
| | (in thousands) | | | |
| Weighted average shares outstanding (basic) | 199,671 | 198,772 | 199,581 | 198,686 |
| Effect of dilutive securities | 1,135 | 755 | 994 | 721 |
| Weighted average shares outstanding (diluted) | 200,806 | 199,527 | 200,575 | 199,407 |

For the three and six months ended June 30, 2012, 5.2 million stock options were excluded from the diluted net income per share computation as their effect would have been anti-dilutive. For the three and six months ended June 30, 2011, 4.6 million stock options were excluded from the diluted net income per share computation as their effect would have been anti-dilutive.

NOTE C – Accumulated Other Comprehensive Income

The following table presents changes in other comprehensive income for the three and six months ended June 30, 2012 and 2011:

| | Before-Tax Amount (in thousands) | Tax Effect | Net of Tax Amount |
|--|--|-------------------|----------------------|
| Three Months Ended June 30, 2012 | | | |
| Unrealized gain (loss) on securities | \$(16,468) | \$5,764 | \$(10,704) |
| Reclassification adjustment for securities (gains) losses included in net income | (1,537) | 538 | (999) |
| Non-credit related unrealized gain (loss) on other-than-temporarily impaired debt securities | (264) | 92 | (172) |
| Unrealized gain on derivative financial instruments | 52 | (18) | 34 |
| Amortization (accretion) of net unrecognized pension and postretirement items | 329 | (115) | 214 |
| Total Other Comprehensive Income (Loss) | \$(17,888) | \$6,261 | \$(11,627) |
| Three Months Ended June 30, 2011 | | | |
| Unrealized gain (loss) on securities | \$20,694 | \$(7,243) | \$13,451 |
| Reclassification adjustment for securities (gains) losses included in net income | 335 | (117) | 218 |
| Non-credit related unrealized gain (loss) on other-than-temporarily impaired debt securities | 738 | (258) | 480 |
| Unrealized gain on derivative financial instruments | 52 | (18) | 34 |
| Amortization (accretion) of net unrecognized pension and postretirement items | (19) | 7 | (12) |
| Total Other Comprehensive Income (Loss) | \$21,800 | \$(7,629) | \$14,171 |
| Six Months Ended June 30, 2012 | | | |
| Unrealized gain (loss) on securities | \$(9,415) | \$3,295 | \$(6,120) |
| Reclassification adjustment for securities (gains) losses included in net income | (2,788) | 976 | (1,812) |
| Non-credit related unrealized gain (loss) on other-than-temporarily impaired debt securities | (57) | 20 | (37) |
| Unrealized gain on derivative financial instruments | 104 | (36) | 68 |
| Amortization (accretion) of net unrecognized pension and postretirement items | 659 | (231) | 428 |
| Total Other Comprehensive Income (Loss) | \$(11,497) | \$4,024 | \$(7,473) |
| Six Months Ended June 30, 2011 | | | |
| Unrealized gain (loss) on securities | \$26,183 | \$(9,164) | \$17,019 |
| Reclassification adjustment for securities (gains) losses included in net income | (1,949) | 682 | (1,267) |
| Non-credit related unrealized gain (loss) on other-than-temporarily impaired debt securities | 1,121 | (392) | 729 |
| Unrealized gain on derivative financial instruments | 104 | (36) | 68 |
| Amortization (accretion) of net unrecognized pension and postretirement items | (37) | 13 | (24) |
| Total Other Comprehensive Income (Loss) | \$25,422 | \$(8,897) | \$16,525 |

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The following table presents changes in each component of accumulated other comprehensive income, net of tax, for the three and six months ended June 30, 2012 and 2011:

| | Unrealized Gains on Investment Securities Not Other-Than-Temporarily Impaired (in thousands) | Unrealized Non-Credit Losses on Other-Than-Temporarily Impaired Debt Securities | Unrecognized Pension and Postretirement Plan Items | Unrealized Effective Portions of Losses on Forward-Starting Interest Rate Swaps | Total |
|--|---|---|---|---|-----------|
| Three months ended June 30, 2012 | | | | | |
| Balance at March 31, 2012 | \$30,825 | \$ (876) | \$ (14,920) | \$ (2,920) | \$12,109 |
| Current-period other comprehensive income (loss) | (11,703) | (172) | 214 | 34 | (11,627) |
| Balance at June 30, 2012 | \$19,122 | \$ (1,048) | \$ (14,706) | \$ (2,886) | \$482 |
| Three months ended June 30, 2011 | | | | | |
| Balance at March 31, 2011 | \$23,791 | \$ (1,460) | \$ (4,426) | \$ (3,056) | \$14,849 |
| Current-period other comprehensive income (loss) | 13,436 | 713 | (12) | 34 | 14,171 |
| Balance at June 30, 2011 | \$37,227 | \$ (747) | \$ (4,438) | \$ (3,022) | \$29,020 |
| Six months ended June 30, 2012 | | | | | |
| Balance at December 31, 2011 | \$27,054 | \$ (1,011) | \$ (15,134) | \$ (2,954) | \$7,955 |
| Current-period other comprehensive income (loss) | (7,932) | (37) | 428 | 68 | (7,473) |
| Balance at June 30, 2012 | \$19,122 | \$ (1,048) | \$ (14,706) | \$ (2,886) | \$482 |
| Six months ended June 30, 2011 | | | | | |
| Balance at December 31, 2010 | \$22,354 | \$ (2,355) | \$ (4,414) | \$ (3,090) | \$12,495 |
| Current-period other comprehensive income (loss) | 14,873 | 1,608 | (24) | 68 | 16,525 |
| Balance at June 30, 2011 | \$37,227 | \$ (747) | \$ (4,438) | \$ (3,022) | \$29,020 |

NOTE D – Investment Securities

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

| Held to Maturity at June 30, 2012 | Amortized Cost (in thousands) | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|---|-------------------------------------|------------------------------|-------------------------------|----------------------------|
| U.S. Government sponsored agency securities | \$6,001 | \$— | \$(27) | \$5,974 |
| State and municipal securities | 179 | — | — | 179 |
| Mortgage-backed securities | 382 | 36 | — | 418 |
| | \$6,562 | \$36 | \$(27) | \$6,571 |
| Available for Sale at June 30, 2012 | | | | |
| Equity securities | \$104,086 | \$2,738 | \$(1,413) | \$105,411 |
| U.S. Government securities | 327 | — | — | 327 |

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| | | | | |
|---|-------------|----------|-----------|---------------|
| U.S. Government sponsored agency securities | 3,939 | 54 | (1 |) 3,992 |
| State and municipal securities | 289,364 | 14,153 | (37 |) 303,480 |
| Corporate debt securities | 135,886 | 5,991 | (11,502 |) 130,375 |
| Collateralized mortgage obligations | 965,499 | 16,441 | (283 |) 981,657 |
| Mortgage-backed securities | 1,098,949 | 36,797 | — | 1,135,746 |
| Auction rate securities | 238,408 | — | (35,126 |) 203,282 |
| | \$2,836,458 | \$76,174 | \$(48,362 |) \$2,864,270 |

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| Held to Maturity at December 31, 2011 | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|---|-------------------|------------------------------|-------------------------------|----------------------------|
| | (in thousands) | | | |
| U.S. Government sponsored agency securities | \$5,987 | \$— | \$(14 |) \$5,973 |
| State and municipal securities | 179 | — | — | 179 |
| Mortgage-backed securities | 503 | 44 | — | 547 |
| | \$6,669 | \$44 | \$(14 |) \$6,699 |
| Available for Sale at December 31, 2011 | | | | |
| Equity securities | \$117,486 | \$2,383 | \$(2,819 |) \$117,050 |
| U.S. Government securities | 334 | — | — | 334 |
| U.S. Government sponsored agency securities | 3,987 | 87 | (1 |) 4,073 |
| State and municipal securities | 306,186 | 15,832 | — | 322,018 |
| Corporate debt securities | 132,855 | 4,979 | (14,528 |) 123,306 |
| Collateralized mortgage obligations | 982,851 | 19,186 | (828 |) 1,001,209 |
| Mortgage-backed securities | 848,675 | 31,837 | (415 |) 880,097 |
| Auction rate securities | 240,852 | 120 | (15,761 |) 225,211 |
| | \$2,633,226 | \$74,424 | \$(34,352 |) \$2,673,298 |

Securities carried at \$1.8 billion as of June 30, 2012 and December 31, 2011 were pledged as collateral to secure public and trust deposits and customer repurchase agreements. Available for sale equity securities include restricted investment securities issued by the Federal Home Loan Bank (FHLB) and the Federal Reserve Bank totaling \$76.1 million and \$82.5 million as of June 30, 2012 and December 31, 2011, respectively.

The amortized cost and estimated fair values of debt securities as of June 30, 2012, by contractual maturity, are shown in the following table. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | Held to Maturity | | Available for Sale | |
|-------------------------------------|-------------------|-------------------------|--------------------|-------------------------|
| | Amortized Cost | Estimated Fair Value | Amortized Cost | Estimated Fair Value |
| | (in thousands) | | | |
| Due in one year or less | \$179 | \$179 | \$53,656 | \$54,119 |
| Due from one year to five years | 6,001 | 5,974 | 61,264 | 64,298 |
| Due from five years to ten years | — | — | 142,646 | 152,850 |
| Due after ten years | — | — | 410,358 | 370,189 |
| | 6,180 | 6,153 | 667,924 | 641,456 |
| Collateralized mortgage obligations | — | — | 965,499 | 981,657 |
| Mortgage-backed securities | 382 | 418 | 1,098,949 | 1,135,746 |
| | \$6,562 | \$6,571 | \$2,732,372 | \$2,758,859 |

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

| | Gross Realized Gains | Gross Realized Losses | Other-than- temporary Impairment Losses | Net Gains (Losses) |
|-----------------------------------|----------------------------|-----------------------------|--|-----------------------|
| | (in thousands) | | | |
| Three months ended June 30, 2012 | | | | |
| Equity securities | \$1,517 | \$— | \$(57) |) \$1,460 |
| Debt securities | 78 | — | — |) 78 |
| Total | \$1,595 | \$— | \$(57) |) \$1,538 |
| Three months ended June 30, 2011: | | | | |
| Equity securities | \$43 | \$— | \$(34) |) \$9 |
| Debt securities | 16 | (1) |) (359) |) (344) |
| Total | \$59 | \$(1) |) \$(393) |) \$(335) |
| Six months ended June 30, 2012 | | | | |
| Equity securities | \$2,603 | \$— | \$(57) |) \$2,546 |
| Debt securities | 243 | — | — |) 243 |
| Total | \$2,846 | \$— | \$(57) |) \$2,789 |
| Six months ended June 30, 2011: | | | | |
| Equity securities | \$48 | \$— | \$(331) |) \$(283) |
| Debt securities | 3,605 | (19) |) (1,353) |) 2,233 |
| Total | \$3,653 | \$(19) |) \$(1,684) |) \$1,950 |

The following table presents a summary of the cumulative credit related other-than-temporary impairment charges, recognized as components of earnings, for debt securities still held by the Corporation at June 30, 2012 and 2011:

| | Three Months ended June 30 | | Six Months ended June 30 | |
|---|-------------------------------|------------|-----------------------------|------------|
| | 2012 | 2011 | 2012 | 2011 |
| | (in thousands) | | | |
| Balance of cumulative credit losses on debt securities, beginning of period | \$(22,692) | \$(28,517) | \$(22,781) | \$(27,560) |
| Additions for credit losses recorded which were not previously recognized as components of earnings | — | (359) | — | (1,353) |
| Reductions for increases in cash flows expected to be collected that are recognized over the remaining life of the security | — | — | 89 | 37 |
| Balance of cumulative credit losses on debt securities, end of period | \$(22,692) | \$(28,876) | \$(22,692) | \$(28,876) |

The following table presents the gross unrealized losses and estimated fair values of investments, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at June 30, 2012:

| | Less than 12 months | | 12 months or longer | | Total | |
|---|----------------------|-------------------|----------------------|-------------------|----------------------|-------------------|
| | Estimated Fair Value | Unrealized Losses | Estimated Fair Value | Unrealized Losses | Estimated Fair Value | Unrealized Losses |
| | (in thousands) | | | | | |
| U.S. Government sponsored agency securities | \$ 112 | \$(1) | \$5,344 | \$(27) | \$5,456 | \$(28) |
| State and municipal securities | 8,356 | (37) | — | — | 8,356 | (37) |
| Corporate debt securities | 6,942 | (1,678) | 37,562 | (9,824) | 44,504 | (11,502) |
| Collateralized mortgage obligations | 95,032 | (283) | — | — | 95,032 | (283) |
| Auction rate securities | 21,868 | (2,064) | 181,414 | (33,062) | 203,282 | (35,126) |
| Total debt securities | 132,310 | (4,063) | 224,320 | (42,913) | 356,630 | (46,976) |
| Equity securities | 6,221 | (613) | 4,287 | (800) | 10,508 | (1,413) |
| | \$138,531 | \$(4,676) | \$228,607 | \$(43,713) | \$367,138 | \$(48,389) |

For its investments in equity securities, particularly its investments in stocks of financial institutions, management evaluates the near-term prospects of the issuers in relation to the severity and duration of the impairment. Based on that evaluation and the Corporation's ability and intent to hold those investments for a reasonable period of time sufficient for a recovery of fair value, the Corporation does not consider those investments with unrealized holding losses as of June 30, 2012 to be other-than-temporarily impaired. As of June 30, 2012, the financial institutions stock portfolio had a cost basis of \$21.3 million and a fair value of \$22.6 million.

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

As of June 30, 2012, approximately \$155 million, or 76%, of the ARCs were rated above investment grade, with approximately \$24 million, or 12%, AAA rated and \$94 million, or 46%, AA rated. Approximately \$48 million, or 24%, of ARCs were either not rated or rated below investment grade by at least one ratings agency. Of this amount, approximately \$30 million, or 61%, of the student loans underlying these ARCs have principal payments which are guaranteed by the federal government. In total, approximately \$184 million, or 90%, of the student loans underlying the ARCs have principal payments which are guaranteed by the federal government. As of June 30, 2012, all ARCs were current and making scheduled interest payments. Based on management's evaluations, ARCs with a fair value of \$203.3 million were not subject to any other-than-temporary impairment charges as of June 30, 2012. The Corporation does not have the intent to sell and does not believe it will more likely than not be required to sell any of these securities prior to a recovery of their fair value to amortized cost, which may be at maturity.

The Corporation's collateralized mortgage obligations and mortgage-backed securities have contractual terms that generally do not permit the issuer to settle the securities at a price less than the amortized cost of the investment. Because the decline in market value of these securities is attributable to changes in interest rates and not credit quality, and because the Corporation does not have the intent to sell and does not believe it will more likely than not be required to sell any of these securities prior to a recovery of their fair value to amortized cost, the Corporation does not consider these investments to be other-than-temporarily impaired as of June 30, 2012.

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

| | June 30, 2012 | | December 31, 2011 | |
|--|----------------|----------------------|-------------------|----------------------|
| | Amortized cost | Estimated fair value | Amortized cost | Estimated fair value |
| | (in thousands) | | | |
| Single-issuer trust preferred securities | \$84,321 | \$76,823 | \$83,899 | \$74,365 |
| Subordinated debt | 43,233 | 46,012 | 40,184 | 41,296 |
| Pooled trust preferred securities | 5,810 | 5,018 | 6,236 | 5,109 |
| Corporate debt securities issued by financial institutions | 133,364 | 127,853 | 130,319 | 120,770 |
| Other corporate debt securities | 2,522 | 2,522 | 2,536 | 2,536 |
| Available for sale corporate debt securities | \$135,886 | \$130,375 | \$132,855 | \$123,306 |

The Corporation's investments in single-issuer trust preferred securities had an unrealized loss of \$7.5 million at June 30, 2012. The Corporation did not record any other-than-temporary impairment charges for single-issuer trust preferred securities during the six months ended June 30, 2012 or 2011. The Corporation held 12 single-issuer trust preferred securities that were rated below investment grade by at least one ratings agency, with an amortized cost of \$41.7 million and an estimated fair value of \$40.7 million at June 30, 2012. The majority of the single-issuer trust preferred securities rated below investment grade were rated BB or Ba. Single-issuer trust preferred securities with an amortized cost of \$8.0 million and an estimated fair value of \$6.5 million at June 30, 2012 were not rated by any ratings agency.

The Corporation held ten pooled trust preferred securities as of June 30, 2012. Nine of these securities, with an amortized cost of \$5.6 million and an estimated fair value of \$4.8 million, were rated below investment grade by at least one ratings agency, with ratings ranging from C to Ca. For each of the nine pooled trust preferred securities rated below investment grade, the class of securities held by the Corporation was below the most senior tranche, with the Corporation's interests being subordinate to other investors in the pool. The Corporation determines the fair value of pooled trust preferred securities based on quotes provided by third-party brokers.

The amortized cost of pooled trust preferred securities is the purchase price of the securities, net of cumulative credit related other-than-temporary impairment charges, determined using an expected cash flows model. The most significant input to the expected cash flows model is the expected payment deferral rate for each pooled trust preferred security. The Corporation evaluates the financial metrics, such as capital ratios and non-performing asset ratios, of the individual financial institution issuers that comprise each pooled trust preferred security to estimate its expected deferral rate. The actual weighted average cumulative defaults and deferrals as a percentage of original collateral were approximately 40.4% as of June 30, 2012.

Based on management's evaluations, corporate debt securities with a fair value of \$130.4 million were not subject to any other-than-temporary impairment charges as of June 30, 2012. The Corporation does not have the intent to sell and does not believe it will more likely than not be required to sell any of these securities prior to a recovery of their fair value to amortized cost, which may be maturity.

NOTE E – Loans and Allowance for Credit Losses

Loans, Net of Unearned Income

Loans, net of unearned income are summarized as follows:

| | June 30, 2012 | December 31, 2011 |
|---|----------------|----------------------|
| | (in thousands) | |
| Real-estate - commercial mortgage | \$4,653,097 | \$4,602,596 |
| Commercial - industrial, financial and agricultural | 3,538,188 | 3,639,368 |
| Real-estate - home equity | 1,599,468 | 1,624,562 |
| Real-estate - residential mortgage | 1,183,613 | 1,097,192 |
| Real-estate - construction | 619,060 | 615,445 |
| Consumer | 308,469 | 318,101 |
| Leasing and other | 69,872 | 63,254 |
| Overdrafts | 18,332 | 15,446 |
| Loans, gross of unearned income | 11,990,099 | 11,975,964 |
| Unearned income | (7,266 |) (6,994 |
| Loans, net of unearned income | \$11,982,833 | \$11,968,970 |
| Allowance for Credit Losses | | |

The allowance for credit losses consists of the allowance for loan losses and the reserve for unfunded lending commitments. The allowance for loan losses represents management's estimate of losses inherent in the loan portfolio as of the balance sheet date and is recorded as a reduction to loans. The reserve for unfunded lending commitments represents management's estimate of losses inherent in its unfunded loan commitments and is recorded in other liabilities on the consolidated balance sheet. The allowance for credit losses is increased by charges to expense, through the provision for credit losses, and decreased by charge-offs, net of recoveries.

The Corporation's established methodology for evaluating the adequacy of the allowance for loan losses considers both components of the allowance: (1) specific allowances allocated to loans evaluated for impairment under the Financial Accounting Standards Board's (FASB) Accounting Standards Codification (ASC) Section 310-10-35, and (2) allowances calculated for pools of loans measured for impairment under FASB ASC Subtopic 450-20.

The development of the Corporation's allowance for credit losses is based first on a segmentation of its loan portfolio by general loan type, or "portfolio segments," as presented in the table under the heading, "Loans, Net of Unearned Income," above. Certain portfolio segments are further disaggregated and evaluated collectively for impairment based on "class segments," which are largely based on the type of collateral underlying each loan. For commercial loans, class segments include loans secured by collateral and unsecured loans. Construction loan class segments include loans secured by commercial real estate and loans secured by residential real estate. Consumer loan class segments are based on collateral types and include direct consumer installment loans and indirect automobile loans.

The following table presents the components of the allowance for credit losses:

| | June 30, 2012 (in thousands) | December 31, 2011 |
|--|------------------------------------|----------------------|
| Allowance for loan losses | \$235,737 | \$256,471 |
| Reserve for unfunded lending commitments | 1,579 | 1,706 |
| Allowance for credit losses | \$237,316 | \$258,177 |

The following table presents the activity in the allowance for credit losses for the three and six months ended June 30:

| | Three months ended | | Six months ended | |
|--|--------------------|-----------|------------------|-----------|
| | June 30 2012 | 2011 | June 30 2012 | 2011 |
| | (in thousands) | | | |
| Balance at beginning of period | \$258,137 | \$271,156 | \$258,177 | \$275,498 |
| Loans charged off | (50,540) | (40,675) | (80,799) | (86,204) |
| Recoveries of loans previously charged off | 4,219 | 2,152 | 6,438 | 5,339 |
| Net loans charged off | (46,321) | (38,523) | (74,361) | (80,865) |
| Provision for credit losses | 25,500 | 36,000 | 53,500 | 74,000 |
| Balance at end of period | \$237,316 | \$268,633 | \$237,316 | \$268,633 |

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The following table presents the activity in the allowance for loan losses by portfolio segment for the three and six months ended June 30, 2012 and 2011:

| | Real Estate Commercial Mortgage | Commercial Industrial, Financial and Agricultural | Real Estate Home Equity | Real Estate Residential Mortgage | Real Estate - Construction | Consumer | Leasing and other and overdrafts | Unallocated | Total |
|--|---------------------------------|---|-------------------------|----------------------------------|----------------------------|----------|----------------------------------|-------------|-----------|
| (in thousands) | | | | | | | | | |
| Three months ended June 30, 2012 | | | | | | | | | |
| Balance at March 31, 2012 | \$81,652 | \$79,756 | \$13,083 | \$24,851 | \$31,186 | \$1,643 | \$3,274 | \$21,051 | \$256,496 |
| Loans charged off | (23,699) | (13,017) | (2,789) | (1,492) | (8,442) | (471) | (630) | — | (50,540) |
| Recoveries of loans previously charged off | 1,153 | 717 | 278 | 71 | 1,539 | 281 | 180 | — | 4,219 |
| Net loans charged off | (22,546) | (12,300) | (2,511) | (1,421) | (6,903) | (190) | (450) | — | (46,321) |
| Provision for loan losses (1) | 10,763 | 4,475 | 3,872 | 3,281 | 1,276 | 363 | 419 | 1,113 | 25,562 |
| Balance at June 30, 2012 | \$69,869 | \$71,931 | \$14,444 | \$26,711 | \$25,559 | \$1,816 | \$3,243 | \$22,164 | \$235,737 |
| Three months ended June 30, 2011 | | | | | | | | | |
| Balance at March 31, 2011 | 48,558 | 100,180 | 5,656 | 19,575 | 55,491 | 4,736 | 2,576 | 33,500 | 270,272 |
| Loans charged off | (7,074) | (15,406) | (1,650) | (7,707) | (7,468) | (681) | (689) | — | (40,675) |
| Recoveries of loans previously charged off | 191 | 1,003 | 2 | 190 | 79 | 433 | 254 | — | 2,152 |
| Net loans charged off | (6,883) | (14,403) | (1,648) | (7,517) | (7,389) | (248) | (435) | — | (38,523) |
| Provision for loan losses | 9,040 | 10,224 | 1,862 | 11,958 | 7,239 | 343 | 590 | (6,322) | 34,934 |
| Impact of change in allowance methodology | 22,883 | (13,388) | 3,690 | 7,896 | (24,771) | (3,076) | (944) | 7,710 | — |
| Provision for loan losses, including impact of change in allowance methodology (1) | 31,923 | (3,164) | 5,552 | 19,854 | (17,532) | (2,733) | (354) | 1,388 | 34,934 |
| Balance at June 30, 2011 | 73,598 | 82,613 | 9,560 | 31,912 | 30,570 | 1,755 | 1,787 | 34,888 | 266,683 |

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| | | | | | | | | | |
|--|-----------|-----------|----------|-----------|-----------|----------|----------|-----------|-----------|
| Six months ended June 30, 2012 | | | | | | | | | |
| Balance at December 31, 2011 | \$85,112 | \$74,896 | \$12,841 | \$22,986 | \$30,066 | \$2,083 | \$2,397 | \$26,090 | \$256,471 |
| Loans charged off | (35,590) | (18,686) | (4,995) | (2,339) | (17,013) | (1,105) | (1,071) | — | (80,799) |
| Recoveries of loans previously charged off | 1,969 | 1,353 | 298 | 144 | 1,603 | 631 | 440 | — | 6,438 |
| Net loans charged off | (33,621) | (17,333) | (4,697) | (2,195) | (15,410) | (474) | (631) | — | (74,361) |
| Provision for loan losses (1) | 18,378 | 14,368 | 6,300 | 5,920 | 10,903 | 207 | 1,477 | (3,926) | 53,627 |
| Balance at June 30, 2012 | \$69,869 | \$71,931 | \$14,444 | \$26,711 | \$25,559 | \$1,816 | \$3,243 | \$22,164 | \$235,737 |
| Six months ended June 30, 2011 | | | | | | | | | |
| Balance at December 31, 2010 | \$40,831 | \$101,436 | \$6,454 | \$17,425 | \$58,117 | \$4,669 | \$3,840 | \$41,499 | \$274,271 |
| Loans charged off | (17,121) | (28,742) | (3,118) | (12,703) | (21,362) | (1,972) | (1,186) | — | (86,204) |
| Recoveries of loans previously charged off | 1,726 | 1,394 | 3 | 234 | 642 | 742 | 598 | — | 5,339 |
| Net loans charged off | (15,395) | (27,348) | (3,115) | (12,469) | (20,720) | (1,230) | (588) | — | (80,865) |
| Provision for loan losses | 25,279 | 21,913 | 2,531 | 19,060 | 17,944 | 1,392 | (521) | (14,321) | 73,277 |
| Impact of change in allowance methodology | 22,883 | (13,388) | 3,690 | 7,896 | (24,771) | (3,076) | (944) | 7,710 | — |
| Provision for loan losses, including impact of change in allowance methodology (1) | 48,162 | 8,525 | 6,221 | 26,956 | (6,827) | (1,684) | (1,465) | (6,611) | 73,277 |
| Balance at June 30, 2011 | \$73,598 | \$82,613 | \$9,560 | \$31,912 | \$30,570 | \$1,755 | \$1,787 | \$34,888 | \$266,683 |

(1) Provision for loan losses is gross of a \$62,000 and \$127,000 decrease, respectively, in provision applied to unfunded commitments for the three and six months ended June 30, 2012. The total provision for credit losses, comprised of allocations for both funded and unfunded loans, was \$25.5 million and \$53.5 million for the three and six months ended June 30, 2012, respectively. Provision for loan losses is net of a \$1.1 million and \$723,000 increase, respectively, in provision applied to unfunded commitments for the three and six months ended June 30, 2011. The total provision for credit losses, comprised of allocations for both funded and unfunded loans, was \$36.0

million and \$74.0 million for the three and six months ended June 30, 2011, respectively.

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The following table present loans, net of unearned income and their related allowance for loan losses, by portfolio segment, as of June 30, 2012 and 2011:

| | Real Estate - Commercial Mortgage | Commercial Industrial, Financial and Agricultural | Real Estate - Home Equity | Real Estate - Residential Mortgage | Real Estate - Construction | Consumer | Leasing and other and overdrafts | Unallocated (1) | Total |
|--|--|--|------------------------------------|---|----------------------------------|-----------|--|--------------------|--------------|
| (in thousands) | | | | | | | | | |
| Allowance for loan losses at June 30, 2012 | | | | | | | | | |
| Measured for impairment under FASB ASC Subtopic 450-20 | \$47,532 | \$46,650 | \$9,619 | \$7,781 | \$15,359 | \$1,811 | \$3,052 | \$22,164 | \$153,968 |
| Evaluated for impairment under FASB ASC Section 310-10-35 | 22,337 | 25,281 | 4,825 | 18,930 | 10,200 | 5 | 191 | N/A | 81,769 |
| | \$69,869 | \$71,931 | \$14,444 | \$26,711 | \$25,559 | \$1,816 | \$3,243 | \$22,164 | \$235,737 |
| Loans, net of unearned income at June 30, 2012 | | | | | | | | | |
| Measured for impairment under FASB ASC Subtopic 450-20 | \$4,541,364 | \$3,471,260 | \$1,591,117 | \$1,138,420 | \$566,163 | \$308,462 | \$80,643 | N/A | \$11,697,429 |
| Evaluated for impairment under FASB ASC Section 310-10-35 | 111,733 | 66,928 | 8,351 | 45,193 | 52,897 | 7 | 295 | N/A | 285,404 |
| | \$4,653,097 | \$3,538,188 | \$1,599,468 | \$1,183,613 | \$619,060 | \$308,469 | \$80,938 | N/A | \$11,982,833 |
| Allowance for loan losses at June 30, 2011 | | | | | | | | | |
| Measured for impairment under FASB ASC Subtopic 450-20 | \$44,600 | \$53,373 | \$9,560 | \$5,953 | \$18,794 | \$1,597 | \$1,727 | \$34,888 | \$170,492 |
| Evaluated for impairment under FASB ASC Section 310-10-35 | 28,998 | 29,240 | — | 25,959 | 11,776 | 158 | 60 | N/A | 96,191 |
| | \$73,598 | \$82,613 | \$9,560 | \$31,912 | \$30,570 | \$1,755 | \$1,787 | \$34,888 | \$266,683 |
| Loans, net of unearned income at June 30, 2011 | | | | | | | | | |
| Measured for impairment under FASB ASC Subtopic 450-20 | \$4,329,750 | \$3,587,702 | \$1,626,545 | \$955,863 | \$623,734 | \$330,754 | \$67,773 | N/A | \$11,522,121 |
| Evaluated for impairment under | 113,275 | 91,156 | — | 67,783 | 57,854 | 211 | 91 | N/A | 330,370 |

FASB ASC

Section 310-10-35

\$4,443,025 \$3,678,858 \$1,626,545 \$1,023,646 \$681,588 \$330,965 \$67,864 N/A \$11,852,491

The Corporation's unallocated allowance, which was approximately 9% and 13% as of June 30, 2012 and June 30, (1)2011, respectively, was reasonable and appropriate as the estimates used in the allocation process are inherently imprecise.

N/A – Not applicable.

In June 2012, the Corporation sold \$44.1 million of non-accrual commercial mortgage, commercial and construction loans to an investor, resulting in a total increase to charge-offs of \$21.2 million during the second quarter of 2012. Because the existing allowance for credit losses on the loans sold exceeded the charge-off amount, no additional provision for credit losses was required. Below is a summary of the transaction:

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

Impaired Loans

A loan is considered to be impaired if it is probable that all amounts will not be collected according to the contractual terms of the loan agreement.

An allowance for loan losses is established for an impaired loan if its carrying value exceeds its estimated fair value.

Impaired

loans with balances greater than \$1.0 million are evaluated individually for impairment. Impaired loans with balances less than \$1.0 million are pooled and measured for impairment collectively. As of June 30, 2012 and December 31, 2011, substantially all of the Corporation's individually evaluated impaired loans were measured based on the estimated fair value of each loan's collateral. Collateral could be in the form of real estate in the case of impaired commercial mortgages, construction loans and residential mortgages, or business assets, such as accounts receivable or inventory, in the case of commercial loans. Commercial loans may also be secured by real property.

As of June 30, 2012 and 2011, approximately 78% and 85%, respectively, of impaired loans with principal balances greater than \$1.0 million, whose primary collateral is real estate, were measured at estimated fair value using certified third-party appraisals that had been updated within the preceding 12 months.

Where updated certified appraisals are not obtained for loans evaluated for impairment under FASB ASC Section 310-10-35 that are secured by real estate, fair values are estimated based on one or more of the following:

Original appraisal – if the original appraisal indicated a very strong loan to value position and, in the opinion of the Corporation's internal loan evaluation staff, there has not been a significant deterioration in the collateral value, the original appraisal may be used to support the value of the collateral. Original appraisals are typically used only when the estimated collateral value, as adjusted, results in a current loan to value ratio that is lower than the Corporation's policy for new loans, generally 80%.

Broker price opinions – in lieu of obtaining an updated certified appraisal, a less formal indication of value, such as a broker price opinion, may be obtained. These opinions are generally used to validate internal estimates of collateral value and are not relied upon as the sole determinant of fair value.

Discounted cash flows – while substantially all of the Corporation's impaired loans are measured based on the estimated fair value of collateral, discounted cash flows analyses may be used to validate estimates of collateral value derived from other approaches.

The following table presents total impaired loans by class segment as of June 30, 2012 and December 31, 2011:

| | June 30, 2012 | | | December 31, 2011 | | |
|---------------------------------------|--------------------------------|------------------------|----------------------|--------------------------------|------------------------|----------------------|
| | Unpaid Principal Balance | Recorded Investment | Related Allowance | Unpaid Principal Balance | Recorded Investment | Related Allowance |
| | (in thousands) | | | | | |
| With no related allowance recorded: | | | | | | |
| Real estate - commercial mortgage | \$68,523 | \$52,478 | \$— | \$54,445 | \$46,768 | \$— |
| Commercial - secured | 27,642 | 21,916 | — | 35,529 | 28,440 | — |
| Commercial - unsecured | 13 | 13 | — | — | — | — |
| Real estate - home equity | 584 | 584 | — | 199 | 199 | — |
| Real estate - residential mortgage | 1,988 | 1,988 | — | — | — | — |
| Construction - commercial residential | 49,881 | 26,975 | — | 62,822 | 31,233 | — |
| Construction - commercial | 2,953 | 2,386 | — | 3,604 | 3,298 | — |
| | 151,584 | 106,340 | | 156,599 | 109,938 | |
| With a related allowance recorded: | | | | | | |
| Real estate - commercial mortgage | 75,818 | 59,255 | 22,337 | 100,529 | 79,566 | 36,060 |
| Commercial - secured | 53,775 | 42,395 | 23,205 | 61,970 | 47,652 | 26,248 |
| Commercial - unsecured | 2,769 | 2,604 | 2,076 | 3,139 | 2,789 | 2,177 |
| Real estate - home equity | 7,767 | 7,767 | 4,825 | 5,294 | 5,294 | 3,076 |
| Real estate - residential mortgage | 43,205 | 43,205 | 18,930 | 39,918 | 39,918 | 16,295 |
| Construction - commercial residential | 25,869 | 19,928 | 8,191 | 41,176 | 25,632 | 11,287 |
| Construction - commercial | 3,380 | 2,687 | 1,470 | 3,221 | 1,049 | 506 |
| Construction - other | 921 | 921 | 539 | 1,127 | 1,127 | 663 |
| Consumer - direct | 7 | 7 | 5 | 368 | 368 | 228 |
| Leasing and other and overdrafts | 295 | 295 | 191 | 56 | 56 | 37 |
| | 213,806 | 179,064 | 81,769 | 256,798 | 203,451 | 96,577 |
| Total | \$365,390 | \$285,404 | \$81,769 | \$413,397 | \$313,389 | \$96,577 |

As of June 30, 2012 and December 31, 2011, there were \$106.3 million and \$109.9 million, respectively, of impaired loans that did not have a related allowance for loan loss. The estimated fair values of the collateral for these loans exceeded their carrying amount and, accordingly, no specific valuation allowance was considered to be necessary.

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The following table presents average impaired loans by class segment for the three and six months ended June 30:

| | Three months ended June 30, 2012 | | Three months ended June 30, 2011 | | Six Months Ended June 30, 2012 | | Six Months Ended June 30, 2011 | |
|---------------------------------------|--|---|--|---|--|---|--|---|
| | Average Recorded Investment (1) | Interest Income Recognized (1) | Average Recorded Investment (1) | Interest Income Recognized (1) | Average Recorded Investment (1) | Interest Income Recognized (1) | Average Recorded Investment (1) | Interest Income Recognized (1) |
| | (in thousands) | | | | | | | |
| With no related allowance recorded: | | | | | | | | |
| Real estate - commercial mortgage | \$46,502 | \$ 127 | \$41,139 | \$ 87 | \$46,591 | \$ 198 | \$45,510 | \$ 490 |
| Commercial - secured | 21,798 | 10 | 32,313 | 15 | 24,012 | 17 | 30,790 | 161 |
| Commercial - unsecured | 13 | — | — | — | 9 | — | 196 | 3 |
| Real estate - home equity | 542 | — | — | — | 428 | — | — | — |
| Real estate - residential mortgage | 1,240 | 11 | — | — | 826 | 13 | 7,071 | 43 |
| Construction - commercial residential | 28,734 | 43 | 20,322 | 6 | 29,567 | 68 | 24,333 | 184 |
| Construction - commercial | 2,765 | 4 | 3,601 | 1 | 2,942 | 6 | 3,109 | 21 |
| | 101,594 | 195 | 97,375 | 109 | 104,375 | 302 | 111,009 | 902 |
| With a related allowance recorded: | | | | | | | | |
| Real estate - commercial mortgage | 64,733 | 161 | 70,441 | 150 | 69,677 | 283 | 81,650 | 989 |
| Commercial - secured | 47,437 | 20 | 47,747 | 22 | 47,508 | 33 | 97,723 | 1,199 |
| Commercial - unsecured | 2,822 | 1 | 3,193 | 2 | 2,811 | 2 | 4,996 | 33 |
| Real estate - home equity | 6,813 | 4 | — | — | 6,306 | 4 | — | — |
| Real estate - residential mortgage | 41,731 | 370 | 71,807 | 487 | 41,127 | 760 | 54,044 | 577 |
| Construction - commercial residential | 24,210 | 35 | 40,219 | 13 | 24,684 | 57 | 61,421 | 448 |
| Construction - commercial | 2,854 | 4 | 313 | — | 2,252 | 6 | 1,089 | 17 |
| Construction - other | 1,047 | 1 | 1,687 | — | 1,073 | 2 | 1,124 | — |
| Consumer - direct | 8 | — | 150 | 2 | 128 | — | 100 | 2 |
| Leasing and other and overdrafts | 164 | — | 77 | — | 128 | — | 51 | — |
| | 191,819 | 596 | 235,634 | 676 | 195,694 | 1,147 | 302,198 | 3,265 |
| Total | \$293,413 | \$ 791 | \$333,009 | \$ 785 | \$300,069 | \$ 1,449 | \$413,207 | \$ 4,167 |

All impaired loans, excluding accruing troubled debt restructurings, were non-accrual loans. Interest income (1) recognized for the three and six months ended June 30, 2012 and 2011 represent amounts earned on accruing troubled debt restructurings.

Credit Quality Indicators and Non-performing Assets

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

| | Pass | | Special Mention | | Substandard or Lower | | Total | |
|---|----------------|-------------------|-----------------|-------------------|----------------------|-------------------|---------------|-------------------|
| | June 30, 2012 | December 31, 2011 | June 30, 2012 | December 31, 2011 | June 30, 2012 | December 31, 2011 | June 30, 2012 | December 31, 2011 |
| | (in thousands) | | | | | | | |
| Real estate - commercial mortgage | \$4,195,679 | \$4,099,103 | \$153,931 | \$160,935 | \$303,487 | \$342,558 | \$4,653,097 | \$4,602,596 |
| Commercial - secured | 2,943,780 | 2,977,957 | 151,545 | 166,588 | 222,268 | 249,014 | 3,317,593 | 3,393,559 |
| Commercial - unsecured | 207,026 | 230,962 | 5,777 | 6,066 | 7,792 | 8,781 | 220,595 | 245,809 |
| Total commercial - industrial, financial and agricultural | 3,150,806 | 3,208,919 | 157,322 | 172,654 | 230,060 | 257,795 | 3,538,188 | 3,639,368 |
| Construction - commercial residential | 165,191 | 175,706 | 57,524 | 50,854 | 108,287 | 126,378 | 331,002 | 352,938 |
| Construction - commercial | 212,631 | 186,049 | 4,016 | 7,022 | 12,877 | 16,309 | 229,524 | 209,380 |
| Total construction (excluding Construction - other) | 377,822 | 361,755 | 61,540 | 57,876 | 121,164 | 142,687 | 560,526 | 562,318 |
| | \$7,724,307 | \$7,669,777 | \$372,793 | \$391,465 | \$654,711 | \$743,040 | \$8,751,811 | \$8,804,282 |
| % of Total | 88.2 | % 87.1 | % 4.3 | % 4.5 | % 7.5 | % 8.4 | % 100.0 | % 100.0 |

The following is a description of the Corporation's internal risk ratings assigned to commercial loans, commercial mortgages and certain construction loans:

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

Special Mention: These loans constitute an undue and unwarranted credit risk, but not to a point of justifying a classification of substandard. Loans in this category are currently acceptable, but are nevertheless potentially weak.

Substandard or Lower: Substandard loans are inadequately protected by current sound worth and paying capacity of the borrower. There exists a well-defined weakness or weaknesses that jeopardize the normal repayment of the debt.

The Corporation believes that internal risk ratings are the most relevant credit quality indicator for these types of loans. The migration of loans through the various internal risk rating categories is a significant component of the allowance for credit loss methodology, which bases the probability of default on this migration.

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

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

| | Performing | | Delinquent (1) | | Non-performing (2) | | Total | |
|------------------------------------|----------------|-------------------|----------------|-------------------|--------------------|-------------------|---------------|-------------------|
| | June 30, 2012 | December 31, 2011 | June 30, 2012 | December 31, 2011 | June 30, 2012 | December 31, 2011 | June 30, 2012 | December 31, 2011 |
| | (in thousands) | | | | | | | |
| Real estate - home equity | \$1,574,781 | \$1,601,722 | \$13,215 | \$11,633 | \$11,472 | \$11,207 | \$1,599,468 | \$1,624,562 |
| Real estate - residential mortgage | 1,123,426 | 1,043,733 | 34,814 | 37,123 | 25,373 | 16,336 | 1,183,613 | 1,097,192 |
| Construction - other | 56,631 | 49,593 | 982 | 2,341 | 921 | 1,193 | 58,534 | 53,127 |
| Consumer - direct | 153,624 | 157,157 | 3,810 | 4,011 | 3,300 | 3,201 | 160,734 | 164,369 |
| Consumer - indirect | 145,554 | 151,112 | 2,021 | 2,437 | 160 | 183 | 147,735 | 153,732 |
| Total consumer | 299,178 | 308,269 | 5,831 | 6,448 | 3,460 | 3,384 | 308,469 | 318,101 |
| Leasing and other and overdrafts | 80,114 | 70,550 | 428 | 1,049 | 396 | 107 | 80,938 | 71,706 |
| | \$3,134,130 | \$3,073,867 | \$55,270 | \$58,594 | \$41,622 | \$32,227 | \$3,231,022 | \$3,164,688 |
| % of Total | 97.0 | % 97.1 | % 1.7 | % 1.9 | % 1.3 | % 1.0 | % 100.0 | % 100.0 |

(1)Includes all accruing loans 31 days to 89 days past due.

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

The following table presents the detail of non-performing assets:

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| | June 30, 2012 | December 31, 2011 |
|--|------------------|----------------------|
| | (in thousands) | |
| Non-accrual loans | \$203,539 | \$257,761 |
| Accruing loans greater than 90 days past due | 30,434 | 28,767 |
| Total non-performing loans | 233,973 | 286,528 |
| Other real estate owned (OREO) | 32,338 | 30,803 |
| Total non-performing assets | \$266,311 | \$317,331 |

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The following table presents troubled debt restructurings (TDRs), by class segment:

| | June 30, 2012 | December 31, 2011 |
|---------------------------------------|------------------|----------------------|
| | (in thousands) | |
| Real-estate - residential mortgage | \$33,516 | \$32,331 |
| Real-estate - commercial mortgage | 32,481 | 22,425 |
| Construction - commercial residential | 10,030 | 7,645 |
| Commercial - secured | 4,679 | 3,449 |
| Real estate - home equity | 620 | 183 |
| Commercial -unsecured | 127 | 132 |
| Consumer - direct | — | 10 |
| Total accruing TDRs | 81,453 | 66,175 |
| Non-accrual TDRs (1) | 27,576 | 32,587 |
| Total TDRs | \$109,029 | \$98,762 |

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

As of June 30, 2012 and December 31, 2011, there were \$1.5 million and \$1.7 million, respectively, of commitments to lend additional funds to borrowers whose loans were modified under TDRs.

The following table presents loans modified as TDRs during the three and six months ended June 30, 2012 and classified as TDRs as of June 30, 2012, by class segment:

| | Three Months Ended June 30, 2012 | | Six Months Ended June 30, 2012 | |
|---------------------------------------|-------------------------------------|------------------------|-----------------------------------|------------------------|
| | Number of Loans | Recorded Investment | Number of Loans | Recorded Investment |
| | (dollars in thousands) | | | |
| Real estate - commercial mortgage | 9 | \$ 10,931 | 13 | \$ 16,600 |
| Real estate - residential mortgage | 11 | 3,436 | 24 | 8,115 |
| Construction - commercial residential | 3 | 4,072 | 6 | 10,437 |
| Real estate - home equity | 4 | 389 | 6 | 560 |
| Commercial - secured | 2 | 167 | 7 | 3,207 |
| | 29 | \$ 18,995 | 56 | \$ 38,919 |

The following table presents loans modified as TDRs within the previous 12 months, and classified as TDRs as of June 30, 2012, which had a payment default during the three and six months ended June 30, 2012, by class segment:

| | Three Months Ended June 30, 2012 | | Six Months Ended June 30, 2012 | |
|---------------------------------------|-------------------------------------|------------------------|-----------------------------------|------------------------|
| | Number of Loans | Recorded Investment | Number of Loans | Recorded Investment |
| | (dollars in thousands) | | | |
| Real estate - commercial mortgage | 12 | \$ 8,160 | 21 | \$ 12,248 |
| Construction - commercial residential | 2 | 5,670 | 5 | 13,220 |
| Real estate - residential mortgage | 16 | 5,217 | 24 | 6,931 |
| Real estate - home equity | 4 | 444 | 6 | 683 |
| Commercial - secured | 3 | 167 | 5 | 282 |
| | 37 | \$ 19,658 | 61 | \$ 33,364 |

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

| | June 30, 2012 | | | | | | | |
|---|--|------------------------------|--|-----------------|--------------------|-------------------|--------------|--------------|
| | 31-59 Days Past Due (in thousands) | 60-89 Days Past Due | ≥ 90 Days Past Due and Accruing | Non- accrual | Total ≥ 90 Days | Total Past Due | Current | Total |
| Real estate - commercial mortgage | \$11,981 | \$7,208 | \$2,927 | \$79,252 | \$82,179 | \$101,368 | \$4,551,729 | \$4,653,097 |
| Commercial - secured | 10,525 | 11,791 | 5,529 | 59,632 | 65,161 | 87,477 | 3,230,117 | 3,317,594 |
| Commercial - unsecured | 570 | 455 | 318 | 2,490 | 2,808 | 3,833 | 216,761 | 220,594 |
| Total commercial - industrial, financial and agricultural | 11,095 | 12,246 | 5,847 | 62,122 | 67,969 | 91,310 | 3,446,878 | 3,538,188 |
| Real estate - home equity | 9,835 | 3,380 | 4,528 | 6,944 | 11,472 | 24,687 | 1,574,781 | 1,599,468 |
| Real estate - residential mortgage | 24,400 | 10,414 | 14,109 | 11,264 | 25,373 | 60,187 | 1,123,426 | 1,183,613 |
| Construction - commercial residential | 2,068 | — | 129 | 36,873 | 37,002 | 39,070 | 291,932 | 331,002 |
| Construction - commercial | 2,820 | — | 128 | 5,073 | 5,201 | 8,021 | 221,503 | 229,524 |
| Construction - other | 982 | — | — | 921 | 921 | 1,903 | 56,631 | 58,534 |
| Total real estate - construction | 5,870 | — | 257 | 42,867 | 43,124 | 48,994 | 570,066 | 619,060 |
| Consumer - direct | 2,668 | 1,142 | 2,505 | 795 | 3,300 | 7,110 | 153,624 | 160,734 |
| Consumer - indirect | 1,688 | 333 | 160 | — | 160 | 2,181 | 145,554 | 147,735 |
| Total consumer | 4,356 | 1,475 | 2,665 | 795 | 3,460 | 9,291 | 299,178 | 308,469 |
| Leasing and other and overdrafts | 312 | 116 | 101 | 295 | 396 | 824 | 80,114 | 80,938 |
| | \$67,849 | \$34,839 | \$30,434 | \$203,539 | \$233,973 | \$336,661 | \$11,646,172 | \$11,982,833 |
| | December 31, 2011 | | | | | | | |
| | 31-59 Days Past Due (in thousands) | 60-89 Days Past Due | ≥ 90 Days Past Due and Accruing | Non- accrual | Total ≥ 90 Days | Total Past Due | Current | Total |
| Real estate - commercial mortgage | \$11,167 | \$14,437 | \$4,394 | \$109,412 | \$113,806 | \$139,410 | \$4,463,186 | \$4,602,596 |
| Commercial - secured | 9,284 | 4,498 | 4,831 | 73,048 | 77,879 | 91,661 | 3,301,899 | 3,393,560 |
| Commercial - unsecured | 671 | 515 | 409 | 2,656 | 3,065 | 4,251 | 241,557 | 245,808 |
| Total commercial - industrial, financial and agricultural | 9,955 | 5,013 | 5,240 | 75,704 | 80,944 | 95,912 | 3,543,456 | 3,639,368 |
| Real estate - home equity | 7,439 | 4,194 | 5,714 | 5,493 | 11,207 | 22,840 | 1,601,722 | 1,624,562 |
| Real estate - residential mortgage | 23,877 | 13,246 | 8,502 | 7,834 | 16,336 | 53,459 | 1,043,733 | 1,097,192 |
| Construction - commercial residential | 2,372 | 4,824 | 1,656 | 53,420 | 55,076 | 62,272 | 290,665 | 352,937 |

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| | | | | | | | | |
|----------------------------------|----------|----------|----------|-----------|-----------|-----------|--------------|--------------|
| Construction - commercial | 31 | — | 128 | 4,347 | 4,475 | 4,506 | 204,875 | 209,381 |
| Construction - other | 2,341 | — | 66 | 1,127 | 1,193 | 3,534 | 49,593 | 53,127 |
| Total real estate - construction | 4,744 | 4,824 | 1,850 | 58,894 | 60,744 | 70,312 | 545,133 | 615,445 |
| Consumer - direct | 2,706 | 1,305 | 2,833 | 368 | 3,201 | 7,212 | 157,157 | 164,369 |
| Consumer - indirect | 1,997 | 440 | 183 | — | 183 | 2,620 | 151,112 | 153,732 |
| Total consumer | 4,703 | 1,745 | 3,016 | 368 | 3,384 | 9,832 | 308,269 | 318,101 |
| Leasing and other and overdrafts | 925 | 124 | 51 | 56 | 107 | 1,156 | 70,550 | 71,706 |
| | \$62,810 | \$43,583 | \$28,767 | \$257,761 | \$286,528 | \$392,921 | \$11,576,049 | \$11,968,970 |

NOTE F – Mortgage Servicing Rights

The following table summarizes the changes in mortgage servicing rights (MSRs) for the three and six months ended June 30, which are included in other assets on the consolidated balance sheets:

| | Three months ended | | Six months ended | |
|---|--------------------|------------|------------------|------------|
| | June 30 | | June 30 | |
| | 2012 | 2011 | 2012 | 2011 |
| | (in thousands) | | | |
| Amortized cost: | | | | |
| Balance at beginning of period | \$35,259 | \$32,060 | \$34,666 | \$30,700 |
| Originations of mortgage servicing rights | 4,058 | 2,010 | 6,836 | 4,668 |
| Amortization | (2,314) | (1,261) | (4,499) | (2,559) |
| Balance at end of period | \$37,003 | \$32,809 | \$37,003 | \$32,809 |
| Valuation allowance | \$(1,550) | \$(1,550) | \$(1,550) | \$(1,550) |
| Net MSRs at end of period | \$35,453 | \$31,259 | \$35,453 | \$31,259 |

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

The Corporation estimates the fair value of its MSRs by discounting the estimated cash flows from servicing income, net of expense, over the expected life of the underlying loans at a discount rate commensurate with the risk associated with these assets. Expected life is based on the contractual terms of the loans, as adjusted for prepayment projections for mortgage-backed securities with rates and terms comparable to the loans underlying the MSRs. No adjustment to the valuation allowance was necessary as of June 30, 2012.

NOTE G – Stock-Based Compensation

The fair value of equity awards granted to employees is recognized as compensation expense over the period during which employees are required to provide service in exchange for such awards. The Corporation grants equity awards to employees, consisting of stock options and restricted stock, under its 2004 Stock Option and Compensation Plan (Employee Option Plan). In addition, employees may purchase stock under the Corporation's Employee Stock Purchase Plan.

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

The following table presents compensation expense and the related tax benefits for equity awards recognized in the consolidated statements of income for the three and six months ended June 30:

| | Three Months Ended June | | Six Months Ended June | |
|--|-------------------------|--------|-----------------------|---------|
| | 30 | | 30 | |
| | 2012 | 2011 | 2012 | 2011 |
| | (in thousands) | | | |
| Stock-based compensation expense | \$2,337 | \$554 | \$3,050 | \$1,101 |
| Tax benefit | (657) | (119) | (816) | (255) |
| Stock-based compensation expense, net of tax | \$1,680 | \$435 | \$2,234 | \$846 |

Stock option fair values are estimated through the use of the Black-Scholes valuation methodology as of the date of grant. Stock options carry terms of up to ten years. Restricted stock fair values are equal to the average trading price of the Corporation's stock on the date of grant. Restricted stock awards earn dividends during the vesting period, which are forfeitable if the awards do not vest. Stock options and restricted stock under the Employee Option Plan have

historically been granted annually and become fully vested over or after a three year vesting period. Restricted stock awards under the Directors' Plan generally vest one year from the date of grant. Certain events, as defined in the Employee Option Plan and Directors' Plan, result in the acceleration of the vesting of both stock options and restricted stock. On April 1, 2012, the Corporation granted approximately 471,000 stock options and

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320,000 shares of restricted stock under its Employee Option Plan. As of June 30, 2012, the Employee Option Plan had 11.9 million shares reserved for future grants through 2013.

On May 1, 2012, the Corporation granted approximately 21,000 shares of restricted stock under its Directors' Plan. As of June 30, 2012, the Directors' Plan had 469,000 shares reserved for future grants through 2021.

NOTE H – Employee Benefit Plans

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

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

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

The net periodic benefit cost for the Corporation's Pension Plan, as determined by consulting actuaries, consisted of the following components for the three and six months ended June 30:

| | Pension Plan | | Six Months Ended | |
|--------------------------------|--------------------|--------|------------------|----------|
| | Three Months Ended | | June 30 | |
| | 2012 | 2011 | 2012 | 2011 |
| | (in thousands) | | | |
| Service cost (1) | \$39 | \$15 | \$78 | \$30 |
| Interest cost | 806 | 853 | 1,612 | 1,706 |
| Expected return on plan assets | (808 |) (837 |) (1,616 |) (1,674 |
| Net amortization and deferral | 420 | 72 | 840 | 144 |
| Net periodic benefit cost | \$457 | \$103 | \$914 | \$206 |

The Pension Plan service cost recorded for the three and six months ended June 30, 2012 and 2011, respectively, (1) was related to administrative costs associated with the plan and not due to the accrual of additional participant benefits.

The net periodic benefit cost for the Corporation's Postretirement Plan, as determined by consulting actuaries, consisted of the following components for the three and six months ended June 30:

| | Postretirement Plan | | Six Months Ended | |
|--------------------------------|---------------------|-------|------------------|--------|
| | Three Months Ended | | June 30 | |
| | 2012 | 2011 | 2012 | 2011 |
| | (in thousands) | | | |
| Service cost | \$53 | \$50 | \$106 | \$101 |
| Interest cost | 87 | 107 | 174 | 214 |
| Expected return on plan assets | (1 |) (1 |) (2 |) (2 |
| Net accretion and deferral | (91 |) (91 |) (182 |) (182 |
| Net periodic benefit cost | \$48 | \$65 | \$96 | \$131 |

NOTE I – Derivative Financial Instruments

In connection with its mortgage banking activities, the Corporation enters into commitments to originate certain fixed-rate residential mortgage loans for customers, also referred to as interest rate locks. In addition, the Corporation

enters into forward commitments for the future sales or purchases of mortgage-backed securities to or from third-party counterparties to hedge the effect of changes in interest rates on the values of both the interest rate locks and mortgage loans held for sale. Forward sales commitments may also be in the form of commitments to sell individual mortgage loans at a fixed price at a future date. Both the interest rate locks and the forward commitments are accounted for as derivative financial instruments and are carried at fair value,

determined as the amount that would be necessary to settle each derivative financial instrument at the balance sheet date. The amount necessary to settle each interest rate lock is based on the price that secondary market investors would pay for loans with similar characteristics, including interest rate and term, as of the date fair value is measured. Gross derivative assets and liabilities are recorded within other assets and other liabilities, respectively, on the consolidated balance sheets, with changes in fair value during the period recorded within mortgage banking income on the consolidated statements of income. The other components of mortgage banking income are gains and losses on sales of mortgage loans, fair value adjustments on mortgage loans held for sale and servicing income, net of MSR amortization.

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

| | June 30, 2012 | | December 31, 2011 | |
|--|-----------------|------------------------------|-------------------|------------------------------|
| | Notional Amount | Asset (Liability) Fair Value | Notional Amount | Asset (Liability) Fair Value |
| | (in thousands) | | | |
| Interest Rate Locks with Customers: | | | | |
| Positive fair values | \$387,362 | \$8,970 | \$181,583 | \$3,888 |
| Negative fair values | 2,049 | (40 |) 1,593 | (10) |
| Net interest rate locks with customers | | 8,930 | | 3,878 |
| Forward Commitments: | | | | |
| Positive fair values | 4,626 | 29 | 3,178 | 13 |
| Negative fair values | 365,114 | (4,553 |) 173,208 | (2,724) |
| Net forward commitments | | (4,524 |) | (2,711) |
| Net derivative fair value asset | | \$4,406 | | \$1,167 |

The following table presents a summary of the fair value gains and losses on derivative financial instruments for the three and six months ended June 30:

| | Three Months Ended | | Six Months Ended | |
|---|--------------------|---------|------------------|-------------|
| | June 30 | June 30 | June 30 | June 30 |
| | 2012 | 2011 | 2012 | 2011 |
| | (in thousands) | | | |
| Interest rate locks with customers | \$4,243 | \$82 | \$5,052 | \$2,002 |
| Forward commitments | (5,159 |) (38 |) (1,813 |) (9,323) |
| Fair value gains (losses) on derivative financial instruments | \$ (916 |) \$44 | \$3,239 | \$ (7,321) |

NOTE J – Commitments and Contingencies

Commitments

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

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

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

| | June 30, 2012 | December 31, 2011 |
|------------------------------|----------------|-------------------|
| | (in thousands) | |
| Commitments to extend credit | \$3,992,822 | \$3,803,532 |
| Standby letters of credit | 424,588 | 444,019 |
| Commercial letters of credit | 27,663 | 31,557 |

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

Residential Lending

Residential mortgages are originated and sold by the Corporation through Fulton Mortgage Company, which operates as a division of each of the Corporation's subsidiary banks. Residential mortgage loans sold are primarily conforming, prime loans sold to government sponsored agencies such as the Federal National Mortgage Association (Fannie Mae). The Corporation provides customary representations and warranties to investors that specify, among other things, that the loans have been underwritten to the standards established by the investor. The Corporation may be required to repurchase a loan or reimburse the investor for a credit loss incurred on a loan if it is determined that the representations and warranties have not been met. This generally results from an underwriting or documentation deficiency. As of June 30, 2012 and December 31, 2011, total outstanding repurchase requests totaled approximately \$4.7 million and \$2.7 million, respectively.

From 2000 to 2011, the Corporation sold loans to the FHLB under its Mortgage Partnership Finance Program (MPF Program). No loans have been sold under this program in 2012. The Corporation provided a "credit enhancement" for residential mortgage loans sold under the MPF Program whereby it would assume credit losses in excess of a defined "First Loss Account" (FLA) balance, up to specified amounts. The FLA is funded by the FHLB based on a percentage of the outstanding principal balance of loans sold. As of June 30, 2012, the unpaid principal balance of loans sold under the MPF Program was approximately \$263 million. During the first six months of 2012, credit losses under the MPF Program were projected to exceed the FLA, and, as a result, the Corporation recorded a \$3.0 million reserve for expected credit losses related to loans sold under the MPF Program. This reserve was calculated based on delinquency status and estimated loss rates established through the Corporation's existing allowance for loan loss methodology. As of June 30, 2012 and December 31, 2011, the reserve for losses on residential mortgage loans sold was \$4.1 million and \$1.5 million, respectively, including both reserves for credit losses under the MPF Program and reserves for representation and warranty exposures. Management believes that the reserves recorded as of June 30, 2012 are adequate. However, declines in collateral values, the identification of additional loans to be repurchased, or a deterioration of the FHLB portfolio's credit quality could necessitate additional reserves in the future.

Other Contingencies

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

NOTE K – Fair Value Option

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

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

| | June 30, 2012 (in thousands) | December 31, 2011 |
|------------|------------------------------------|----------------------|
| Cost | \$68,779 | \$45,324 |
| Fair value | 71,406 | 47,009 |

During the three and six months ended June 30, 2012, the Corporation recorded gains related to changes in fair values of mortgage loans held for sale of \$1.1 million and \$941,000, respectively, compared to gains of \$533,000 and \$1.8 million, respectively, for the three and six months ended June 30, 2011.

NOTE L – Fair Value Measurements

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

Level 1 – Inputs that represent quoted prices for identical instruments in active markets.

Level 2 – Inputs that represent quoted prices for similar instruments in active markets, or quoted prices for identical instruments in non-active markets. Also includes valuation techniques whose inputs are derived principally from observable market data other than quoted prices, such as interest rates or other market-corroborated means.

Level 3 – Inputs that are largely unobservable, as little or no market data exists for the instrument being valued.

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

In May 2011, the FASB issued ASC Update 2011-04, "Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs." ASC Update 2011-04 amends fair value measurement and disclosure requirements in U.S. GAAP for the purpose of improving the comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with U.S. GAAP and International Financial Reporting Standards (IFRS). Among the amendments in ASC Update 2011-04 are expanded disclosure requirements that require companies to quantitatively disclose inputs used in recurring Level 3 fair value measurements and to disclose the sensitivity of fair value measurement to changes in unobservable inputs. Effective March 31, 2012, the Corporation adopted the provisions of ASC Update 2011-04 and, as such, has included the required disclosures related to Level 3 fair value measurements below.

Following is a summary of the Corporation's assets and liabilities measured at fair value on a recurring basis and reported on the consolidated balance sheets:

| | June 30, 2012 | | | |
|---|---------------------------|-------------|-----------|-------------|
| | Level 1 (in thousands) | Level 2 | Level 3 | Total |
| Mortgage loans held for sale | \$— | \$71,406 | \$— | \$71,406 |
| Available for sale investment securities: | | | | |
| Equity securities | 29,300 | — | — | 29,300 |
| U.S. Government securities | — | 327 | — | 327 |
| U.S. Government sponsored agency securities | — | 3,992 | — | 3,992 |
| State and municipal securities | — | 303,480 | — | 303,480 |
| Corporate debt securities | — | 121,257 | 9,118 | 130,375 |
| Collateralized mortgage obligations | — | 981,657 | — | 981,657 |
| Mortgage-backed securities | — | 1,135,746 | — | 1,135,746 |
| Auction rate securities | — | — | 203,282 | 203,282 |
| Total available for sale investments | 29,300 | 2,546,459 | 212,400 | 2,788,159 |
| Other financial assets | 13,746 | 8,999 | — | 22,745 |
| Total assets | \$43,046 | \$2,626,864 | \$212,400 | \$2,882,310 |
| Other financial liabilities | \$13,746 | \$4,593 | \$— | \$18,339 |

| | December 31, 2011 | | | Total |
|---|---------------------------|-------------|-----------|-------------|
| | Level 1 (in thousands) | Level 2 | Level 3 | |
| Mortgage loans held for sale | \$— | \$47,009 | \$— | \$47,009 |
| Available for sale investment securities: | | | | |
| Equity securities | 34,586 | — | — | 34,586 |
| U.S. Government securities | — | 334 | — | 334 |
| U.S. Government sponsored agency securities | — | 4,073 | — | 4,073 |
| State and municipal securities | — | 322,018 | — | 322,018 |
| Corporate debt securities | — | 114,017 | 9,289 | 123,306 |
| Collateralized mortgage obligations | — | 1,001,209 | — | 1,001,209 |
| Mortgage-backed securities | — | 880,097 | — | 880,097 |
| Auction rate securities | — | — | 225,211 | 225,211 |
| Total available for sale investments | 34,586 | 2,321,748 | 234,500 | 2,590,834 |
| Other financial assets | 13,130 | 3,901 | — | 17,031 |
| Total assets | \$47,716 | \$2,372,658 | \$234,500 | \$2,654,874 |
| Other financial liabilities | \$13,130 | \$2,734 | \$— | \$15,864 |

The valuation techniques used to measure fair value for the items in the preceding tables are as follows:

Mortgage loans held for sale – This category consists of mortgage loans held for sale that the Corporation has elected to measure at fair value. Fair values as of June 30, 2012 and December 31, 2011 were measured as the price that secondary market investors were offering for loans with similar characteristics.

Available for sale investment securities – Included within this asset category are both equity and debt securities. Level 2 available for sale debt securities are valued by a third-party pricing service commonly used in the banking industry. The pricing service uses evaluated pricing models that vary based on asset class and incorporate available market information including quoted prices of investment securities with similar characteristics. Because many fixed income securities do not trade on a daily basis, evaluated pricing models use available information, as applicable, through processes such as benchmark yield curves, benchmarking of like securities, sector groupings, and matrix pricing. Standard market inputs include: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data including market research publications. For certain security types, additional inputs may be used, or some of the standard market inputs may not be applicable.

Management tests the values provided by the pricing service by obtaining securities prices from an alternative third-party source and comparing the results. This test is done for approximately 80% of the securities valued by the pricing service. Generally, differences by security in excess of 5% are researched to reconcile the difference.

Equity securities – Equity securities consist of stocks of financial institutions (\$22.6 million at June 30, 2012 and \$27.9 million at December 31, 2011) and other equity investments (\$6.6 million at June 30, 2012 and \$6.7 million at December 31, 2011). These Level 1 investments are measured at fair value based on quoted prices for identical securities in active markets. Restricted equity securities issued by the FHLB and Federal Reserve Bank (\$76.1 million at June 30, 2012 and \$82.5 million at December 31, 2011) have been excluded from the preceding tables.

U.S. Government securities/U.S. Government sponsored agency securities/State and municipal securities/Collateralized mortgage obligations/Mortgage-backed securities – These debt securities are classified as Level 2 investments. Fair values are determined by a third-party pricing service, as detailed above.

Corporate debt securities – This category consists of subordinated debt issued by financial institutions (\$46.0 million at June 30, 2012 and \$41.3 million at December 31, 2011), single-issuer trust preferred securities issued by financial institutions (\$76.8 million at June 30, 2012 and \$74.4 million at December 31, 2011), pooled trust preferred securities issued by financial institutions (\$5.0 million at June 30, 2012 and \$5.1 million at December 31, 2011) and other corporate debt issued by non-financial institutions (\$2.5 million at June 30, 2012 and December 31, 2011).

Classified as Level 2 investments are the Corporation's subordinated debt, other corporate debt issued by non-

financial institutions and \$72.7 million and \$70.2 million of single-issuer trust preferred securities held at June 30, 2012 and December 31, 2011, respectively. These corporate debt securities are measured at fair value by a third-party pricing service, as detailed above.

Classified as Level 3 assets are the Corporation's investments in pooled trust preferred securities and certain single-issuer trust preferred securities (\$4.1 million at June 30, 2012 and \$4.2 million at December 31, 2011). The fair values of these securities were determined based on quotes provided by third-party brokers who determined fair values based predominantly on internal valuation models which were not indicative prices or binding offers. The Corporation's third-party pricing service cannot derive fair values for these securities primarily due to inactive markets for similar investments. Level 3 values are tested by management primarily through trend analysis, by comparing current values to those reported at the end of the preceding calendar quarter, and determining if they are reasonable based on price and spread movements for this asset class.

Auction rate securities – Due to their illiquidity, ARCs are classified as Level 3 investments and are valued through the use of an expected cash flows model prepared by a third-party valuation expert. The assumptions used in preparing the expected cash flows model include estimates for coupon rates, time to maturity and market rates of return. The most significant unobservable input to the expected cash flows model is an assumed return to market liquidity sometime within the next five years. If the assumed return to market liquidity was lengthened beyond the next five years, this would result in a decrease in the fair value of these ARCs. Expected cash flows models performed prior to June 30, 2012 assumed a return to market liquidity sometime within the next three years. The three year expected term was based on the Corporation's assumption that market liquidity would resume, in some form, within a relatively short period of time. Although there has been a material reduction in the Corporation's outstanding ARCs, a more protracted period of sporadic trust refinancing and periodic tenders of bonds is expected. The Corporation believes that the trusts underlying the ARCs will self-liquidate as student loans are paid down. Based on this historical experience, the Corporation elected to increase the expected term as of June 30, 2012.

Management tests Level 3 valuations for ARCs by performing a trend analysis of the market price and discount rate. Changes in the price and discount rates are compared to changes in market data, including bond ratings, parity ratios, balances and delinquency levels. Any inconsistencies are reconciled through discussions with the third-party valuation expert.

Other financial assets – Included within this asset category are: Level 1 assets, consisting of mutual funds that are held in trust for employee deferred compensation plans and measured at fair value based on quoted prices for identical securities in active markets; and Level 2 assets, representing the fair value of mortgage banking derivatives in the form of interest rate locks and forward commitments with secondary market investors. The fair value of the Corporation's interest rate locks and forward commitments are determined as the amounts that would be required to settle the derivative financial instruments at the balance sheet date. See Note I, "Derivative Financial Instruments," for additional information.

Other financial liabilities – Included within this category are: Level 1 employee deferred compensation liabilities which represent amounts due to employees under the deferred compensation plans, described under the heading "Other financial assets" above and Level 2 mortgage banking derivatives, described under the heading "Other financial assets" above.

The following table presents the changes in the Corporation's assets and liabilities measured at fair value on a recurring basis using unobservable inputs (Level 3) for the three and six months ended June 30, 2012 and 2011:

| | Three months ended June 30, 2012 | | |
|---|--|-----------------|-------------|
| | Available for Sale Investment Securities | | |
| | Pooled Trust | Single-issuer | ARC |
| | Preferred | Trust Preferred | Investments |
| | Securities | Securities | |
| | (in thousands) | | |
| Balance at March 31, 2012 | \$5,062 | \$4,360 | \$223,877 |
| Unrealized adjustment to fair value (1) | 137 | (262 |) (17,322 |
| Settlements - calls | (180 |) — | (4,193 |
| (Premium amortization) discount accretion (2) | (1 |) 2 | 920 |
| Balance at June 30, 2012 | \$5,018 | \$4,100 | \$203,282 |
| | Three months ended June 30, 2011 | | |
| Balance at March 31, 2011 | \$4,816 | \$8,094 | \$256,413 |
| Realized adjustment to fair value (3) | (359 |) — | — |
| Unrealized adjustment to fair value (1) | 1,110 | 280 | (1,308 |
| Settlements - calls | (133 |) (555 |) (976 |
| (Premium amortization) discount accretion (2) | (1 |) — | 1,013 |
| Balance at June 30, 2011 | \$5,433 | \$7,819 | \$255,142 |
| | Six months ended June 30, 2012 | | |
| | Available for Sale Investment Securities | | |
| | Pooled Trust | Single-issuer | ARC |
| | Preferred | Trust Preferred | Investments |
| | Securities | Securities | |
| | (in thousands) | | |
| Balance at December 31, 2011 | \$5,109 | \$4,180 | \$225,211 |
| Unrealized adjustment to fair value (1) | 314 | (84 |) (19,486 |
| Settlements - calls | (403 |) — | (4,510 |
| (Premium amortization) discount accretion (2) | (2 |) 4 | 2,067 |
| Balance at June 30, 2012 | \$5,018 | \$4,100 | \$203,282 |
| | Six months ended June 30, 2011 | | |
| Balance, December 31, 2010 | \$4,528 | \$8,583 | \$260,679 |
| Transfer to Level 3 from Level 2 (4) | — | (800 |) — |
| Realized adjustment to fair value (3) | (1,353 |) — | — |
| Unrealized adjustment to fair value (1) | 2,478 | 591 | (1,231 |
| Settlements - calls | (218 |) (555 |) (6,499 |
| (Premium amortization) discount accretion (2) | (2 |) — | 2,193 |
| Balance at June 30, 2011 | \$5,433 | \$7,819 | \$255,142 |

Pooled trust preferred securities, single-issuer trust preferred securities and ARCs are classified as available for sale investment securities; as such, the unrealized adjustment to fair value was recorded as an unrealized holding gain (loss) and included as a component of available for sale investment securities on the consolidated balance sheet.

(2) Included as a component of net interest income on the consolidated statements of income.

(3) Realized adjustments to fair value represent credit related other-than-temporary impairment charges that were recorded as a reduction to investment securities gains on the consolidated statements of income.

(4) During the six months ended June 30, 2011, one single-issuer trust preferred security with a fair value of \$800,000 was reclassified as a Level 2 asset.

Certain financial assets are not measured at fair value on an ongoing basis but are subject to fair value measurement in certain circumstances, such as upon their acquisition or when there is evidence of impairment. The following table presents the Corporation's financial assets measured at fair value on a nonrecurring basis and reported on the Corporation's consolidated balance sheets:

| | June 30, 2012 | | | |
|------------------------|-------------------|---------|-----------|-----------|
| | Level 1 | Level 2 | Level 3 | Total |
| | (in thousands) | | | |
| Net loans | \$— | \$— | \$203,635 | \$203,635 |
| Other financial assets | — | — | 67,791 | 67,791 |
| Total assets | \$— | \$— | \$271,426 | \$271,426 |
| | December 31, 2011 | | | |
| | Level 1 | Level 2 | Level 3 | Total |
| | (in thousands) | | | |
| Net loans | \$— | \$— | \$216,812 | \$216,812 |
| Other financial assets | — | — | 63,919 | 63,919 |
| Total assets | \$— | \$— | \$280,731 | \$280,731 |

The valuation techniques used to measure fair value for the items in the tables above are as follows:

Net loans – This category consists of loans that were evaluated for impairment under FASB ASC Section 310-10-35 and have been classified as Level 3 assets. The amount shown is the balance of impaired loans, net of the related allowance for loan losses. See Note E, "Loans and Allowance for Credit Losses," for additional details.

Other financial assets – This category includes OREO (\$32.3 million at June 30, 2012 and \$30.8 million at December 31, 2011) and MSRs, net of the MSR valuation reserve (\$35.5 million at June 30, 2012 and \$33.1 million at December 31, 2011), both classified as Level 3 assets.

Fair values for OREO were based on estimated selling prices less estimated selling costs for similar assets in active markets.

MSRs are initially recorded at fair value upon the sale of residential mortgage loans, which the Corporation continues to service, to secondary market investors. MSRs are amortized as a reduction to servicing income over the estimated lives of the underlying loans. MSRs are stratified and evaluated for impairment by comparing each stratum's carrying amount to its estimated fair value. Fair values are determined at the end of each quarter through a discounted cash flows valuation. Significant inputs to the valuations include expected net servicing income, the discount rate and the expected life of the underlying loans. Expected life is based on the contractual terms of the loans, as adjusted for prepayment projections for mortgage-backed securities with rates and terms comparable to the loans underlying the MSRs. The annual constant prepayment rates used in the June 30, 2012 discounted cash flows valuation ranged from 11.2% to 18.5%, and were based on the weighted average remaining term of loans in each stratum.

As required by FASB ASC Section 825-10-50, the following table details the book values and estimated fair values of the Corporation's financial instruments as of June 30, 2012 and December 31, 2011. In addition, a general description of the methods and assumptions used to estimate such fair values is also provided.

Fair values of financial instruments are significantly affected by assumptions used, principally the timing of future cash flows and discount rates. Because assumptions are inherently subjective in nature, the estimated fair values cannot be substantiated by comparison to independent market quotes and, in many cases, the estimated fair values could not necessarily be realized in an immediate sale or settlement of the instrument. The aggregate fair value amounts presented do not necessarily represent management's estimate of the underlying value of the Corporation.

| | June 30, 2012 | | December 31, 2011 | |
|--|----------------|----------------------|-------------------|----------------------|
| | Book Value | Estimated Fair Value | Book Value | Estimated Fair Value |
| | (in thousands) | | | |
| FINANCIAL ASSETS | | | | |
| Cash and due from banks | \$242,811 | \$242,811 | \$292,598 | \$292,598 |
| Interest-bearing deposits with other banks | 118,468 | 118,468 | 175,336 | 175,336 |
| Loans held for sale (1) | 71,406 | 71,406 | 47,009 | 47,009 |
| Securities held to maturity | 6,562 | 6,571 | 6,669 | 6,699 |
| Securities available for sale (1) | 2,864,270 | 2,864,270 | 2,673,298 | 2,673,298 |
| Loans, net of unearned income (1) | 11,982,833 | 11,943,390 | 11,968,970 | 11,992,586 |
| Accrued interest receivable | 48,283 | 48,283 | 51,098 | 51,098 |
| Other financial assets (1) | 144,910 | 144,910 | 315,952 | 315,952 |
| FINANCIAL LIABILITIES | | | | |
| Demand and savings deposits | \$8,497,839 | \$8,497,839 | \$8,511,789 | \$8,511,789 |
| Time deposits | 3,734,645 | 3,771,367 | 4,013,950 | 4,056,247 |
| Short-term borrowings | 931,681 | 931,681 | 597,033 | 597,033 |
| Accrued interest payable | 23,725 | 23,725 | 25,686 | 25,686 |
| Other financial liabilities (1) | 85,440 | 85,440 | 69,816 | 69,816 |
| Federal Home Loan Bank advances and long-term debt | 908,809 | 864,733 | 1,040,149 | 982,010 |

(1) Description of fair value determinations for these financial instruments, or certain financial instruments within these categories, measured at fair value on the Corporation's consolidated balance sheets, are disclosed above. For short-term financial instruments, defined as those with remaining maturities of 90 days or less and excluding those recorded at fair value on the Corporation's consolidated balance sheets, book value was considered to be a reasonable estimate of fair value.

The following instruments are predominantly short-term:

| | |
|-----------------------------|-----------------------------|
| Assets | Liabilities |
| Cash and due from banks | Demand and savings deposits |
| Interest bearing deposits | Short-term borrowings |
| Accrued interest receivable | Accrued interest payable |
| | Other financial liabilities |

For those financial instruments within the above-listed categories with remaining maturities greater than 90 days, fair values were determined by discounting contractual cash flows using rates which could be earned for assets with similar remaining maturities and, in the case of liabilities, rates at which the liabilities with similar remaining maturities could be issued as of the balance sheet date.

The estimated fair values of securities held to maturity as of June 30, 2012 and December 31, 2011 were based on quoted market prices. The estimated fair value of securities would be categorized within Level 2 assets under FASB ASC Topic 820.

Estimated fair values for loans and time deposits were estimated by discounting future cash flows using the current rates at which similar loans would be made to borrowers for the same remaining maturities. Fair values estimated in this manner do not fully incorporate an exit price approach to fair value, as defined in FASB ASC Topic 820.

The fair value of FHLB advances and long-term debt was estimated by discounting the remaining contractual cash flows using a rate at which the Corporation could issue debt with a similar remaining maturity as of the balance sheet date. The estimated fair value of these borrowings would be categorized within Level 2 assets under FASB ASC Topic 820.

The fair values of commitments to extend credit and standby letters of credit are estimated to equal their carrying amounts.

NOTE M – Common Stock Repurchase Plan

In June 2012, the Corporation announced that its board of directors approved a share repurchase program pursuant to which the Corporation is authorized to repurchase up to five million shares, or approximately 2.5% of the Corporation's outstanding shares,

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through December 31, 2012. Repurchased shares will be added to treasury stock, at cost, and will be used for general corporate purposes. As permitted by securities laws and other legal requirements and subject to market conditions and other factors, purchases may be made from time to time in open market purchases at prevailing prices. The program may be discontinued at any time. As of June 30, 2012, the Corporation had not repurchased any shares under this program.

NOTE N – Reclassifications

Certain amounts in the 2011 consolidated financial statements and notes have been reclassified to conform to the 2012 presentation.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations (Management's Discussion) relates to Fulton Financial Corporation (the Corporation), a financial holding company registered under the Bank Holding Company Act and incorporated under the laws of the Commonwealth of Pennsylvania in 1982, and its wholly owned subsidiaries. Management's Discussion should be read in conjunction with the consolidated financial statements and notes presented in this report.

FORWARD-LOOKING STATEMENTS

The Corporation has made, and may continue to make, certain forward-looking statements with respect to its financial condition and results of operations. Many factors could affect future financial results including, without limitation: the impact of adverse changes in the economy and real estate markets; increases in non-performing assets which may reduce the level of earning assets and require the Corporation to increase the allowance for credit losses, charge-off loans and incur elevated collection and carrying costs related to such non-performing assets; acquisition and growth strategies; market risk; changes or adverse developments in political or regulatory conditions; a disruption in, or abnormal functioning of, credit and other markets, including the lack of or reduced access to markets for mortgages and other asset-backed securities and for commercial paper and other short-term borrowings; changes in the levels of, or methodology for determining, FDIC deposit insurance premiums and assessments; the effect of competition and interest rates on net interest margin and net interest income; investment strategy and other income growth; investment securities gains and losses; declines in the value of securities which may result in charges to earnings; changes in rates of deposit and loan growth or a decline in loans originated; relative balances of rate-sensitive assets to rate-sensitive liabilities; salaries and employee benefits and other expenses; amortization of intangible assets; goodwill impairment; capital and liquidity strategies; and other financial and business matters for future periods. Do not unduly rely on forward-looking statements. Forward-looking statements can be identified by the use of words such as "may," "should," "will," "could," "estimates," "predicts," "potential," "continue," "anticipates," "believes," "plans," "expects," "future," "intends" and similar expressions which are intended to identify forward-looking statements. These statements are not guarantees of future performance and are subject to risks and uncertainties, some of which are beyond the Corporation's control and ability to predict, that could cause actual results to differ materially from those expressed in the forward-looking statements. The Corporation undertakes no obligation, other than as required by law, to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

RESULTS OF OPERATIONS

Summary Financial Results

The Corporation generates the majority of its revenue through net interest income, or the difference between interest earned on loans and investments and interest paid on deposits and borrowings. Growth in net interest income is dependent upon balance sheet growth and/or maintaining or increasing the net interest margin, which is net interest income (fully taxable-equivalent, or FTE) as a percentage of average interest-earning assets. The Corporation also generates revenue through fees earned on the various services and products offered to its customers and through sales of assets, such as loans, investments or properties. Offsetting these revenue sources are provisions for credit losses, operating expenses and income taxes.

The following table presents a summary of the Corporation's earnings and selected performance ratios:

| | As of or for the | | As of or for the | | |
|---|--------------------|----------|------------------|----------|---|
| | Three months ended | | Six months ended | | |
| | June 30 | | June 30 | | |
| | 2012 | 2011 | 2012 | 2011 | |
| Income before income taxes (in thousands) | \$53,251 | \$49,539 | \$104,915 | \$95,699 | |
| Net income (in thousands) | \$39,891 | \$36,385 | \$78,023 | \$70,170 | |
| Diluted net income per share | \$0.20 | \$0.18 | \$0.39 | \$0.35 | |
| Return on average assets | 0.98 | % 0.91 | % 0.96 | % 0.88 | % |
| Return on average equity | 7.84 | % 7.53 | % 7.72 | % 7.38 | % |
| Net interest margin (1) | 3.78 | % 3.95 | % 3.81 | % 3.93 | % |
| Non-performing assets to total assets | 1.63 | % 2.18 | % 1.63 | % 2.18 | % |
| Net charge-offs to average loans | 1.55 | % 1.30 | % 1.24 | % 1.36 | % |

(1) Presented on an FTE basis, using a 35% Federal tax rate and statutory interest expense disallowances. See also the "Net Interest Income" section of Management's Discussion.

The Corporation's income before income taxes for the second quarter of 2012 increased \$3.7 million, or 7.5%, from the same period in 2011. Income before income taxes for the first half of 2012 increased \$9.2 million, or 9.6%, from the same period in 2011.

Asset quality and net interest income continue to be key drivers of financial performance for the Corporation. Results for the first half of 2012 were also impacted by mortgage banking activities and higher non-interest expenses. The following is a brief overview of each of these areas.

Asset Quality - Economic conditions improved throughout most of the Corporation's markets during the first half of 2012. For the three and six months ended June 30, 2012, the Corporation's provision for credit losses decreased \$10.5 million, or 29.2%, and \$20.5 million, or 27.7%, respectively, in comparison to the same periods in 2011. In comparison to June 30, 2011, non-performing loans decreased \$76.9 million, or 24.7%, due in large part to the sale of \$34.7 million of non-accrual residential mortgages in December 2011 and \$44.1 million of non-accrual commercial mortgages, commercial and construction loans in June 2012. Overall loan delinquency also improved in comparison to June 30, 2011, decreasing to 2.81% from 3.48%.

Mortgage Banking Operations - During the three and six months ended June 30, 2012, mortgage banking income increased \$5.1 million, or 84.2%, and \$9.7 million, or 84.1%, respectively, in comparison to the same periods in 2011. Gains on sales of mortgage loans for the three and six months ended June 30, 2012 increased \$5.9 million, or 116.8%, and \$11.0 million, or 115.0%, respectively. The three and six-month increases in gains on sales of mortgage loans were due to both increases in pricing spreads and increases in new loan commitments. During the three and six months ended June 30, 2012, new commitments increased \$303.1 million, or 85.9%, and \$590.5 million, or 86.7%, respectively, in comparison to the same periods in 2011. This increase was largely due to an increase in refinances in the persistent low interest rate environment.

Estimated losses on residential mortgage loans previously originated and sold by the Corporation, recorded as a component of operating risk loss on the consolidated statements of income, were \$681,000 and \$3.6 million for the three and six months ended June 30, 2012 in comparison to credits of \$500,000 and \$1.4 million for the same periods in 2011. During the three and six months ended June 30, 2012, the Corporation recorded \$362,000 and \$3.0 million, respectively, of charges due to exposure in one specific investor program with the Federal Home Loan Bank (FHLB). Under this program, the Corporation provided a "credit enhancement" for residential mortgage loans sold, whereby it was responsible for credit losses above defined levels, up to specified amounts. The credits recorded during the three and six months ended June 30, 2011 resulted from a decrease in the Corporation's exposure due to entering into settlement agreements with certain secondary market investors. See Note J, "Commitments and Contingencies," in the Notes to Consolidated Financial Statements for additional details.

Net Interest Income and Net Interest Margin - Net interest income decreased \$3.1 million, or 2.2%, and \$4.0 million, or 1.4%, respectively, for the three and six months ended June 30, 2012 in comparison to the same periods in 2011. These decreases were driven by decreases in the net interest margin of 17 basis points, or 4.3%, and 12 basis points, or

3.1%, respectively, for the three and six months ended June 30, 2012 in comparison to the same periods in 2011. The decrease in the net interest margin resulted from the continuing low interest rate environment, in which yields on earning assets declined more significantly than the cost of funds.

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Non-Interest Expenses - During the three and six months ended June 30, 2012, total non-interest expenses increased \$11.3 million, or 11.2%, and \$21.1 million, or 10.5%, respectively. These increases resulted from salaries and benefits costs, loan workout expenses, operating risk loss and higher consulting expenses. For more details, see the "Non-Interest Expense" sections of Management's Discussion.

Quarter Ended June 30, 2012 compared to the Quarter Ended June 30, 2011

Net Interest Income

FTE net interest income decreased \$2.9 million, or 2.0%, from \$144.6 million in the second quarter of 2011 to \$141.7 million in the second quarter of 2012. This decrease was primarily due to a decrease in net interest margin, partially offset by the impact of a \$378.4 million, or 2.6%, increase in average interest-earning assets.

Net interest margin decreased 17 basis points, or 4.3%, from 3.95% for the second quarter of 2011 to 3.78% for the second quarter of 2012. The decrease in net interest margin was due to the net effect of a 40 basis point, or 8.2%, decrease in yields on interest-earning assets, which more than offset a 26 basis point, or 21.8%, decrease in funding costs.

The following table provides a comparative average balance sheet and net interest income analysis for the second quarter of 2012 as compared to the same period in 2011. Interest income and yields are presented on an FTE basis, using a 35% Federal tax rate and statutory interest expense disallowances. The discussion following this table is based on these FTE amounts. All dollar amounts are in thousands.

| ASSETS | Three months ended June 30 | | | 2011 | | | Yield/ Rate | |
|---|----------------------------|-----------------|----------------|--------------------|-----------------|----------------|----------------|---|
| | 2012 Average Balance | Interest (1) | Yield/ Rate | Average Balance | Interest (1) | Yield/ Rate | | |
| Interest-earning assets: | | | | | | | | |
| Loans, net of unearned income (2) | \$11,965,704 | \$144,263 | 4.85 | % \$11,883,019 | \$151,974 | 5.13 | % | |
| Taxable investment securities (3) | 2,533,060 | 18,624 | 2.94 | 2,141,307 | 20,749 | 3.88 | | |
| Tax-exempt investment securities (3) | 283,736 | 3,992 | 5.63 | 343,214 | 4,840 | 5.64 | | |
| Equity securities (3) | 106,954 | 707 | 2.65 | 128,258 | 775 | 2.42 | | |
| Total investment securities | 2,923,750 | 23,323 | 3.19 | 2,612,779 | 26,364 | 4.04 | | |
| Loans held for sale | 55,813 | 538 | 3.85 | 36,793 | 492 | 5.34 | | |
| Other interest-earning assets | 129,272 | 45 | 0.14 | 163,548 | 101 | 0.25 | | |
| Total interest-earning assets | 15,074,539 | 168,169 | 4.48 | % 14,696,139 | 178,931 | 4.88 | % | |
| Noninterest-earning assets: | | | | | | | | |
| Cash and due from banks | 233,427 | | | 278,393 | | | | |
| Premises and equipment | 216,881 | | | 207,141 | | | | |
| Other assets | 1,093,673 | | | 1,098,116 | | | | |
| Less: Allowance for loan losses | (259,327) | | | (273,593) | | | | |
| Total Assets | \$16,359,193 | | | \$16,006,196 | | | | |
| LIABILITIES AND EQUITY | | | | | | | | |
| Interest-bearing liabilities: | | | | | | | | |
| Demand deposits | \$2,484,730 | \$1,025 | 0.17 | % \$2,352,961 | \$1,371 | 0.23 | % | |
| Savings deposits | 3,292,620 | 1,510 | 0.18 | 3,356,361 | 3,258 | 0.39 | | |
| Time deposits | 3,791,362 | 12,208 | 1.30 | 4,353,352 | 17,146 | 1.58 | | |
| Total interest-bearing deposits | 9,568,712 | 14,743 | 0.62 | 10,062,674 | 21,775 | 0.87 | | |
| Short-term borrowings | 961,900 | 411 | 0.17 | 455,831 | 168 | 0.15 | | |
| FHLB advances and long-term debt | 929,318 | 11,301 | 4.88 | 1,025,637 | 12,347 | 4.82 | | |
| Total interest-bearing liabilities | 11,459,930 | 26,455 | 0.93 | % 11,544,142 | 34,290 | 1.19 | % | |
| Noninterest-bearing liabilities: | | | | | | | | |
| Demand deposits | 2,669,152 | | | 2,362,614 | | | | |
| Other | 183,794 | | | 162,202 | | | | |
| Total Liabilities | 14,312,876 | | | 14,068,958 | | | | |
| Shareholders' equity | 2,046,317 | | | 1,937,238 | | | | |
| Total Liabilities and Shareholders' Equity | \$16,359,193 | | | \$16,006,196 | | | | |
| Net interest income/net interest margin (FTE) | | 141,714 | 3.78 | % | | 144,641 | 3.95 | % |
| Tax equivalent adjustment | | (4,184) | | | | (3,996) | | |
| Net interest income | | \$137,530 | | | | \$140,645 | | |

(1) Includes dividends earned on equity securities.

(2) Includes non-performing loans.

(3) Balances include amortized historical cost for available for sale securities; the related unrealized holding gains (losses) are included in other assets.

The following table summarizes the changes in FTE interest income and interest expense due to changes in average balances (volume) and changes in rates:

| | 2012 vs. 2011 | | |
|----------------------------------|--------------------------------------|------------|------------|
| | Increase (decrease) due to change in | | |
| | Volume | Rate | Net |
| | (in thousands) | | |
| Interest income on: | | | |
| Loans, net of unearned income | \$ 1,002 | \$(8,713) | \$(7,711) |
| Taxable investment securities | 3,389 | (5,514) | (2,125) |
| Tax-exempt investment securities | (842) | (6) | (848) |
| Equity securities | (135) | 67 | (68) |
| Loans held for sale | 208 | (162) | 46 |
| Other interest-earning assets | (18) | (38) | (56) |
| Total interest income | \$3,604 | \$(14,366) | \$(10,762) |
| Interest expense on: | | | |
| Demand deposits | \$73 | \$(419) | \$(346) |
| Savings deposits | (61) | (1,687) | (1,748) |
| Time deposits | (2,061) | (2,877) | (4,938) |
| Short-term borrowings | 212 | 31 | 243 |
| FHLB advances and long-term debt | (1,199) | 153 | (1,046) |
| Total interest expense | \$(3,036) | \$(4,799) | \$(7,835) |

Note: Changes which are attributable to both volume and rate are allocated to the volume and rate components presented above based on the percentage of direct changes that are attributable to each component.

As summarized above, a 40 basis point, or 8.2%, decrease in average yields resulted in a \$14.4 million decrease in FTE interest income, which was partially offset by a \$3.6 million increase in FTE interest income as a result of a \$378.4 million, or 2.6%, increase in average interest-earning assets.

The increase in average interest-earning assets was primarily due to a \$311.0 million, or 11.9%, increase in average investments. During the first half of 2012, the Corporation increased its investments in mortgage-backed securities in anticipation of a continued low interest rate environment.

The average yield on investment securities decreased 85 basis points, or 21.0%, from 4.04% in 2011 to 3.19% in 2012, as the reinvestment of cash flows and purchases of taxable investment securities were at yields that were lower than the overall portfolio yield. An increase in net premium amortization of \$2.1 million due to higher prepayments on mortgage-backed securities contributed 29 basis points to the decrease in average investment yields and 5 basis points to the decrease in net interest margin.

Average loans, by type, are summarized in the following table:

| | Three months ended | | Increase (decrease) | | |
|---|------------------------|--------------|---------------------|--------|---|
| | June 30 | | | | |
| | 2012 | 2011 | \$ | % | |
| | (dollars in thousands) | | | | |
| Real estate – commercial mortgage | \$4,634,436 | \$4,430,046 | \$204,390 | 4.6 | % |
| Commercial – industrial, financial and agricultural | 3,529,947 | 3,689,877 | (159,930) | (4.3) |) |
| Real estate – home equity | 1,599,702 | 1,623,438 | (23,736) | (1.5) |) |
| Real estate – residential mortgage | 1,179,513 | 1,023,471 | 156,042 | 15.2 | |
| Real estate – construction | 640,282 | 712,638 | (72,356) | (10.2) |) |
| Consumer | 307,071 | 332,960 | (25,889) | (7.8) |) |
| Leasing and other | 74,753 | 70,589 | 4,164 | 5.9 | |
| Total | \$11,965,704 | \$11,883,019 | \$82,685 | 0.7 | % |

Loan demand has remained somewhat weak due to continued slow economic growth. Moderate loan growth in the Corporation's Pennsylvania market has been largely offset by decreases in the New Jersey, Virginia and Maryland

markets.

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Geographically, the \$204.4 million, or 4.6%, increase in commercial mortgages was throughout all of the Corporation's markets, with increases in Pennsylvania (\$142.8 million, or 6.1%), Maryland (\$28.3 million, or 7.2%), Virginia (\$17.3 million, or 5.2%), Delaware (\$11.0 million, or 8.4%) and New Jersey (\$5.0 million, or 0.4%). Largely offsetting the growth in commercial mortgages was a \$159.9 million, or 4.3%, decrease in commercial loans, driven largely by business customers remaining conservative, avoiding additional debt and postponing significant spending until economic indicators are more stable. Geographically, the decrease was in the Corporation's Virginia (\$73.0 million, or 28.8%), New Jersey (\$47.1 million, or 8.4%), Maryland (\$30.8 million, or 9.2%) and Pennsylvania (\$15.2 million, or 0.6%) markets.

The \$156.0 million, or 15.2%, increase in residential mortgages was largely due to the Corporation's retention in portfolio of certain 10 and 15 year fixed rate mortgages and certain adjustable rate mortgages, originated primarily during the fourth quarter of 2011 and first quarter of 2012.

Geographically, the \$72.4 million, or 10.2%, decline in construction loans occurred in the Corporation's Maryland (\$39.7 million, or 31.0%), New Jersey (\$24.6 million, or 21.2%), and Virginia (\$21.5 million, or 14.0%) markets, partially offset by an increase in the Pennsylvania (\$14.6 million, or 5.0%) market, which is the result of several owner-occupied construction projects.

The average yield on loans decreased 28 basis points, or 5.5%, from 5.13% in 2011 to 4.85% in 2012. The decrease in average yields on loans was attributable to increased refinancing activity, repayments of higher-yielding loans and new loan production at significantly lower rates, due in part, to competitive pressures in obtaining high quality credits. Interest expense decreased \$7.8 million, or 22.8%, to \$26.5 million in the second quarter of 2012 from \$34.3 million in the second quarter of 2011. Interest expense decreased \$4.8 million due to a 26 basis point, or 21.8%, decrease in the average cost of total interest-bearing liabilities. Interest expense decreased an additional \$3.0 million as a result of an \$84.2 million, or 0.7%, decline in average interest-bearing liabilities.

Average deposits, by type, are summarized in the following table:

| | Three months ended | | Increase (decrease) | | |
|----------------------------|------------------------|--------------|---------------------|--------|----|
| | 2012 | 2011 | \$ | % | |
| | (dollars in thousands) | | | | |
| Noninterest-bearing demand | \$2,669,152 | \$2,362,614 | \$306,538 | 13.0 | % |
| Interest-bearing demand | 2,484,730 | 2,352,961 | 131,769 | 5.6 | |
| Savings | 3,292,620 | 3,356,361 | (63,741) | (1.9) |) |
| Total demand and savings | 8,446,502 | 8,071,936 | 374,566 | 4.6 | |
| Time deposits | 3,791,362 | 4,353,352 | (561,990) | (12.9) |) |
| Total deposits | \$12,237,864 | \$12,425,288 | \$(187,424) | (1.5) |)% |

Total demand and savings accounts increased \$374.6 million, or 4.6%, primarily due to increased promotional efforts by the Corporation. The increase in noninterest-bearing account balances was primarily due to a \$253.5 million, or 15.4%, increase in business account balances. Also contributing to the increase was a \$43.7 million, or 7.3%, increase in personal account balances. The \$131.8 million, or 5.6%, increase in interest-bearing demand account balances was largely due to a \$108.0 million, or 7.9%, increase in personal account balances, a result of customers' migration away from certificates of deposit. Also contributing to the increase was a \$32.8 million, or 39.4%, increase in business account balances. The \$63.7 million, or 1.9%, decrease in savings account balances was due to a \$27.9 million, or 4.8%, decrease in municipal account balances, a \$24.7 million, or 3.1%, decrease in business account balances and an \$11.1 million, or 0.6%, decrease in personal account balances.

The decrease in time deposits was almost entirely due to customer certificates of deposit, which decreased \$556.3 million, or 12.8%, with the remaining \$5.7 million decrease realized in brokered certificates of deposit. The decrease in customer certificates of deposit was in accounts with original maturity terms of less than three years (\$543.1 million, or 17.1%) and jumbo certificates of deposit (\$59.3 million, or 26.4%), partially offset by increases in longer-term certificates of deposit with original maturity terms of greater than three years. As noted above, the decrease in customer certificates of deposit was due to customers migrating funds to interest-bearing demand accounts in the current low interest rate environment.

The average cost of interest-bearing deposits decreased 25 basis points, or 28.7%, from 0.87% in 2011 to 0.62% in 2012 due to a reduction in rates paid on interest-bearing demand and savings deposits and the repricing of time deposits to lower rates. Since July 1, 2011, excluding early redemptions, approximately \$3.2 billion of time deposits matured at a weighted average rate of 0.96%, while approximately \$2.9 billion of time deposits were issued at a weighted average rate of 0.52%.

The following table summarizes changes in average short-term and long-term borrowings, by type:

| | Three months ended | | Increase (decrease) | | |
|--------------------------------------|------------------------|-------------|---------------------|--------|---|
| | June 30 | | | | |
| | 2012 | 2011 | \$ | % | |
| | (dollars in thousands) | | | | |
| Short-term borrowings: | | | | | |
| Customer repurchase agreements | \$226,216 | \$217,657 | \$8,559 | 3.9 | % |
| Customer short-term promissory notes | 146,307 | 171,958 | (25,651) | (14.9) |) |
| Total short-term customer funding | 372,523 | 389,615 | (17,092) | (4.4) |) |
| Federal funds purchased and other | 589,377 | 66,216 | 523,161 | 790.1 | |
| Total short-term borrowings | 961,900 | 455,831 | 506,069 | 111.0 | |
| Long-term debt: | | | | | |
| FHLB advances | 559,780 | 641,851 | (82,071) | (12.8) |) |
| Other long-term debt | 369,538 | 383,786 | (14,248) | (3.7) |) |
| Total long-term debt | 929,318 | 1,025,637 | (96,319) | (9.4) |) |
| Total | \$1,891,218 | \$1,481,468 | \$409,750 | 27.7 | % |

The \$17.1 million, or 4.4%, decrease in short-term customer funding was primarily due to customers transferring funds from the non-deposit cash management program into deposit products due to the low interest rate environment. The \$523.2 million increase in Federal funds purchased and other short-term borrowings was a result of the Corporation's purchase of investment securities during the first half of 2012 and the decrease in average deposits. The \$82.1 million, or 12.8%, decrease in FHLB advances was due to maturities, which were not replaced with new advances. The \$14.2 million, or 3.7%, decrease in other long-term debt was due to the call of certain junior subordinated deferrable interest debentures during the first half of 2012 and the fourth quarter of 2011.

Provision for Credit Losses and Allowance for Credit Losses

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

| | Three months ended | | |
|---|------------------------|--------------|---|
| | June 30 | | |
| | 2012 | 2011 | |
| | (dollars in thousands) | | |
| Loans, net of unearned income, outstanding at end of period | \$11,982,833 | \$11,852,491 | |
| Daily average balance of loans, net of unearned income | \$11,965,704 | \$11,883,019 | |
| | | | |
| Balance of allowance for credit losses at beginning of period | \$258,137 | \$271,156 | |
| Loans charged off: | | | |
| Real estate – commercial mortgage | 23,699 | 7,074 | |
| Commercial – industrial, financial and agricultural | 13,017 | 15,406 | |
| Real estate – construction | 8,442 | 7,468 | |
| Real estate – home equity | 2,789 | 1,650 | |
| Real estate – residential mortgage | 1,492 | 7,707 | |
| Consumer | 471 | 681 | |
| Leasing and other | 630 | 689 | |
| Total loans charged off | 50,540 | 40,675 | |
| Recoveries of loans previously charged off: | | | |
| Real estate – commercial mortgage | 1,153 | 191 | |
| Commercial – industrial, financial and agricultural | 717 | 1,003 | |
| Real estate – construction | 1,539 | 79 | |
| Real estate – home equity | 278 | 2 | |
| Real estate – residential mortgage | 71 | 190 | |
| Consumer | 281 | 433 | |
| Leasing and other | 180 | 254 | |
| Total recoveries | 4,219 | 2,152 | |
| Net loans charged off | 46,321 | 38,523 | |
| Provision for credit losses | 25,500 | 36,000 | |
| Balance of allowance for credit losses at end of period | \$237,316 | \$268,633 | |
| Components of the Allowance for Credit Losses: | | | |
| Allowance for loan losses | \$235,737 | \$266,683 | |
| Reserve for unfunded lending commitments | 1,579 | 1,950 | |
| Allowance for credit losses | \$237,316 | \$268,633 | |
| Selected Ratios: | | | |
| Net charge-offs to average loans (annualized) | 1.55 | % 1.30 | % |
| Allowance for credit losses to loans outstanding | 1.98 | % 2.27 | % |

The provision for credit losses was \$25.5 million for the second quarter of 2012, a decrease of \$10.5 million, or 29.2%, from the second quarter of 2011. The decrease in the provision for credit losses was due to the continuing improvement in the Corporation's credit quality metrics, including a reduction in the level of non-performing loans and overall delinquency.

As previously noted, in June 2012, the Corporation sold \$44.1 million of non-accrual commercial mortgage, commercial and construction loans to an investor, resulting in a total increase to charge-offs of \$21.2 million during the second quarter of 2012. Because the existing allowance for credit loss on the loans sold exceeded the charge-off amount, no additional provision for credit losses was required. Below is a summary of the transaction:

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

Existing allocation for credit losses on sold loans \$(15,090) \$(7,510) \$(1,520) \$(24,120)
 Net charge-offs increased \$7.8 million, or 20.2%, to \$46.3 million for the second quarter of 2012 compared to \$38.5 million for the second quarter of 2011. The increase in net charge-offs was due to increases in commercial mortgage net charge-offs (\$15.7 million, or 227.6%), partially offset by decreases in residential mortgage net charge-offs (\$6.1 million, or 81.1%) and commercial loan net charge-offs (\$2.1 million, or 14.6%).

Of the \$46.3 million of net charge-offs recorded in the second quarter of 2012, 43.1% were for loans originated in New Jersey, 31.6% in Pennsylvania, 12.3% in Virginia and 10.1% in Maryland. Charge-offs for the second quarter of 2012 included three individual charge-offs of \$1.0 million or greater, totaling \$8.0 million, of which \$4.4 million were construction loans and \$3.6 million was a commercial mortgage.

The following table summarizes non-performing assets as of the indicated dates:

| | June 30, 2012 | December 31, 2011 | June 30, 2011 | |
|---|------------------------|----------------------|---------------|---|
| | (dollars in thousands) | | | |
| Non-accrual loans | \$203,539 | \$257,761 | \$274,973 | |
| Loans 90 days past due and accruing | 30,434 | 28,767 | 35,869 | |
| Total non-performing loans | 233,973 | 286,528 | 310,842 | |
| Other real estate owned (OREO) | 32,338 | 30,803 | 37,493 | |
| Total non-performing assets | \$266,311 | \$317,331 | \$348,335 | |
| Non-accrual loans to total loans | 1.70 | % 2.15 | % 2.32 | % |
| Non-performing assets to total assets | 1.63 | % 1.94 | % 2.18 | % |
| Allowance for credit losses to non-performing loans | 101.43 | % 90.11 | % 86.42 | % |
| Non-performing assets to tangible common shareholders' equity and allowance for credit losses | 15.34 | % 18.60 | % 20.78 | % |

The following table summarizes non-performing loans, by type, as of the indicated dates:

| | June 30, 2012 | December 31, 2011 | June 30, 2011 |
|---|----------------|----------------------|---------------|
| | (in thousands) | | |
| Real estate – commercial mortgage | \$82,179 | \$113,806 | \$102,724 |
| Commercial – industrial, financial and agricultural | 67,969 | 80,944 | 94,855 |
| Real estate – construction | 43,124 | 60,744 | 58,381 |
| Real estate – residential mortgage | 25,373 | 16,336 | 43,200 |
| Real estate – home equity | 11,472 | 11,207 | 9,440 |
| Consumer | 3,460 | 3,384 | 2,090 |
| Leasing | 396 | 107 | 152 |
| Total non-performing loans | \$233,973 | \$286,528 | \$310,842 |

Non-performing loans decreased to \$234.0 million at June 30, 2012, from \$310.8 million at June 30, 2011. The \$76.9 million, or 24.7%, decrease was due to a \$26.9 million, or 28.3%, decrease in non-performing commercial loans, a \$20.5 million, or 20.0%, decrease in non-performing commercial mortgages and a \$15.3 million, or 26.1%, decrease in non-performing construction loans. The decreases in these loan types were largely due to the aforementioned loan sale in June 2012, as well as normal charge-offs and repayments. Also contributing to the decrease in non-performing loans was a \$17.8 million, or 41.3%, decrease in non-performing residential mortgages, which was due to the sale of \$34.7 million of non-performing residential mortgages in December 2011, partially offset by additions during the first half of 2012.

Geographically, the \$26.9 million decrease in non-performing commercial loans was primarily due to decreases in the Pennsylvania (\$11.9 million, or 21.4%), Virginia (\$8.0 million, or 68.1%) and Maryland (\$4.6 million, 45.5%) markets.

Geographically, the \$20.5 million decrease in non-performing commercial mortgages was due to decreases in the Pennsylvania (\$10.4 million, or 27.5%) and New Jersey (\$16.0 million, or 33.7%) markets, partially offset by an increase in the Maryland (\$9.1 million, or 134.9%) market.

Geographically, the decrease in non-performing construction loans was primarily in the Virginia (\$12.6 million, or 57.5%) and Maryland (\$6.1 million, or 36.0%) markets, partially offset by an increase in the Pennsylvania (\$5.3 million, or 104.5%) market.

The following table presents accruing loans whose terms have been modified under troubled debt restructurings (TDRs), by type, as of the indicated dates:

| | June 30, 2012 | December 31, 2011 | June 30, 2011 |
|---|----------------|----------------------|---------------|
| | (in thousands) | | |
| Real estate – residential mortgage | \$33,516 | \$32,331 | \$37,006 |
| Real estate – commercial mortgage | 32,481 | 22,425 | 30,735 |
| Real estate – construction | 10,030 | 7,645 | 5,589 |
| Commercial – industrial, financial and agricultural | 4,806 | 3,581 | 3,055 |
| Consumer and home equity | 620 | 193 | 258 |
| Total accruing TDRs | \$81,453 | \$66,175 | \$76,643 |

The following table summarizes the Corporation's OREO, by property type, as of the indicated dates:

| | June 30, 2012 | December 31, 2011 | June 30, 2011 |
|------------------------|----------------|----------------------|---------------|
| | (in thousands) | | |
| Commercial properties | \$16,730 | \$15,184 | \$17,033 |
| Residential properties | 9,680 | 10,499 | 15,881 |
| Undeveloped land | 5,928 | 5,120 | 4,579 |
| Total OREO | \$32,338 | \$30,803 | \$37,493 |

The following table summarizes loan delinquency rates, by type, as of June 30:

| | 2012 | | | 2011 | | | |
|---|---------------|------------------|-----------|---------------|------------------|-----------|---|
| | 31-89 Days | > 90 Days (1) | Total | 31-89 Days | > 90 Days (1) | Total | |
| Real estate – commercial mortgage | 0.41 | % 1.78 | % 2.19 | % 0.57 | % 2.32 | % 2.89 | % |
| Commercial – industrial, financial and agricultural | 0.66 | % 1.91 | % 2.57 | % 0.54 | % 2.58 | % 3.12 | % |
| Real estate – construction | 0.95 | % 6.96 | % 7.91 | % 0.62 | % 8.56 | % 9.18 | % |
| Real estate – residential mortgage | 2.94 | % 2.15 | % 5.09 | % 3.37 | % 4.22 | % 7.59 | % |
| Real estate – home equity | 0.83 | % 0.71 | % 1.54 | % 0.74 | % 0.58 | % 1.32 | % |
| Consumer, leasing and other | 1.61 | % 0.99 | % 2.60 | % 1.22 | % 0.56 | % 1.78 | % |
| Total | 0.86 | % 1.95 | % 2.81 | % 0.85 | % 2.63 | % 3.48 | % |
| Total dollars (in thousands) | \$102,688 | \$233,973 | \$336,661 | \$101,213 | \$310,842 | \$412,055 | |

(1)Includes non-accrual loans.

The Corporation believes that the allowance for credit losses of \$237.3 million as of June 30, 2012 is sufficient to cover losses inherent in both the loan portfolio and the unfunded lending commitments as of that date and is appropriate based on applicable accounting standards.

Non-Interest Income

The following table presents the components of non-interest income:

| | Three months ended June 30 | | Increase (decrease) | | |
|-------------------------------------|-------------------------------|---------|---------------------|------|---|
| | 2012 | 2011 | \$ | % | |
| | (dollars in thousands) | | | | |
| Overdraft fees | \$8,095 | \$8,029 | \$66 | 0.8 | % |
| Cash management fees | 2,816 | 2,677 | 139 | 5.2 | |
| Other | 4,456 | 3,626 | 830 | 22.9 | |
| Service charges on deposit accounts | 15,367 | 14,332 | 1,035 | 7.2 | |
| Merchant fees | 3,376 | 2,516 | 860 | 34.2 | |
| Foreign currency processing income | | | | | |