FIRST CITIZENS BANCSHARES INC /DE/
Form 10-Q
August 06, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended June 30, 2010

or

¨ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
Commission File Number: 001-16715

First Citizens BancShares, Inc.

(Exact name of Registrant as specified in its charter)

Delaware	**56-1528994**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**
4300 Six Forks Road, Raleigh, North Carolina	**27609**
(Address of principle executive offices)	**(Zip code)**

(919) 716-7000

(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 twelve 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 ninety days. Yes x 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 such shorter period that the Registrant was required to submit and post such files) Yes x 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. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act:

Large accelerated filer x	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 x

Class A Common Stock $1 Par Value 8,756,778 shares

Class B Common Stock $1 Par Value 1,677,675 shares

(Number of shares outstanding, by class, as of August 6, 2010)

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Part 1

Item 1. Financial Statements (Unaudited)

First Citizens BancShares, Inc. and Subsidiaries

Consolidated Balance Sheets

Unaudited

	June 30* 2010	December 31# 2009	June 30* 2009
	(thousands, except share data)		
Assets			
Cash and due from banks	**$ 625,857**	$ 480,242	$ 637,896
Overnight investments	**736,896**	723,260	229,668
Investment securities available for sale	**3,768,777**	2,929,162	3,745,385
Investment securities held to maturity	**3,084**	3,603	4,140
Loans held for sale	**91,076**	67,381	115,920
Loans and leases:			
Covered by loss share agreements	**2,367,090**	1,173,020	0
Not covered by loss share agreements	**11,622,494**	11,644,999	11,523,045
Less allowance for loan and lease losses	**188,169**	172,282	162,282
Net loans and leases	**13,801,415**	12,645,737	11,360,763
Premises and equipment	**846,702**	837,082	821,219
Other real estate owned:			
Covered by loss share agreements	**98,416**	93,774	0
Not covered by loss share agreements	**46,763**	40,607	33,301
Income earned not collected	**77,186**	60,684	66,226
Receivable from FDIC for loss share agreements	**692,242**	249,842	0
Goodwill	**102,625**	102,625	102,625
Other intangible assets	**12,936**	6,361	3,035
Other assets	**201,794**	225,703	197,702
Total assets	**$ 21,105,769**	$ 18,466,063	$ 17,317,880
Liabilities			
Deposits:			
Noninterest-bearing	**$ 3,730,321**	$ 3,215,414	$ 2,974,494
Interest-bearing	**14,056,920**	12,122,153	11,383,655
Total deposits	**17,787,241**	15,337,567	14,358,149
Short-term borrowings	**541,709**	642,405	599,853
Long-term obligations	**918,930**	797,366	735,803
Other liabilities	**164,580**	129,610	189,862
Total liabilities	**19,412,460**	16,906,948	15,883,667
Shareholders Equity			
Common stock:			
Class A - $1 par value (8,756,778 shares issued for all periods)	**8,757**	8,757	8,757
Class B - $1 par value (1,677,675 shares issued for all periods)	**1,678**	1,678	1,678
Surplus	**143,766**	143,766	143,766

Retained earnings	**1,561,665**	1,429,863	1,334,655
Accumulated other comprehensive income (loss)	**(22,557)**	(24,949)	(54,643)
Total shareholders equity	**1,693,309**	1,559,115	1,434,213
Total liabilities and shareholders equity	**$ 21,105,769**	$ 18,466,063	$ 17,317,880

* Unaudited

\# Derived from the 2009 Annual Report on Form 10-K.

See accompanying Notes to Consolidated Financial Statements.

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First Citizens BancShares, Inc. and Subsidiaries

Consolidated Statements of Income

Unaudited

	Three Months Ended June 30		Six Months Ended June 30	
	2010	2009	2010	2009
	(thousands, except share and per share data)			
Interest income				
Loans and leases	$ 202,541	$ 155,449	$ 389,615	$ 312,033
Investment securities:				
U. S. Government	10,250	18,118	19,601	39,277
Residential mortgage backed securities	1,873	1,234	3,437	2,382
Corporate bonds	2,198	1,580	4,333	1,858
State, county and municipal	15	104	48	155
Other	12	164	82	371
Total investment securities interest and dividend income	14,348	21,200	27,501	44,043
Overnight investments	546	192	1,019	417
Total interest income	217,435	176,841	418,135	356,493
Interest expense				
Deposits	41,091	48,890	79,207	101,836
Short-term borrowings	640	1,281	1,396	2,602
Long-term obligations	10,842	9,638	21,634	19,218
Total interest expense	52,573	59,809	102,237	123,656
Net interest income	164,862	117,032	315,898	232,837
Provision for loan and lease losses	31,826	20,759	48,756	39,482
Net interest income after provision for loan and lease losses	133,036	96,273	267,142	193,355
Noninterest income				
Gain on acquisitions	0	0	132,623	0
Cardholder and merchant services	28,505	24,107	52,294	45,599
Service charges on deposit accounts	19,513	19,163	38,340	37,014
Wealth management services	14,222	11,481	25,956	22,253
Fees from processing services	7,226	7,136	14,449	14,688
Securities (losses) gains	(186)	(139)	945	(139)
Other service charges and fees	5,110	4,068	9,758	8,417
Mortgage income	1,924	2,369	3,334	5,821
Insurance commissions	1,794	1,825	4,600	4,295
ATM income	1,699	1,772	3,354	3,501
Adjustments to FDIC receivable for loss share agreements	12,713	0	15,452	0
Other	102	(366)	89	(341)
Total noninterest income	92,622	71,416	301,194	141,108
Noninterest expense				
Salaries and wages	74,475	63,751	146,635	129,297
Employee benefits	15,839	15,773	34,150	33,092
Occupancy expense	18,517	15,970	36,353	31,376
Equipment expense	16,604	14,749	32,419	29,472
FDIC deposit insurance	6,609	13,763	11,496	17,949

Foreclosure-related expenses		4,014		1,785		8,075		3,422
Other		45,718		33,329		85,598		69,005
Total noninterest expense		181,776		159,120		354,726		313,613
Income before income taxes		43,882		8,569		213,610		20,850
Income taxes		15,280		2,369		80,452		5,987
Net income	$	28,602	$	6,200	$	133,158	$	14,863
Average shares outstanding		10,434,453		10,434,453		10,434,453		10,434,453
Net income per share	$	2.74	$	0.59	$	12.76	$	1.42

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First Citizens BancShares, Inc. and Subsidiaries

Consolidated Statements of Changes in Shareholders Equity

Unaudited

	Class A Common Stock	Class B Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Income (loss)	Total Shareholders Equity
	(thousands, except share and per share data)					
Balance at December 31, 2008	$ 8,757	$ 1,678	$ 143,766	$ 1,326,054	$ (36,880)	$ 1,443,375
Comprehensive loss:						
Net income	0	0	0	14,863	0	14,863
Change in unrealized securities gains arising during period, net of $13,108 deferred tax benefit	0	0	0	0	(20,322)	(20,322)
Change in unrecognized loss on cash flow hedge, net of $1,670 deferred tax	0	0	0	0	2,559	2,559
Total comprehensive loss						(2,900)
Cash dividends of $0.60 per share	0	0	0	(6,262)	0	(6,262)
Balance at June 30, 2009	$ 8,757	$ 1,678	$ 143,766	$ 1,334,655	$ (54,643)	$ 1,434,213
Balance at December 31, 2009	$ 8,757	$ 1,678	$ 143,766	$ 1,429,863	$ (24,949)	$ 1,559,115
Adjustment resulting from adoption of change in accounting for QSPEs and controlling financial interests effective January 1, 2010				4,904		$ 4,904
Comprehensive income:						
Net income	0	0	0	133,158	0	133,158
Change in unrealized securities gains arising during period, net of $2,238 deferred tax	0	0	0	0	5,988	5,988
Change in unrecognized loss on cash flow hedge, net of $2,346 deferred tax benefit	0	0	0	0	(3,596)	(3,596)
Total comprehensive income						135,550
Cash dividends of $0.60 per share	0	0	0	(6,260)	0	(6,260)
Balance at June 30, 2010	$ 8,757	$ 1,678	$ 143,766	$ 1,561,665	$ (22,557)	$ 1,693,309

At June 30, 2010, Accumulated Other Comprehensive Loss includes on an after-tax basis $27,418 in unrealized gains on investment securities available for sale, $43,131 in unrealized losses resulting from the funded status of the defined benefit plan and an unrealized loss of $6,844 on cash flow hedges.

At June 30, 2009, Accumulated Other Comprehensive Income includes on an after-tax basis $25,069 in unrealized gains on investment securities available for sale, $75,815 in unrealized losses resulting from the funded status of the defined benefit plan and an unrealized loss of $3,897 on cash flow hedges.

See accompanying Notes to Consolidated Financial Statements.

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Consolidated Statements of Cash Flows

First Citizens BancShares, Inc. and Subsidiaries

	For the six months ended June 30 2010	2009
OPERATING ACTIVITIES		
Net income	$ 133,158	$ 14,863
Adjustments to reconcile net income to cash provided by operating activities:		
Amortization of intangibles	3,164	869
Provision for loan and lease losses	48,756	39,482
Deferred tax (benefit) expense	(35,427)	8,589
Change in current taxes payable	13,899	(3,825)
Depreciation	30,296	27,816
Change in accrued interest payable	2,771	8,884
Change in income earned not collected	(8,842)	5,803
Gain on acquisitions	(132,623)	0
Securities losses (gains)	(945)	139
Origination of loans held for sale	(255,495)	(483,656)
Proceeds from sale of loans held for sale	235,171	442,659
Gain on sale of loans held for sale	(3,371)	(5,524)
Proceeds from sale of other real estate	40,943	14,836
Loss on sale of other real estate	720	2,126
Net amortization of premiums and discounts	21,550	19,507
Receivable from FDIC for loss share agreements	67,552	0
Net change in other assets	46,361	(12,174)
Net change in other liabilities	46,492	(19,332)
Net cash provided by operating activities	254,130	61,062
INVESTING ACTIVITIES		
Net change in loans and leases outstanding	307,745	71,765
Purchases of investment securities available for sale	(1,603,861)	(1,293,856)
Proceeds from maturities of investment securities held to maturity	518	1,808
Proceeds from maturities of investment securities available for sale	797,949	715,300
Proceeds from sales of investment securities available for sale	24,137	0
Net change in overnight investments	(13,636)	(55,052)
Additions to premises and equipment	(39,916)	(50,126)
Net cash received from acquisitions	106,489	0
Net cash used by investing activities	(420,575)	(610,161)
FINANCING ACTIVITIES		
Net change in time deposits	86,680	(53,721)
Net change in demand and other interest-bearing deposits	655,263	698,107
Net change in short-term borrowings	(505,105)	(47,501)
Origination of long-term obligations	81,482	2,997
Cash dividends paid	(6,260)	(6,262)
Net cash provided by financing activities	312,060	593,620
Change in cash and due from banks	145,615	44,521
Cash and due from banks at beginning of period	480,242	593,375

Cash and due from banks at end of period	$ 625,857	$ 637,896
CASH PAYMENTS FOR:		
Interest	$ 99,466	$ 114,772
Income taxes	46,041	17,516
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING ACTIVITIES:		
Unrealized securities gains (losses)	$ 8,226	$ (33,430)
Unrealized (loss) gain on cash flow hedge	(5,942)	4,229
Transfers of loans to other real estate	55,559	20,307
Acquisitions:		
Assets acquired	2,288,282	0
Liabilities assumed	(2,155,861)	0
Net assets acquired	132,421	0

See accompanying Notes to Consolidated Financial Statements

First Citizens BancShares, Inc. and Subsidiaries

Notes to Unaudited Consolidated Financial Statements

(Dollars in thousands, except per share amounts)

Note A

Accounting Policies and Other Matters

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (US GAAP) for interim financial information. Accordingly, they do not include all of the information and notes required by US GAAP for complete financial statements.

In the opinion of management, the consolidated financial statements contain all material adjustments necessary to present fairly the financial position of First Citizens BancShares, Inc. and Subsidiaries (BancShares) as of and for each of the periods presented, and all such adjustments are of a normal recurring nature. The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent liabilities at the date of the financial statements and the reported amounts of income and expenses during the period. Actual results could differ from those estimates.

Management has evaluated subsequent events through the filing date of the Quarterly Report on Form 10-Q.

These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in BancShares 2009 Form 10-K. Certain amounts for prior periods have been reclassified to conform with statement presentations for 2010. However, the reclassifications have no effect on shareholders equity or net income as previously reported.

FDIC-Assisted Transactions

US GAAP requires that the acquisition method of accounting be used for all business combinations, including those resulting from FDIC-assisted transactions and that an acquirer be identified for each business combination. Under US GAAP, the acquirer is the entity that obtains control of one or more businesses in the business combination, and the acquisition date is the date the acquirer achieves control. US GAAP requires that the acquirer recognize the fair value of assets acquired, liabilities assumed, and any noncontrolling interest in the acquiree at the acquisition date. In addition, acquisition-related costs and restructuring costs are recognized as period expenses as incurred.

During 2010 and 2009, BancShares wholly-owned subsidiary First-Citizens Bank & Trust Company (FCB) acquired assets and assumed liabilities of four entities as noted below (collectively referred to as the Acquisitions) with the assistance of the Federal Deposit Insurance Corporation (FDIC), which had been appointed Receiver of each entity by its respective state banking authority.

Name of entity	Headquarters location	Date of transaction
Sun American Bank (SAB)	Boca Raton, Florida	March 5, 2010
First Regional Bank (First Regional)	Los Angeles, California	January 29, 2010
Venture Bank (VB)	Lacey, Washington	September 11, 2009
Temecula Valley Bank (TVB)	Temecula, California	July 17, 2009

The acquired assets and assumed liabilities were measured at estimated fair value. Management made significant estimates and exercised significant judgment in accounting for the Acquisitions. Management judgmentally assigned risk ratings to loans based on credit quality, appraisals and estimated collateral values, estimated expected cash flows, and applied appropriate liquidity and coupon discounts to measure fair values for loans. Other real estate acquired through foreclosure was valued based upon pending sales contracts and appraised values, adjusted for current market conditions. FCB also recorded identifiable intangible assets representing the estimated values of the assumed core deposits and other customer relationships. Management used quoted or current market prices to determine the fair value of investment securities, short-term borrowings and long-term obligations.

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Loans and Leases

Loans and leases that are held for investment purposes are carried at the principal amount outstanding. Loans that are classified as held for sale are carried at the lower of aggregate cost or fair value. Interest on substantially all loans is accrued and credited to interest income on a constant yield basis based upon the daily principal amount outstanding.

Acquired loans are recorded at fair value at the date of acquisition. The fair values of acquired loans with evidence of credit deterioration since origination (impaired loans) are recorded net of a nonaccretable difference and, if appropriate, an accretable yield. The difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition is the nonaccretable difference, which is included in the carrying amount of acquired loans. Subsequent decreases to the expected cash flows will generally result in a provision for credit losses. Subsequent increases in expected cash flows result in either a reversal of the provision for credit losses to the extent of prior charges, or a reclassification of the difference from nonaccretable to accretable with a positive impact on the accretable yield. Any excess of cash flows expected at acquisition over the estimated fair value is referred to as the accretable yield and is recognized in interest income over the remaining life of the loan when there is a reasonable expectation regarding the amount and timing of such cash flows. BancShares did not estimate the amount and timing of cash flows for impaired loans acquired from TVB and VB, but cash flow analyses were performed on all loans deemed impaired that were acquired from First Regional and SAB in order to determine the cash flows expected to be collected.

Receivable from FDIC for Loss Share Agreements

The receivable from the FDIC for loss share agreements is measured separately from the related covered assets as it is not contractually embedded in the assets and is not transferable should the assets be sold. Fair value was estimated using projected cash flows related to the loss share agreements based on the expected reimbursements for losses using the applicable loss share percentages and the estimated true-up payment at the expiration of the loss share agreements, if applicable. These cash flows were discounted to reflect the estimated timing of the receipt of the loss share reimbursement from the FDIC and the true-up payment to the FDIC, when applicable. The FDIC receivable has been reviewed and updated prospectively as loss estimates related to covered loans and other real estate owned change and as reimbursements are received from the FDIC.

Other Real Estate Owned Covered by Loss Share Agreements

Other real estate owned (OREO) covered by loss share agreements with the FDIC are reported exclusive of expected reimbursement cash flows from the FDIC. Subsequent downward adjustments to the estimated recoverable value of covered OREO result in a reduction of covered OREO, a charge to other expense and an increase in the FDIC receivable for the estimated amount to be reimbursed, with a corresponding amount recorded as other noninterest income. OREO is presented at the estimated present value that management expects to receive when the property is sold, net of related costs of disposal. Management used appraisals of properties to determine fair values and applied additional discounts where appropriate for passage of time or, in certain cases, for subsequent events occurring after the appraisal date.

Recently Adopted Accounting Policies and Other Regulatory Issues

Under revisions to US GAAP that became effective January 1, 2010, the concept of a qualifying special-purpose entity (QSPE) was removed, resulting in a change in the accounting for QSPEs that were previously exempt. Further changes required evaluation of variable interests to determine whether a controlling financial interest exists. Upon adoption, the off-balance sheet accounting treatment for the 2005 asset securitization of home equity loans was discontinued, and the loans that were sold in the securitization and the corresponding debt obligations were reported on the consolidated balance sheet in the first quarter of 2010. The adoption resulted in increases of $97,291 in noncovered revolving mortgage loans, $681 in allowance for loan and lease losses, $86,926 in long-term obligations, and $3,189 in deferred tax liabilities. The retained interest in the residual interest strip and the servicing asset were written off, resulting in reductions of $1,287 and $304 to investment securities available for sale and other assets, respectively. The adoption also resulted in an adjustment to the beginning balance of retained earnings in the amount of $4,904.

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Note B

Federally Assisted Acquisitions of First Regional Bank and Sun American Bank

On January 29, 2010, FCB purchased substantially all the assets and assumed substantially all the liabilities of First Regional from the FDIC, as Receiver. First Regional operated through 8 offices in the state of California, primarily serving Southern California. The FDIC took First Regional under receivership upon its closure by the California Department of Financial Institutions. FCB s bid to the FDIC included the purchase of substantially all of First Regional s assets at a discount of $299,400 in exchange for assuming certain First Regional deposits and certain other liabilities. No cash, deposit premium or other consideration was paid by FCB. FCB and the FDIC entered into loss share agreements regarding future losses incurred on loans and other real estate acquired through foreclosure existing at the acquisition date. Under the terms of the loss share agreements, there is no reimbursement by the FDIC until net losses reach $41,815. The FDIC will reimburse FCB for 80 percent of net losses incurred up to $1,017,000, and 95 percent of net losses exceeding $1,017,000.

The Purchase and Assumption Agreement between FCB and the FDIC also includes a true-up payment at the end of year 10. On March 17, 2020, the true-up measurement date, FCB is required to make a true-up payment to the FDIC equal to 50 percent of the excess, if any, of (i) 20 percent of the stated threshold, or $203.4 million, less (ii) the sum of (a) 25 percent of the asset discount, or $74.9 million, plus (b) 25 percent of the cumulative loss share payments plus (c) the cumulative servicing amount. The cumulative servicing amount is 1 percent of the average covered assets for each year during the terms of the loss share agreements. Current projections suggest a true-up payment of $65,919 will be payable under the First Regional loss share agreements. This estimate is subject to change over the term of the agreements.

The term for loss share on residential real estate loans is ten years, while the term for loss share on non-residential real estate loans is five years in respect to losses and eight years in respect to loss recoveries. As a result of the loss share agreements with the FDIC and considering an estimate of a contingent true-up payment to the FDIC, FCB recorded a receivable of $365,170 at the time of acquisition. During the second quarter of 2010, adjustments were made to the FDIC receivable based on changes in loss estimates related to covered loans and other real estate owned that affect the respective acquisition date fair values. These adjustments were made retroactive to the first quarter of 2010 and increased the receivable by $24,391.

On March 5, 2010, FCB purchased substantially all the assets and assumed substantially all the liabilities of SAB from the FDIC, as Receiver. SAB operated 12 offices in the state of Florida, primarily serving South Florida. The FDIC took SAB under receivership upon its closure by the Florida Office of Financial Regulation. FCB s bid to the FDIC included the purchase of substantially all of SAB s assets at a discount of $69,400 in exchange for assuming certain SAB deposits and certain other liabilities. The FDIC paid FCB $31,965 in additional cash consideration at closing. FCB and the FDIC entered into loss share agreements regarding future losses incurred on loans and other real estate acquired through foreclosure existing at the acquisition date. Under the terms of the loss share agreements, the FDIC will reimburse FCB for 80 percent of net losses incurred up to $99,000 and 95 percent of net losses exceeding $99,000.

The Purchase and Assumption Agreement between FCB and the FDIC also includes a true-up payment at the end of year 10. On May 15, 2020, the true-up measurement date, FCB is required to make a true-up payment to the FDIC equal to 50 percent of the excess, if any, of (i) 20 percent of the stated threshold, or $19.8 million, less (ii) the sum of (a) 25 percent of the asset discount, or $17.5 million, plus (b) 25 percent of the cumulative loss share payments plus (c) the cumulative servicing amount. The cumulative servicing amount is 1 percent of the average covered assets for each year during the terms of the loss share agreements. Although no true-up payment is currently projected under the SAB loss share agreements, those projections are subject to change.

The term for loss share on residential real estate loans is ten years, while the term for loss share on non-residential real estate loans is five years in respect to losses and eight years in respect to loss recoveries. As a result of the loss share agreements with the FDIC, FCB recorded a receivable of $92,360 at the time of acquisition. During the second quarter of 2010, adjustments were made to the FDIC receivable based on changes in loss estimates related to covered loans and other real estate owned that affect the respective acquisition date fair values. These adjustments were made retroactive to the first quarter of 2010 and decreased the receivable by $2,626.

The acquisitions of First Regional and SAB were accounted for using the acquisition method of accounting. The statement of net assets acquired, adjustments to the acquisition date fair values made in the second quarter and the resulting bargain purchase gains are presented in the following tables. As indicated in the explanatory notes that accompany the following tables, the purchased assets, assumed liabilities and identifiable intangible assets were recorded at their respective acquisition date estimated fair values. Fair values are subject to refinement for up to one year after the closing date of each merger as additional information regarding closing date fair values becomes available. Adjustments to the estimated fair values made in the second quarter were based on additional information regarding the acquisition date fair values, which included updated appraisals on several commercial properties on acquired impaired loans and updated financial statements for some borrowers which allowed for adjustments to expected cash flows that more closely reflect the borrowers ability to repay the debt.

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First quarter noninterest income included bargain purchase gains of $137,447 that resulted from the 2010 Acquisitions. The gains resulted from the difference between the estimated fair values of acquired assets and assumed liabilities. During the second quarter of 2010, adjustments were made to the gains based on additional information regarding the respective acquisition date fair values, which reduced the gains by a net of $5,026. These adjustments were made retroactive to the first quarter of 2010, the period the 2010 acquisitions were consummated, resulting in an adjusted gain of $132,421. FCB recorded a deferred tax liability for the gains totaling $51,856. To the extent there are additional adjustments to the respective acquisition date fair values up to one year following the respective acquisitions, there will be additional adjustments to the gains.

The following tables identify the assets acquired and liabilities assumed by FCB from First Regional and SAB. The tables provide the balances recorded by First Regional and SAB at the time of the respective FDIC-assisted transactions, the fair value adjustments recorded and the resulting adjusted fair values recorded by FCB for the acquisition date.

First Regional Bank

Acquisition date: January 29, 2010

	As recorded by First Regional	Fair value adjustments at acquisition date	Subsequent acquisition-date adjustments	As recorded by FCB
		(thousands)		
Assets				
Cash and due from banks	$ 37,508	$	$	$ 37,508
Investment securities available for sale	3,250			3,250
Loans covered by loss share agreements	1,853,325	(576,171) a	(30,488) a	1,246,666
Other real estate owned covered by loss share agreements	61,488	(20,353) b	414 b	41,549
Income earned not collected	6,048			6,048
Receivable from FDIC for loss share agreements		365,170 c	24,391 c	389,561
Intangible assets		9,110 d		9,110
Other assets	23,782	(500) e		23,282
Total assets acquired	$ 1,985,401	$ (222,744)	$ (5,683)	$ 1,756,974
Liabilities				
Deposits:				
Noninterest-bearing	$ 528,235	$	$	$ 528,235
Interest-bearing	759,484			759,484
Total deposits	1,287,719			1,287,719
Short-term borrowings	361,876			361,876
Other liabilities	1,188	1,547 h		2,735
Total liabilities assumed	1,650,783	1,547		1,652,330
Excess of assets acquired over liabilities assumed	$ 334,618			
Aggregate fair value adjustments		$ (224,291)	$ (5,683)	
Gain on acquisition of First Regional				$ 104,644

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Sun American Bank

Acquisition date: March 5, 2010

	As recorded by SAB	Fair value adjustments at acquisition date	Subsequent acquisition-date adjustments	As recorded by FCB
		(thousands)		
Assets				
Cash and due from banks	$ 37,016	$	$	$ 37,016
Investment securities available for sale	66,968			66,968
Loans covered by loss share agreements	411,315	(123,707) a	3,283 a	290,891
Other real estate owned covered by loss share agreements	15,220	(7,200) b		8,020
Income earned not collected	1,612			1,612
Receivable from FDIC for loss share agreements		92,360 c	(2,626) c	89,734
Intangible assets		629 d		629
Other assets	4,473			4,473
Total assets acquired	$ 536,604	$ (37,918)	$ 657	$ 499,343
Liabilities				
Deposits:				
Noninterest-bearing	$ 39,435	$	$	$ 39,435
Interest-bearing	380,577			380,577
Total deposits	420,012			420,012
Short-term borrowings	42,485	48 f		42,533
Long-term obligations	37,000	3,082 g		40,082
Other liabilities	853	51 h		904
Total liabilities assumed	500,350	3,181		503,531
Excess of assets acquired over liabilities assumed	$ 36,254			
Aggregate fair value adjustments		$ (41,099)	$ 657	
Cash received from the FDIC				$ 31,965
Gain on acquisition of Sun American				$ 27,777

Explanation of fair value adjustments

a - Adjustment reflects the fair value adjustments based on FCB s evaluation of the acquired loan portfolio.

b - Adjustment reflects the estimated OREO losses based on FCB s evaluation of the acquired OREO portfolio.

c - Adjustment reflects the estimated fair value of payments FCB will receive from the FDIC under the loss share agreements.

d - Adjustment reflects the estimated value of intangible assets, which includes core deposit intangibles and when applicable, trust customer relationships.

e - Adjustment reflects the amount needed to adjust the carrying value of other assets to estimated fair value.

f - Adjustment arises since the rates on short-term borrowings are higher than rates available on similar borrowings at date of acquisition.

g - Adjustment arises since the rates on long-term obligations are higher than rates available on similar borrowings at date of acquisition.

h - Adjustment reflects amount needed to adjust the carrying value of other liabilities to estimated fair value.

Results of operations for First Regional and SAB prior to their respective acquisition dates are not included in the income statement.

Due to the significant amount of fair value adjustments, the resulting accretion of those fair value adjustments and the protection resulting from the FDIC loss share agreements, historical results of First Regional and SAB are not relevant to BancShares results of operations. Therefore, no pro forma information is presented.

Note C

Investments

The aggregate values of investment securities at June 30, 2010, December 31, 2009 and June 30, 2009, along with unrealized gains and losses determined on an individual security basis are as follows:

	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Investment securities available for sale				
June 30, 2010				
U. S. Government	$ 3,073,134	$ 11,606	$ 23	$ 3,084,717
Corporate bonds	480,738	8,845		489,583
Residential mortgage-backed securities	168,307	6,313	104	174,516
Equity securities	1,358	17,333		18,691
State, county and municipal	1,242	30	2	1,270
Total investment securities available for sale	$ 3,724,779	$ 44,127	$ 129	$ 3,768,777
December 31, 2009				
U. S. Government	$ 2,274,084	$ 14,005	$ 666	$ 2,287,423
Corporate bonds	481,341	4,326		485,667
Residential mortgage-backed securities	126,601	4,489	752	130,338
Equity securities	2,377	14,245		16,622
State, county and municipal	7,053	35	275	6,813
Other	1,937	362		2,299
Total investment securities available for sale	$ 2,893,393	$ 37,462	$ 1,693	$ 2,929,162
June 30, 2009				
U. S. Government	$ 3,144,025	$ 27,447	$ 1,589	$ 3,169,883
Corporate bonds	457,572	1,410	1,240	457,742
Residential mortgage-backed securities	95,181	2,052	512	96,721
Equity securities	2,862	12,071	336	14,597
State, county and municipal	1,600	26	9	1,617
Other	2,894	1,931		4,825
Total investment securities available for sale	$ 3,704,134	$ 44,937	$ 3,686	$ 3,745,385
Investment securities held to maturity				
June 30, 2010				
Residential mortgage-backed securities	$ 2,933	$ 276	$ 26	$ 3,183
State, county and municipal	151			151
Total investment securities held to maturity	$ 3,084	$ 276	$ 26	$ 3,334
December 31, 2009				
Residential mortgage-backed securities	$ 3,452	$ 230	$	$ 3,682
State, county and municipal	151	1		152
Total investment securities held to maturity	$ 3,603	$ 231	$	$ 3,834

June 30, 2009								
Residential mortgage-backed securities	$	3,988	$	266	$	27	$	4,227
State, county and municipal		152						152
Total investment securities held to maturity	$	4,140	$	266	$	27	$	4,379

Investments in corporate bonds represent debt securities issued by various financial institutions under the Temporary Liquidity Guarantee Program. These debt obligations were issued with the full faith and credit of the United States of America. The guarantee for these securities is triggered when an issuer defaults on a scheduled payment.

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The following table provides maturity information for investment securities as of the dates indicated. Callable securities are assumed to mature on their earliest call date.

	June 30, 2010		December 31, 2009		June 30, 2009	
	Cost	Fair Value	Cost	Fair Value	Cost	Fair Value
Investment securities available for sale						
Maturing in:						
One year or less	$ 2,342,011	$ 2,351,171	$ 1,544,063	$ 1,554,657	$ 1,616,772	$ 1,630,131
One through five years	1,220,914	1,232,535	1,226,202	1,233,604	1,986,438	1,999,122
Five through 10 years	1,912	1,946	1,943	2,201	3,623	5,561
Over 10 years	158,584	164,434	118,808	122,078	94,439	95,974
Equity securities	1,358	18,691	2,377	16,622	2,862	14,597
Total investment securities available for sale	$ 3,724,779	$ 3,768,777	$ 2,893,393	$ 2,929,162	$ 3,704,134	$ 3,745,385
Investment securities held to maturity						
Maturing in:						
One through five years	$ 151	$ 151	$ 151	$ 152	$ 152	$ 152
Five through 10 years	2,797	3,005	3,306	3,497	3,834	4,035
Over 10 years	136	178	146	185	154	192
Total investment securities held to maturity	$ 3,084	$ 3,334	$ 3,603	$ 3,834	$ 4,140	$ 4,379

The following table provides information regarding securities with unrealized losses as of June 30, 2010, December 31, 2009 and June 30, 2009:

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
June 30, 2010						
Investment securities available for sale:						
U.S. Government	$ 4,005	$ 23	$	$	$ 4,005	$ 23
Residential mortgage-backed securities	5,151	81	1,152	23	6,303	104
State, county and municipal			439	2	439	2
Total	$ 9,156	$ 104	$ 1,591	$ 25	$ 10,747	$ 129
Investment securities held to maturity:						
Residential mortgage-backed securities	$ 151		$ 28	$ 26	$ 179	$ 26
December 31, 2009						
Investment securities available for sale:						
U.S. Government	$ 250,600	$ 666	$	$	$ 250,600	$ 666
Residential mortgage-backed securities	25,608	621	2,434	131	28,042	752
State, county and municipal	5,476	271	439	4	5,915	275
Total	$ 281,684	$ 1,558	$ 2,873	$ 135	$ 284,557	$ 1,693
June 30, 2009						
Investment securities available for sale:						
U.S. Government	$ 622,984	$ 1,589	$	$	$ 622,984	$ 1,589
Corporate Bonds	177,515	1,240			177,515	1,240

Residential mortgage-backed securities	21,298	450	1,411	62	22,709	512
Equity securities	485	336			485	336
State, county and municipal	113	2	437	7	550	9
Total	$ 822,395	$ 3,617	$ 1,848	$ 69	$ 824,243	$ 3,686
Investment securities held to maturity:						
Residential mortgage-backed securities	$	$	$ 33	$ 27	$ 33	$ 27

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Investment securities with an aggregate fair value of $1,619 have had continuous unrealized losses for more than twelve months as of June 30, 2010 with an aggregate unrealized loss of $51. These 21 investments include residential mortgage-backed and state, county and municipal securities. None of the unrealized losses identified as of June 30, 2010 related to the marketability of the securities or the issuer s ability to honor redemption obligations. Consequently, the securities were not deemed to be other than temporarily impaired.

With respect to investment securities held to maturity, BancShares has the ability and intent to hold those securities until they mature.

For each period presented, securities gains (losses) include the following:

	Six months ended June 30, 2010	2009
Gross gains on sales of investment securities available for sale	$ 2,636	$
Gross losses on sales of investment securities available for sale	(1,505)	
Other than temporary impairment loss on equity investments	(186)	(139)
Total securities gains (losses)	$ 945	$ (139)

Investment securities having an aggregate carrying value of $1,694,084 at June 30, 2010, $2,121,783 at December 31, 2009 and $2,012,080 at June 30, 2009, were pledged as collateral to secure public funds on deposit, to secure certain short-term borrowings and for other purposes as required by law.

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Note D

Loans and Leases

Loans and leases outstanding include the following as of the dates indicated:

	June 30, 2010	December 31, 2009	June 30, 2009
Loans covered by loss share agreements	$ 2,367,090	$ 1,173,020	$
Loans and leases not covered by loss share agreements			
Real estate:			
Construction and land development	627,899	622,354	677,884
Commercial mortgage	4,625,351	4,552,078	4,397,247
Residential mortgage	921,346	864,704	858,036
Revolving mortgage	2,187,978	2,147,223	2,052,941
Other mortgage	157,333	158,187	155,483
Total real estate loans	8,519,907	8,344,546	8,141,591
Commercial and industrial	1,801,465	1,832,670	1,858,910
Consumer	815,008	941,986	1,070,290
Lease financing	300,047	330,713	332,644
Other	186,067	195,084	119,610
Total loans and leases not covered by loss share agreements	11,622,494	11,644,999	11,523,045
Total loans and leases	13,989,584	12,818,019	11,523,045
Less allowance for loan and lease losses	188,169	172,282	162,282
Net loans and leases	$ 13,801,415	$ 12,645,737	$ 11,360,763

	June 30, 2010		
	Impaired at acquisition date	All other acquired loans	Total
Loans covered by loss share agreements			
Real estate:			
Construction and land development	$ 172,256	$ 561,002	$ 733,258
Commercial mortgage	121,134	947,197	1,068,331
Residential mortgage	33,853	40,144	73,997
Revolving mortgage	128	25,041	25,169
Other mortgage	35,346	197,740	233,086
Total real estate loans	362,717	1,771,124	2,133,841
Commercial and industrial	9,195	211,669	220,864
Consumer	133	7,441	7,574
Other	72	4,739	4,811
Total loans covered by loss share agreements	$ 372,117	$ 1,994,973	$ 2,367,090

Impaired loans are loans that have evidence of deterioration in credit quality since origination, suggesting it is probable that all contractually required payments will not be collected. The following table provides information on all impaired loans, exclusive of those loans evaluated collectively as a homogeneous group.

	June 30, 2010	December 31, 2009	June 30, 2009
Impaired loans:			
Covered by loss share agreements	$ 372,117	$ 116,446	$
Not covered by loss share agreements	54,457	50,797	35,098
Total	$ 426,574	$ 167,243	$ 35,098
Allowance for loan and lease losses related to:			
Impaired loans covered by loss share agreements	$ 16,006	$ 3,500	$
Impaired loans and leases not covered by loss share agreements	3,781	9,611	5,689
Impaired loans with no allowance for loan and lease loss:			
Loans covered by loss share agreements	323,319	106,498	
Loans and leases not covered by loss share agreements	2,039	9,902	10,807

Interest previously accrued on acquired loans covered by loss share agreements with the FDIC (Covered Loans) placed on nonaccrual status is charged against interest income. Payments received are applied against the principal balance of the fully impaired loans until such time as full collection of the remaining recorded balance is expected. Additional interest payments received after that time are recorded as interest income on a cash basis.

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When the fair values of Covered Loans were established, certain loans were identified as impaired. Due to uncertainty regarding the timing of future cash flows, no accretable yield is being recorded for loans deemed impaired at acquisition from TVB and VB, and these loans are being accounted for using the cost recovery method. Cash flow analyses were completed for loans deemed impaired at acquisition from First Regional and SAB and therefore the accretion method is being applied with respect to recognition of accretable yield on those loans.

The following table provides changes in the carrying value of acquired impaired loans during the six-month period ended June 30, 2010:

Balance, December 31, 2009	$ 75,368
Fair value of acquired impaired loans covered by loss share agreements	412,627
Reductions for repayments, foreclosures and decreases in fair value	(115,878)
Balance, June 30, 2010	$ 372,117

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Information regarding the June 30, 2010 and December 31, 2009 carrying amount of acquired loans that were identified as impaired at acquisition follows:

	June 30, 2010	December 31, 2009
Outstanding balance	$ 807,288	$ 200,310
Carrying amount	372,117	75,368

The cash flow analyses prepared for loans originated by First Regional and SAB are being used to determine the amount of accretable yield recognized on those loans identified as impaired at acquisition. Improvements in fair values subsequent to acquisition on several loans for TVB and VB resulted in the reclassification of nonaccretable yield to accretable yield.

	Accretable Yield
Balance at December 31, 2009	$
Additions	45,523
Accretion	(12,170)
Reclassifications from (to) nonaccretable difference	2,795
Disposals	(1,070)
Balance at June 30, 2010	$ 35,078

Note E

Allowance for Loan and Lease Losses

Activity in the allowance for loan and lease losses is summarized as follows:

	Six months ended June 30,	
	2010	2009
Balance, January 1	$ 172,282	$ 157,569
Adjustment resulting from adoption of change in accounting for QSPEs and controlling financial interests, effective January 1, 21010	681	
Provision for loan and lease losses	48,756	39,482
Loans and leases charged-off:		
Covered by loss share agreements	(7,358)	
Not covered by loss share agreements	(29,244)	(37,024)
Loans and leases recovered:		
Covered by loss share agreements		
Not covered by loss share agreements	3,052	2,255
Net charge-offs	(33,550)	(34,769)
Balance, June 30	$ 188,169	$ 162,282

	June 30, 2010	December 31, 2009	June 30, 2009
Allowance for loan and lease losses allocated to:			
Loans covered by loss share agreements	$ 16,006	$ 3,500	$
Loans and leases not covered by loss share agreements	172,163	168,782	162,282

Total	$ 188,169	$ 172,282	$ 162,282

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Note F

Receivable from FDIC for Loss Share Agreements

The following table provides changes in the receivable from the FDIC during the first six months of 2010:

	June 30, 2010
Balance at December 31, 2009	$ 249,842
Additional receivable from 2010 acquisitions	479,295
Accretion of premium and discount, net	2,386
Receipt of payments from FDIC	(52,422)
Post-acquisition adjustments	13,141
Balance at June 30, 2010	$ 692,242

The receivable from the FDIC for loss share agreements is measured separately from the related covered assets and is recorded at fair value. The fair value was estimated using projected cash flows related to the loss share agreements based on the expected reimbursements for losses and the applicable loss share percentages.

Post-acquisition adjustments represent the net change in loss estimates related to covered loans and other real estate owned as a result of changes in estimated fair values and the allowance for loan and lease losses related to covered loans. For loans covered by loss share agreements, subsequent decreases in the amount expected to be collected from the borrower result in a provision for loan and lease losses, an increase in the allowance for loan and lease losses, and a proportional adjustment to the receivable from the FDIC for the estimated amount to be reimbursed. Subsequent increases in the amount expected to be collected result in the reversal of any previously recorded provision for loan and lease losses and related allowance for loan and lease losses and adjustments to the receivable from the FDIC, or prospective adjustment to the accretable yield if no provision for loan and lease losses had been recorded. Adjustments related to acquisition date fair values, made within one year after the closing date of the respective acquisition, are reflected in the bargain purchase gain.

Note G

Estimated Fair Values

Fair value estimates are made at a specific point in time based on relevant market information and information about each financial instrument. Where information regarding the fair value of a financial instrument is publicly available, those values are used, as is the case with investment securities, residential mortgage loans and certain long-term obligations. In these cases, an open market exists in which those financial instruments are actively traded.

Because no market exists for many financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates. For those financial instruments with a fixed interest rate, an analysis of the related cash flows was the basis for estimating fair values. The expected cash flows were then discounted to the valuation date using an appropriate discount rate. The discount rates used represent the rates under which similar transactions would be currently negotiated. For each period presented, the fair value for loans, net of allowance for loan and lease losses, included an adjustment to reflect the unfavorable liquidity conditions that existed in various financial markets. Generally, the fair value of variable rate financial instruments equals the book value.

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	June 30, 2010		December 31, 2009		June 30, 2009	
	Carrying Value	Fair Value	Carrying Value	Fair Value	Carrying Value	Fair Value
Cash and due from banks	$ 625,857	$ 625,857	$ 480,242	$ 480,242	$ 637,896	$ 637,896
Overnight investments	736,896	736,896	723,260	723,260	229,668	229,668
Investment securities available for sale	3,768,777	3,768,777	2,929,162	2,929,162	3,745,385	3,745,385
Investment securities held to maturity	3,084	3,334	3,603	3,834	4,140	4,379
Loans held for sale	91,076	91,076	67,381	67,381	115,920	115,920
Loans covered by loss share agreements, net of allowance for loan and lease losses	2,351,084	2,296,345	1,169,520	1,169,520		
Loans and leases not covered by loss share agreements, net of allowance for loan and lease losses	11,450,331	10,952,196	11,476,217	11,060,532	11,360,763	10,921,038
Receivable from FDIC for loss share agreements	692,242	692,242	249,842	249,842		
Income earned not collected	77,186	77,186	60,684	60,684	66,226	66,226
Stock issued by:						
Federal Home Loan Bank of Atlanta	50,688	50,688	47,361	47,361	46,677	46,677
Federal Home Loan Bank of San Francisco	16,781	16,781	5,592	5,592		
Federal Home Loan Bank of Seattle	4,490	4,490	4,490	4,490		
Deposits	17,787,241	17,855,490	15,337,567	15,396,423	14,358,149	14,435,457
Short-term borrowings	541,709	541,709	642,405	642,405	599,853	599,853
Long-term obligations	918,930	933,064	797,366	788,004	735,803	702,920
Accrued interest payable	40,652	40,652	37,881	37,881	59,807	59,807

For off-balance sheet commitments and contingencies, carrying amounts are reasonable estimates of the fair values for such financial instruments. Carrying amounts include unamortized fee income and, in some cases, reserves for any credit losses from those financial instruments. These amounts are not material to BancShares financial position.

Fair value represents the price that would be received to sell an asset or transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities, BancShares considers the principal or most advantageous market in which those assets or liabilities are sold and considers assumptions that market participants would use when pricing those assets or liabilities. As required under US GAAP, individual fair value estimates are ranked based on the relative reliability of the inputs used in the valuation. Fair values determined using level 1 inputs rely on active and observable markets to price identical assets or liabilities. In situations where identical assets and liabilities are not traded in active markets, fair values may be determined based on level 2 inputs, which exist when observable data exists for similar assets and liabilities. Fair values for assets and liabilities that are not actively traded in observable markets are based on level 3 inputs, which are considered to be nonobservable.

Among BancShares assets and liabilities, investment securities available for sale and interest rate swaps accounted for as cash flow hedges are reported at their fair values on a recurring basis. Certain other assets are adjusted to their fair value on a nonrecurring basis, including loans held for sale, which are carried at the lower of cost or market. Impaired loans, OREO, goodwill and other intangible assets are periodically tested for impairment. Loans held for investment, deposits, short-term borrowings and long-term obligations are not reported at fair value. BancShares did not elect to voluntarily report any assets or liabilities at fair value.

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For assets and liabilities carried at fair value on a recurring basis, the following table provides fair value information as of June 30, 2010, December 31, 2009 and June 30, 2009:

		Fair value measurements using:		
Description	**Fair value**	**Quoted prices in active markets for identical assets and liabilities (Level 1 inputs)**	**Quoted prices for similar assets and liabilities (Level 2 inputs)**	**Significant unobservable inputs (Level 3 inputs)**
June 30, 2010				
Assets measured at fair value				
Investment securities available for sale				
U.S. Government	$ 3,084,717	$ 3,084,717	$	$
Corporate bonds	489,583	489,583		
Residential mortgage-backed securities	174,516		174,516	
Equity securities	18,691	18,691		
State, county, municipal	1,270		1,270	
Total	$ 3,768,777	$ 3,592,991	$ 175,786	$
Liabilities measured at fair value				
Interest rate swaps accounted for as cash flow hedges	$ 11,309	$	$ 11,309	$
December 31, 2009				
Assets measured at fair value				
Investment securities available for sale				
U.S. Government	$ 2,287,423	$ 2,287,423	$	$
Corporate bonds	485,667	485,667		
Residential mortgage-backed securities	130,338		130,338	
Equity securities	16,622	16,622		
State, county, municipal	6,813		6,813	
Other	2,299	1,012		1,287
Total	$ 2,929,162	$ 2,790,724	$ 137,151	$ 1,287
Liabilities measured at fair value				
Interest rate swaps accounted for as cash flow hedges	$ 5,367	$	$ 5,367	$
June 30, 2009				
Assets measured at fair value				
Investment securities available for sale				
U.S. Government	$ 3,169,883	$ 3,169,883	$	$
Corporate bonds	457,742	457,742		
Residential mortgage-backed securities	96,721		96,721	
Equity securities	14,597	14,597		
State, county, municipal	1,617		1,617	
Other	4,825			4,825
Total	$ 3,745,385	$ 3,642,222	$ 98,338	$ 4,825

Liabilities measured at fair value								
Interest rate swaps accounted for as cash flow hedges	$	6,440	$		$	6,440	$	

Prices for US Government securities and corporate bonds are readily available in the active markets in which those securities are traded and the resulting fair values are shown in the Level 1 input column. Prices for mortgage-backed securities, state, county and municipal securities are obtained using the fair values of similar assets and the resulting fair values are shown in the Level 2 input column. At December 31, 2009, the fair value for the retained residual interest from a securitization transaction was determined based on Level 3 nonobservable inputs. Based on changes to US GAAP related to accounting for QSPEs and controlling financial interests that became effective January 1, 2010, the previously securitized loans were consolidated and the residual interest strip was removed from the consolidated balance sheet. There were no transfers between Level 1 and Level 2 inputs during the six months ended June 30, 2010.

At June 30, 2010, other assets include $71,959 of stock in various Federal Home Loan Banks (FHLB). The FHLB stock, which is redeemable only through the issuer, is carried at its par value. The investment in the FHLB stock is considered a long-term investment and its value is based on the ultimate recoverability of par value. Management has concluded that the investment in FHLB stock was not other-than-temporarily impaired as of June 30, 2010.

Under the terms of the existing cash flow hedges, BancShares pays a fixed payment to the counterparty in exchange for receipt of a variable payment that is determined based on the 3-month LIBOR rate. The fair value of the cash flow hedges are therefore based on projected LIBOR rates for the duration of the hedges, values that, while observable in the market, are subject to adjustment due to pricing considerations for the specific instrument.

For those investment securities available for sale with fair values that are determined by reliance on significant nonobservable inputs, the following table identifies the factors causing the change in fair value during the first six months of 2010 and 2009:

	Investment securities available for sale with fair values based on significant nonobservable inputs	
Description	**2010**	**2009**
Beginning balance, January 1,	$ 1,287	$ 5,427
Total gains (losses), realized or unrealized:		
Included in earnings		
Included in other comprehensive income		195
Purchases, sales, issuances and settlements, net		(797)
Transfers in/out of Level 3	(1,287)	
Ending balance, June 30	$	$ 4,825

No gains or losses were reported for the six month periods ended June 30, 2010 and 2009 that relate to fair values estimated based on significant nonobservable inputs. The investment securities valued using level 3 inputs that were transferred out during the first quarter of 2010 result from changes in US GAAP adopted January 1, 2010 related to investments in the retained interest of a residual interest strip that resulted from an asset securitization.

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Certain assets and liabilities are carried at fair value on a nonrecurring basis. Loans held for sale are carried at the lower of aggregate cost or fair value and are therefore carried at fair value only when fair value is less than the asset cost. Certain impaired loans are also carried at fair value. For assets and liabilities carried at fair value on a nonrecurring basis, the following table provides fair value information as of June 30, 2010, December 31, 2009 and June 30, 2009:

		Fair value measurements using:		
Description	**Fair value**	**Quoted prices in active markets for identical assets and liabilities (Level 1 inputs)**	**Quoted prices for similar assets and liabilities (Level 2 inputs)**	**Significant nonobservable inputs (Level 3 inputs)**
June 30, 2010				
Loans held for sale	$ 91,076	$	$ 91,076	$
Impaired loans:				
Covered by loss share agreements	356,111			356,111
Not covered by loss share agreements	50,676			50,676
December 31, 2009				
Loans held for sale	67,381		67,381	
Impaired loans:				
Covered by loss share agreements	112,946			112,946
Not covered by loss share agreements	40,895			40,895
June 30, 2009				
Loans held for sale	39,997		39,997	
Impaired loans:				
Covered by loss share agreements				
Not covered by loss share	18,624			18,624

The values of loans held for sale are based on prices observed for similar pools of loans. The values of impaired loans are determined by either the collateral value or by the discounted present value of the expected cash flows. No financial liabilities were carried at fair value on a nonrecurring basis as of June 30, 2010 or December 31, 2009.

Certain non-financial assets and non-financial liabilities are measured at fair value on a nonrecurring basis. OREO is measured and reported at fair value using Level 2 inputs for observable market data or Level 3 inputs for valuations based on nonobservable criteria. During the six month period ended June 30, 2010, foreclosures of other real estate not covered by loss share agreements totaled $16,217, all of which were valued using Level 3 inputs. In connection with the measurement and initial recognition of noncovered OREO, BancShares recognized loan charge-offs totaling $8,497. Based on updates to Level 3 inputs, noncovered OREO with a fair value of $6,006 as of June 30, 2010 incurred write-downs that totaled $1,160 during the six month period ended June 30, 2010.

Note H

Employee Benefit Plans

Pension expense is a component of employee benefits expense. For the three and six month periods ended June 30, 2010 and 2009, the components of pension expense are as follows:

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	Three months ended June 30, 2010	2009	Six month periods ended June 30, 2010	2009
Service cost	$ 3,667	$ 3,669	$ 6,671	$ 6,282
Interest cost	7,317	6,584	12,546	10,867
Expected return on assets	(9,497)	(8,584)	(16,018)	(13,751)
Amortization of prior service cost	68	63	115	104
Amortization of net actuarial loss	1,155	1,075	2,080	1,788
Total pension expense	$ 2,710	$ 2,807	$ 5,394	$ 5,290

For the six month periods ended June 30, 2010 and 2009 the assumed discount rate is 6.00 percent, the expected long-term rate of return on plan assets is 8.00 percent and the assumed rate of salary increases is 4.50 percent.

Note I

Contingencies

BancShares and various subsidiaries have been named as defendants in various legal actions arising from their normal business activities in which damages in various amounts are claimed. Although the amount of any ultimate liability with respect to those other matters cannot be determined, in the opinion of management, any such liability will not have a material effect on BancShares consolidated financial statements.

Note J

Derivatives

At June 30, 2010, BancShares had two interest rate swaps that qualify as cash flow hedges under US GAAP. The fair values of these derivatives are included in other liabilities in the consolidated balance sheets and in the net change in other liabilities in the consolidated statements of cash flows.

The interest rate swaps are used for interest rate risk management purposes and convert variable-rate exposure on outstanding debt to a fixed rate. The interest rate swaps each have a notional amount of $115,000, representing the amount of variable-rate trust preferred capital securities issued during 2006. The 2006 interest rate swap hedges interest payments through June 2011 and requires fixed-rate payments by BancShares at 7.125 percent in exchange for variable-rate payments of 175 basis points above 3-month LIBOR, which is equal to the interest paid to the holders of the trust preferred capital securities. The 2009 interest rate swap hedge interest payments from July 2011 through June 2016 and requires fixed-rate payments by BancShares at 5.50 percent in exchange for variable-rate payments of 175 basis points above 3-month LIBOR. As of June 30, 2010, collateral with a fair value of $10,366 was pledged to secure the existing obligation under the interest rate swaps. For both swaps, settlement occurs quarterly.

	June 30, 2010 Notional amount	Estimated fair value of liability	December 31, 2009 Notional amount	Estimated fair value of (asset) liability
2006 interest rate swap hedging variable rate exposure on trust preferred capital securities 2006-2011	$ 115,000	$ 5,384	$ 115,000	$ 7,424
2009 interest rate swap hedging variable rate exposure on trust preferred capital securities 2011-2016	115,000	5,925	115,000	(2,057)
		$ 11,309		$ 5,367

For cash flow hedges, the effective portion of the gain or loss due to changes in the fair value of the derivative hedging instrument is included in other comprehensive income, while the ineffective portion, representing the excess of the cumulative change in the fair value of the derivative over the cumulative change in expected future discounted cash flows on the hedged transaction, is recorded in the consolidated income statement. BancShares interest rate swaps have been fully effective since inception. Therefore, changes in the fair value of the interest rate swaps have had no impact on net income. For the six month periods ended June 30, 2010 and 2009, BancShares recognized interest expense of $2,951 and $2,238, respectively, resulting from the interest rate swaps, none of which related to ineffectiveness.

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The following table discloses activity in accumulated other comprehensive income (loss) related to the interest rate swaps during the six month periods ended June 30, 2010 and 2009.

	2010	2009
Accumulated other comprehensive loss resulting from interest rate swaps as of January 1, net of tax	$ (3,248)	$ (6,456)
Other comprehensive (loss) income recognized during six month period ended June 30, net of tax	(3,596)	2,559
Accumulated other comprehensive loss resulting from interest rate swaps as of June 30, net of tax	$ (6,844)	$ (3,897)

BancShares monitors the credit risk of the interest rate swap counterparty.

Note K

Segment Disclosures

BancShares conducts its banking operations through its two wholly-owned subsidiaries, FCB and ISB. Although FCB and ISB offer similar products and services to customers, each entity operates in distinct geographic markets, except California, Washington and Florida, and has separate management groups. Additionally, the financial results and trends of ISB reflect the de novo nature of its growth.

FCB operates from a single charter from its branch network in North Carolina, Virginia, West Virginia, Maryland, Tennessee, California, Washington, Florida and Washington, DC. FCB s entrance into California, Washington and Florida during 2009 and 2010 resulted from participation in FDIC-assisted transactions. ISB began operations in 1997 and operates from a thrift charter in Florida, Georgia, Texas, New Mexico, Arizona, California, Oregon, Washington, Colorado, Oklahoma, Missouri and Kansas.

Management has determined that FCB and ISB are reportable business segments. In the aggregate, FCB and its consolidated subsidiaries, which are integral to its branch operation, and ISB account for more than 90 percent of consolidated assets, revenues and net income. The Other category in the accompanying table includes activities of the parent company and Neuse, Incorporated (Neuse), a subsidiary that owns real property used in the banking operation and owns other real estate. The other real estate owned (non-performing assets) by Neuse relates to loans originated by ISB. During 2009, Neuse purchased some of ISB s OREO to reduce ISB s nonperforming assets. To facilitate the potential purchase of additional OREO in the future, ISB has agreed to lend Neuse up to $15,000 under a revolving line of credit. No amount was owed by Neuse to ISB as of June 30, 2010 under the revolving line of credit.

The adjustments in the accompanying tables represent the elimination of the impact of certain intercompany transactions. The adjustments for interest income and interest expense neutralize the earnings and cost of intercompany borrowings. The adjustments to noninterest income and noninterest expense reflect the elimination of management fees and other service fees paid from one company to another within BancShares consolidated group.

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	ISB	FCB	Other	Total	Adjustments	Consolidated
June 30, 2010						
Total assets	$ 2,807,642	$ 18,155,558	$ 2,181,898	$ 23,145,098	$ (2,039,329)	$ 21,105,769
Loans and leases:						
Covered by loss share agreements		2,367,090		2,367,090		2,367,090
Not covered by loss share agreements	2,255,885	9,457,684		11,713,569	(91,075)	11,622,494
Allowance for loan and lease losses	41,875	146,294		188,169		188,169
Goodwill	793	60,593		61,386	41,239	102,625
Nonperforming assets:						
Covered by loss share agreements		362,578		362,578		362,578
Not covered by loss share agreements	63,731	77,524	15,331	156,586		156,586
Deposits	2,187,421	15,633,900		17,821,321	(34,080)	17,787,241
December 31, 2009						
Total assets	$ 2,573,605	$ 15,791,475	$ 2,181,898	$ 20,546,978	$ (2,080,915)	$ 18,466,063
Loans and leases:						
Covered by loss share agreements		1,173,020		1,173,020		1,173,020
Not covered by loss share agreements	2,194,659	9,450,340		11,644,999		11,644,999
Allowance for loan and lease losses	41,675	130,607		172,282		172,282
Goodwill	793	101,832		102,625		102,625
Nonperforming assets:						
Covered by loss share agreements		220,233		220,233		220,233
Not covered by loss share agreements	62,881	76,622	14,546	154,049		154,049
Deposits	1,967,824	13,406,484		15,374,308	(36,741)	15,337,567
June 30, 2009						
Total assets	$ 2,654,534	$ 14,601,756	$ 2,181,110	$ 19,437,400	$ (2,119,520)	$ 17,317,880
Loans and leases not covered by loss share agreements	2,154,136	9,368,909		11,523,045		11,523,045
Allowance for loan and lease losses	38,425	123,857		162,282		162,282
Goodwill	793	101,832		102,625		102,625
Nonperforming assets	61,246	33,364	7,801	102,411		102,411
Deposits	2,050,384	12,334,886		14,385,270	(27,121)	14,358,149

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	As of and for the quarter ended June 30, 2010					
	ISB	FCB	Other	Total	Adjustments	Consolidated
Interest income	$ 33,832	$ 183,364	$ 413	$ 217,609	$ (174)	$ 217,435
Interest expense	10,415	36,675	5,657	52,747	(174)	52,573
Net interest income	23,417	146,689	(5,244)	164,862		164,862
Provision for credit losses	4,889	26,937		31,826		31,826
Net interest income after provision for credit losses	18,528	119,752	(5,244)	133,036		133,036
Noninterest income	3,856	90,820	(140)	94,536	(1,914)	92,622
Noninterest expense	22,624	160,712	354	183,690	(1,914)	181,776
Income (loss) before income taxes	(240)	49,860	(5,738)	43,882		43,882
Income taxes	(42)	17,321	(1,999)	15,280		15,280
Net income (loss)	$ (198)	$ 32,539	$ (3,739)	$ 28,602	$	$ 28,602

	As of and for the quarter ended June 30, 2009					
	ISB	FCB	Other	Total	Adjustments	Consolidated
Interest income	$ 32,461	$ 143,061	$ 1,454	$ 176,976	$ (135)	$ 176,841
Interest expense	13,484	40,844	5,616	59,944	(135)	59,809
Net interest income	18,977	102,217	(4,162)	117,032		117,032
Provision for credit losses	10,064	10,695		20,759		20,759
Net interest income after provision for credit losses	8,913	91,522	(4,162)	96,273		96,273
Noninterest income	3,318	71,143	(545)	73,916	(2,500)	71,416
Noninterest expense	23,181	137,927	512	161,620	(2,500)	159,120
Income (loss) before income taxes	(10,950)	24,738	(5,219)	8,569		8,569
Income taxes	(3,886)	8,078	(1,823)	2,369		2,369
Net income (loss)	$ (7,064)	$ 16,660	$ (3,396)	$ 6,200	$	$ 6,200

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	As of and for the six months ended June 30, 2010					
	ISB	FCB	Other	Total	Adjustments	Consolidated
Interest income	$ 66,475	$ 351,117	$ 916	$ 418,508	$ (373)	$ 418,135
Interest expense	21,296	70,009	11,305	102,610	(373)	102,237
Net interest income	45,179	281,108	(10,389)	315,898		315,898
Provision for credit losses	8,746	40,010		48,756		48,756
Net interest income after provision for credit losses	36,433	241,098	(10,389)	267,142		267,142
Noninterest income	7,189	298,106	(122)	305,173	(3,979)	301,194
Noninterest expense	45,021	313,022	662	358,705	(3,979)	354,726
Income (loss) before income taxes	(1,399)	226,182	(11,173)	213,610		213,610
Income taxes	(435)	84,794	(3,907)	80,452		80,452
Net income (loss)	$ (964)	$ 141,388	$ (7,266)	$ 133,158	$	$ 133,158

	As of and for the six months ended June 30, 2009					
	ISB	FCB	Other	Total	Adjustments	Consolidated
Interest income	$ 65,125	$ 288,041	$ 3,630	$ 356,796	$ (303)	$ 356,493
Interest expense	28,620	83,983	11,356	123,959	(303)	123,656
Net interest income	36,505	204,058	(7,726)	232,837		232,837
Provision for credit losses	19,141	20,341		39,482		39,482
Net interest income after provision for credit losses	17,364	183,717	(7,726)	193,355		193,355
Noninterest income	6,537	140,214	(546)	146,205	(5,097)	141,108
Noninterest expense	45,308	272,430	972	318,710	(5,097)	313,613
Income (loss) before income taxes	(21,407)	51,501	(9,244)	20,850		20,850
Income taxes	(7,655)	16,878	(3,236)	5,987		5,987
Net income (loss)	$ (13,752)	$ 34,623	$ (6,008)	$ 14,863	$	$ 14,863

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

INTRODUCTION

Management s discussion and analysis of earnings and related financial data are presented to assist in understanding the financial condition and results of operations of First Citizens BancShares, Inc. and Subsidiaries (BancShares). This discussion and analysis should be read in conjunction with the unaudited Consolidated Financial Statements and related notes presented within this report. Intercompany accounts and transactions have been eliminated. Although certain amounts for prior years have been reclassified to conform to statement presentations for 2010, the reclassifications have no effect on shareholders equity or net income as previously reported. Unless otherwise noted, the terms we, us and BancShares refer to the consolidated financial position and consolidated results of operations for BancShares.

FDIC-ASSISTED TRANSACTIONS

First Regional Bank. On January 29, 2010, First-Citizens Bank & Trust Company (FCB) entered into an agreement with the FDIC to purchase substantially all the assets and assume the majority of the liabilities of First Regional Bank (First Regional) of Los Angeles, California. Immediately prior to the effectiveness of the transaction, the FDIC had been appointed Receiver of First Regional by the California Department of Financial Institutions.

Table 1 identifies the assets acquired and liabilities assumed, the fair value adjustments, the amounts recorded by FCB, and the calculation of the gain recognized.

First Regional Bank **Table 1**

Acquisition date: January 29, 2010

	As recorded by First Regional	Fair value adjustments at acquisition date	Subsequent acquisition-date adjustments	As recorded by FCB
		(thousands)		
Assets				
Cash and due from banks	$ 37,508	$	$	$ 37,508
Investment securities available for sale	3,250			3,250
Loans covered by loss share agreements	1,853,325	(576,171)	(30,488)	1,246,666
Other real estate owned covered by loss share agreements	61,488	(20,353)	414	41,549
Income earned not collected	6,048			6,048
Receivable from FDIC for loss share agreements		365,170	24,391	389,561
Intangible assets		9,110		9,110
Other assets	23,782	(500)		23,282
Total assets acquired	$ 1,985,401	$ (222,744)	$ (5,683)	$ 1,756,974
Liabilities				
Deposits:				
Noninterest-bearing	$ 528,235	$	$	$ 528,235
Interest-bearing	759,484			759,484
Total deposits	1,287,719			1,287,719
Short-term borrowings	361,876			361,876
Other liabilities	1,188	1,547		2,735
Total liabilities assumed	1,650,783	1,547		1,652,330

Excess of assets acquired over liabilities assumed	$ 334,618			
Aggregate fair value adjustments		$ (224,291)	$ (5,683)	
Gain on acquisition of First Regional				$ 104,644

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The loans and other real estate acquired through foreclosure are covered by loss share agreements that provide for the FDIC to absorb 80 percent of losses incurred on covered loans and other real estate in excess of $41.8 million. The 80 percent coverage ratio applies to losses up to $1.0 billion with losses in excess of $1.0 billion covered by the FDIC at a rate of 95 percent. FCB recorded a receivable from the FDIC equal to $389.6 million as an estimate of the fair value of the amount that will be reimbursed by the FDIC from the loss share agreements. The Purchase and Assumption Agreement between FCB and the FDIC includes a true-up payment at the end of year 10. On March 17, 2020, the true-up measurement date, FCB is required to make a true-up payment to the FDIC equal to 50 percent of the excess, if any, of (i) 20 percent of the stated threshold, or $203.4 million, less (ii) the sum of (a) 25 percent of the asset discount, or $74.9 million, plus (b) 25 percent of the cumulative loss share payments plus (c) the cumulative servicing amount. The cumulative servicing amount is 1 percent of the average covered assets for each year during the terms of the loss share agreements.

First quarter noninterest income included a bargain purchase gain of $110.3 million that resulted from the FDIC-assisted acquisition of First Regional. During the second quarter of 2010, adjustments were made to the initial gain based on additional information regarding the respective acquisition date fair values, which reduced the gain by $5.7 million. These adjustments were made retroactive to the first quarter of 2010 resulting in an adjusted gain of $104.6 million. Our operating results for the period ended June 30, 2010 include the results of the acquired assets and liabilities for the period from January 29, 2010 through June 30, 2010. Accretion and amortization of various purchase accounting discounts and premiums were recorded in the first and second quarters of 2010.

Sun American Bank. On March 5, 2010, FCB entered into an agreement with the FDIC to purchase substantially all the assets and assume the majority of the liabilities of Sun American Bank (SAB) of Boca Raton, Florida. Immediately prior to the effectiveness of the acquisition, the FDIC had been appointed Receiver of SAB by the Florida Office of Financial Regulation.

Table 2 identifies the assets acquired and liabilities assumed, the fair value adjustments, the amounts recorded by FCB, and the calculation of the gain recognized.

Sun American Bank **Table 2**

Acquisition date: March 5, 2010

	As recorded by SAB	Fair value adjustments at acquisition date	Subsequent acquisition-date adjustments	As recorded by FCB
		(thousands)		
Assets				
Cash and due from banks	$ 37,016	$	$	$ 37,016
Investment securities available for sale	66,968			66,968
Loans covered by loss share agreements	411,315	(123,707)	3,283	290,891
Other real estate owned covered by loss share agreements	15,220	(7,200)		8,020
Income earned not collected	1,612			1,612
Receivable from FDIC for loss share agreements		92,360	(2,626)	89,734
Intangible assets		629		629
Other assets	4,473			4,473
Total assets acquired	$ 536,604	$ (37,918)	$ 657	$ 499,343
Liabilities				
Deposits:				
Noninterest-bearing	$ 39,435	$	$	$ 39,435
Interest-bearing	380,577			380,577
Total deposits	420,012			420,012
Short-term borrowings	42,485	48		42,533
Long-term obligations	37,000	3,082		40,082
Other liabilities	853	51		904

Total liabilities assumed	500,350	3,181		503,531
Excess of assets acquired over liabilities assumed	$ 36,254			
Aggregate fair value adjustments		$ (41,099)	$ 657	
Cash received from the FDIC				$ 31,965
Gain on acquisition of Sun American				$ 27,777

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The loans and other real estate acquired through foreclosure are covered by loss share agreements that provide for the FDIC to absorb 80 percent of all losses incurred on covered loans and other real estate up to $99.0 million. Losses in excess of $99.0 million are covered by the FDIC at a rate of 95 percent. FCB recorded a receivable from the FDIC equal to $92.4 million as an estimate of the fair value of the amount that will be reimbursed by the FDIC from the loss share agreements. The Purchase and Assumption Agreement between FCB and the FDIC includes a true-up payment at the end of year 10. On May 15, 2020, the true-up measurement date, FCB is required to make a true-up payment to the FDIC equal to 50 percent of the excess, if any, of (i) 20 percent of the stated threshold, or $19.8 million, less (ii) the sum of (a) 25 percent of the asset discount, or $17.5 million, plus (b) 25 percent of the cumulative loss share payments plus (c) the cumulative servicing amount. The cumulative servicing amount is 1 percent of the average covered assets for each year during the terms of the loss share agreements.

First quarter noninterest income included a bargain purchase gain of $27.1 million that resulted from the FDIC-assisted acquisition of SAB. During the second quarter of 2010, adjustments were made to the initial gain based on additional information regarding the respective acquisition date fair values, which increased the gain by $656,000. These adjustments were made retroactive to the first quarter of 2010 resulting in an adjusted gain of $27.8 million. Our operating results for the period ended June 30, 2010 include the results of the acquired assets and liabilities for the period from March 5, 2010 through June 30, 2010. Accretion and amortization of various purchase accounting discounts and premiums were recorded in the first and second quarters of 2010.

The 2010 transactions involving First Regional and SAB represented the third and fourth transactions involving BancShares since July 17, 2009. Table 3 provides information regarding the four entities from which we have acquired assets and assumed liabilities in FDIC-assisted transactions during 2010 and 2009. Adjustments to acquisition date fair values are subject to change for one year following the closing date of each respective acquisition.

FDIC-Assisted Transactions

Table 3

			Fair value of			
Entity	**Date of transaction**	**# branches**	**Loans acquired**	**Deposits assumed**	**Short-term borrowings assumed**	**Long-term obligations assumed**
				(thousands)		
Sun American Bank	March 5, 2010	12	$ 290,892	$ 420,012	$ 42,533	$ 40,082
First Regional Bank	January 29, 2010	8	1,246,666	1,287,719	361,876	
Venture Bank	September 11, 2009	18	456,995	709,091		55,618
Temecula Valley Bank	July 17, 2009	11	855,583	965,431	79,096	
Total		49	$ 2,850,136	$ 3,382,253	$ 483,505	$ 95,700

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EXECUTIVE OVERVIEW AND PERFORMANCE SUMMARY

BancShares is a financial holding company headquartered in Raleigh, North Carolina that offers full-service banking through two wholly-owned banking subsidiaries, First-Citizens Bank & Trust Company (FCB), a North Carolina-chartered bank, and IronStone Bank (ISB), a federally-chartered thrift institution. FCB operates branches in eight states and the District of Columbia. ISB operates branches in urban areas of twelve states. Beyond the traditional branch network, we offer customer sales and service through telephone, online banking and an extensive ATM network.

BancShares earnings and cash flows are primarily derived from the commercial banking activities conducted by its banking subsidiaries. We offer commercial and consumer loans, deposit and treasury services products, cardholder and merchant services, wealth management services as well as various other products and services typically offered by commercial banks. FCB and ISB gather deposits from retail and commercial customers. BancShares and its subsidiaries also secure funding through various non-deposit sources. We invest the liquidity generated from these funding sources in interest-earning assets such as loans and leases, investment securities and overnight investments. We also invest in the bank premises, furniture and equipment used to conduct the subsidiaries commercial banking business.

Various external factors influence the focus of our business efforts. Due to unprecedented asset quality challenges, capital shortages and the onset of a global economic recession, the U.S. banking industry experienced serious financial challenges during the period from 2008 through mid-2010. During this time of industry-wide turmoil, while maintaining our long-standing attention to prudent banking practices, we have modified our growth focus to benefit from the opportunities that currently exist through participation in FDIC-assisted transactions involving distressed financial institutions. BancShares ability to participate in FDIC-assisted transactions creates opportunities to significantly increase our business volumes in markets in which we presently operate and to expand our banking presence to additional markets which we deem demographically attractive. Additionally, due to purchase discounts and loss share agreements that protect us from a substantial portion of the asset quality risk that we would otherwise incur, we are able to create a substantial portion of the equity required to fund the transactions through significant acquisition gains.

Despite the recognition of significant acquisition gains during 2010 and 2009, recessionary economic conditions, high rates of unemployment, and a growing inability for some businesses and consumers to meet their debt service obligations continue to exert pressure on our core earnings and profitability.

In addition, real estate demand in many of our markets remains weak, resulting in continued depressed real estate prices that have adversely affected collateral values for many borrowers. In particular, the stressed residential real estate markets in Georgia and Florida had a material negative impact on the profitability of ISB during 2009. The financial impact of depressed real estate markets continues to affect earnings during 2010 at a more modest rate.

The demand for our deposit and treasury services products has been influenced by extraordinarily low interest rates and instability in alternative investment markets. Our balance sheet liquidity position remains strong, but our continuing participation in FDIC-assisted transactions creates pressure on liquidity management due to the uncertainty regarding retention of assumed deposit liabilities at a reasonable cost.

Ongoing economic weakness continues to have a significant impact on virtually all financial institutions in the United States, including BancShares. In addition to the various actions previously enacted by governmental agencies and the recently enacted Dodd-Frank Wall Street Reform and Consumer Protection Act, it is likely that further changes will occur as the Federal government attempts to restore stability to the financial services sector.

We operate in diverse geographic markets and can increase our business volumes and profitability by offering competitive products and superior customer service. In addition to our focus on retaining customers of the four banks involved in the FDIC-assisted transactions, we continue to concentrate our marketing efforts on business owners, medical and other professionals and financially active individuals. We seek to increase fee income in areas such as wealth management, cardholder and merchant services, and insurance and treasury services. Leveraging on our investments in technology, we also focus on opportunities to generate income by providing various processing services to other banks.

BancShares consolidated net income during the second quarter of 2010 equaled $28.6 million, an increase of $22.4 million over the $6.2 million earned during the corresponding period of 2009. The annualized return on average assets and equity amounted to 0.54 percent and 6.83 percent respectively during the second quarter of 2010, compared to 0.14 and 1.73 percent during the same period of 2009. Net income per share during the second quarter of 2010 totaled $2.74, compared to $0.59 during the second quarter of 2009. The increase in net income during 2010 resulted from higher net interest income and noninterest income offset in part by increased provision for loan and lease losses and noninterest expenses.

For the six-month period ending June 30, 2010, net income equaled $133.2 million compared to $14.9 million earned during the same period of 2009. Return on assets and equity during 2010 equaled 1.31 percent and 16.46 percent respectively, up from 0.18 percent and 2.09 percent during the six-month period ended June 30, 2009. Net income per share equaled $12.76 during the first six months of 2010 compared to $1.42 in the first six months of 2009. The increase in net income during 2010 was attributable primarily to gains arising from FDIC-assisted transactions completed during the first quarter of 2010.

Net interest income increased $47.8 million from $117.0 million in the second quarter of 2009 to $164.9 million in 2010, an increase of 40.9 percent resulting from balance sheet growth caused primarily by acquisitions and a significant improvement in the net yield on interest-earning assets. The net yield on interest-earning assets improved by 52 basis points from 3.02 in the second quarter 2009 to 3.54 percent in 2010 due to favorable changes in deposit costs and the positive impact of yields and rates on acquired loans and assumed deposits. Year-to-date net interest income increased $83.1 million, or 35.7 percent during 2010. The net yield on interest-earning assets increased 47 basis points to 3.54 percent during the six-month period ended June 30, 2010.

The provision for loan and lease losses recorded during the second quarter of 2010 equaled $31.8 million, compared to $20.8 million during the second quarter of 2009. During the first six months of 2010, the provision for loan and lease losses equaled $48.8 million, an increase of $9.3 million or 23.5 percent from the same period of 2009. The current year increase was caused primarily by post-acquisition deterioration of acquired loans from TVB and VB covered by loss share agreements with the FDIC.

Noninterest income increased $21.2 million or 29.7 percent in the second quarter of 2010 and $160.1 million or 113.4 percent in the first six months of 2010 when compared to the same period of 2009. The significant increase during the six-month period ended June 30, 2010 is primarily due to gains on acquisitions totaling $132.6 million. Noninterest expense increased $22.7 million or 14.2 percent in the second quarter of 2010 and $41.1 million or 13.1 percent in the first six months of 2010 when compared to the same period in 2009. The increase in noninterest expense is due to acquisition related activities, including operating costs for acquired branches and expenses related to the operation and disposition of other real estate.

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Financial Summary Table 4

	2010		2009			Six months ended June 30	
	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	2010	2009
	(thousands, except share data and ratios)						
Summary of Operations							
Interest income	$ 217,435	$ 200,700	$ 191,976	$ 189,690	$ 176,841	$ 418,135	$ 356,493
Interest expense	52,573	49,664	49,575	54,413	59,809	102,237	123,656
Net interest income	164,862	151,036	142,401	135,277	117,032	315,898	232,837
Provision for loan and lease losses	31,826	16,930	21,617	18,265	20,759	48,756	39,482
Net interest income after provision for loan and lease losses	133,036	134,106	120,784	117,012	96,273	267,142	193,355
Gains on acquisitions		132,623	(536)	104,970		132,623	
Other noninterest income	92,622	75,949	82,800	77,661	71,416	168,571	141,108
Noninterest expense	181,776	172,950	174,165	166,277	159,120	354,726	313,613
Income before income taxes	43,882	169,728	28,883	133,366	8,569	213,610	20,850
Income taxes	15,280	65,172	9,883	50,898	2,369	80,452	5,987
Net income	$ 28,602	$ 104,556	$ 19,000	$ 82,468	$ 6,200	$ 133,158	$ 14,863
Net interest income, taxable equivalent	$ 165,937	$ 151,870	$ 143,446	$ 136,426	$ 118,350	$ 318,013	$ 235,575
Per Share Data							
Net income	$ 2.74	$ 10.02	$ 1.82	$ 7.90	$ 0.59	$ 12.76	$ 1.42
Cash dividends	0.300	0.300	0.300	0.300	0.300	0.600	0.600
Market price at period end (Class A)	192.33	198.76	164.01	159.10	133.65	192.33	133.65
Book value at period end	162.28	159.91	149.42	145.16	137.45	162.28	137.45
Tangible book value at period end	151.21	148.68	138.98	134.66	127.32	151.21	127.32
Selected Quarterly Averages							
Total assets	$ 21,222,673	$ 19,957,379	$ 18,386,775	$ 17,892,599	$ 17,309,656	$ 20,550,439	$ 17,128,427
Investment securities	3,732,320	3,060,237	3,134,971	3,596,422	3,578,604	3,398,135	3,413,655
Loans and leases (covered and not covered)	14,202,809	13,789,081	12,877,150	12,078,390	11,621,450	13,953,897	11,640,555
Interest-earning assets	18,778,108	17,507,787	16,319,611	15,862,964	15,725,319	18,103,265	15,550,310
Deposits	17,881,444	16,576,039	15,291,720	14,792,449	14,316,103	17,232,348	14,107,973
Interest-bearing liabilities	15,598,726	14,681,127	13,467,532	13,137,412	12,840,612	15,099,410	12,719,207
Long-term obligations	921,859	964,944	795,646	810,049	734,042	900,231	733,567
Shareholders equity	$ 1,679,837	$ 1,593,072	$ 1,535,828	$ 1,457,599	$ 1,433,427	$ 1,631,756	$ 1,435,695
Shares outstanding	10,434,453	10,434,453	10,434,453	10,434,453	10,434,453	10,434,453	10,434,453

Selected Quarter-End Balances							
Total assets	$ 21,105,769	$ 21,215,692	$ 18,466,063	$ 18,512,878	$ 17,317,880	$ 21,105,769	$ 17,317,880
Investment securities	3,771,861	3,378,482	2,932,765	3,287,309	3,749,525	3,771,861	3,749,525
Loans and leases (covered and not covered)	14,080,660	14,242,302	12,818,019	12,778,161	11,638,965	14,080,660	11,638,965
Deposits	17,787,241	17,843,827	15,337,567	15,348,955	14,358,149	17,787,241	14,358,149
Shareholders equity	1,693,309	1,668,593	1,559,115	1,514,684	1,434,213	1,693,309	1,434,213
Selected Ratios and Other Data							
Rate of return on average assets (annualized)	0.54%	2.12%	0.41%	1.83%	0.14%	1.31%	0.18%
Rate of return on average shareholders equity (annualized)	6.83	26.62	4.92	22.45	1.73	16.46	2.09
Net yield on interest-earning assets (taxable equivalent)	3.54	3.52	3.49	3.41	3.02	3.54	3.05
Allowance for loan and lease losses to noncovered loans and leases at period end	1.48	1.46	1.45	1.43	1.41	1.48	1.41
Nonperforming assets to total loans and leases plus other real estate at period end:							
Covered by loss share agreements	14.71	9.50	17.39	15.08		14.71	
Not covered by loss share agreements	1.34	1.37	1.32	0.92	0.89	1.34	0.89
Tier 1 risk-based capital ratio	14.26	13.81	13.34	13.33	13.30	14.26	13.30
Total risk-based capital ratio	16.33	16.04	15.59	15.58	15.59	16.33	15.59
Leverage capital ratio	8.90	9.34	9.54	9.73	9.68	8.90	9.68
Dividend payout ratio	10.95	2.99	16.48	3.80	50.85	4.70	42.25
Average loans and leases to average deposits	79.43	83.19	84.21	81.65	81.18	80.98	82.51%

Average loans and leases includes nonaccrual loans and loans held for sale.

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INTEREST-EARNING ASSETS

Interest-earning assets include loans and leases, investment securities and overnight investments, all of which reflect varying interest rates based on the risk level and repricing characteristics of the underlying asset. Riskier investments typically carry a higher interest rate, but expose us to potentially increased levels of default.

We have historically focused on maintaining high asset quality, which results in a loan and lease portfolio subjected to strenuous underwriting and monitoring procedures. That focus on asset quality also influences the composition of our investment securities portfolio. At June 30, 2010, United States Treasury and government agency securities represent 81.9 percent of our investment securities portfolio; corporate bonds issued under the FDIC s Treasury Liquidity Guaranty Program represent 13.0 percent; and residential mortgage-backed securities represent 4.7 percent of the total portfolio. Overnight investments are selectively made with other financial institutions that are within our risk tolerance.

During 2010, changes in our interest-earning assets primarily reflect the impact of assets acquired in the FDIC-assisted transactions. The investment securities portfolio changes are primarily based on trends among loans and leases, deposits and short-term borrowings. When inflows arising from deposit and treasury services products exceed loan and lease demand, we invest excess funds in the securities portfolio. Conversely, when loan demand exceeds growth in deposits and short-term borrowings, we allow overnight investments to decline and use proceeds from maturing securities to fund loan demand.

During the second quarter of 2010, interest-earning assets averaged $18.78 billion, an increase of $2.46 billion or 15.1 percent since December 31, 2009 and $3.1 billion or 19.4 percent from the second quarter of 2009. This increase results from assets acquired in the FDIC-assisted transactions and deposit growth in excess of loan and lease demand.

Loans and leases. At June 30, 2010, December 31, 2009 and June 30, 2009, loans and leases totaled $13.99 billion, $12.82 billion and $11.52 billion, respectively. Loans covered by loss share agreements with the FDIC totaled $2.37 billion at June 30, 2010 compared to $1.17 billion at December 31, 2009. There were no covered loans outstanding at June 30, 2009. Loans not covered by loss share agreements equaled $11.62 billion at June 30, 2010, a slight decrease from December 31, 2009 and an increase of $99.4 million or 0.9 percent over June 30, 2009.

Commercial real estate loans not covered by loss share agreements totaled $4.63 billion at June 30, 2010, 39.8 percent of noncovered loans and leases. This balance represents an increase of $73.3 million or 1.6 percent since December 31, 2009 and $228.1 million or 5.2 percent since June 30, 2009. Demand for loans secured by owner-occupied medical and professional facilities remained reasonably strong through December 31, 2009, but weakened during the first half of 2010. These loans are underwritten based primarily upon the cash flow from the operation of the business rather than the value of the real estate collateral.

At June 30, 2010, revolving mortgage loans not covered by loss share agreements totaled $2.19 billion, representing 18.8 percent of total noncovered loans outstanding, an increase of $40.8 million or 1.9 percent since December 31, 2009 and $135.1 million or 6.6 percent compared to June 30, 2009. The 2010 increase results from changes to accounting for QSPEs and controlling financial interests that became effective on January 1, 2010. As a result of the accounting change, $97.3 million of revolving mortgage loans that were previously securitized, sold and removed from the consolidated balance sheet were returned to the balance sheet in the first quarter of 2010 upon adoption of the new accounting guidance.

Commercial and industrial loans not covered by loss share agreements equaled $1.80 billion or 15.5 percent of total noncovered loans and leases. These loans decreased $31.2 million or 1.7 percent since December 31, 2009 and $57.4 million or 3.1 percent since June 30, 2009 due to a decline in customer demand driven by recessionary economic conditions.

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Loans and Leases Table 5

	2010			2009	
	Second Quarter	First Quarter	Fourth Quarter (thousands)	Third Quarter	Second Quarter
Loans covered by loss share agreements	$ 2,367,090	$ 2,602,261	$ 1,173,020	$ 1,257,478	$
Loans and leases not covered by loss share agreements:					
Real estate:					
Construction and land development	627,899	644,031	622,354	621,176	677,884
Commercial mortgage	4,625,351	4,589,291	4,552,078	4,514,554	4,397,247
Residential mortgage	921,346	912,955	864,704	876,001	858,036
Revolving mortgage	2,187,978	2,159,581	2,147,223	2,114,018	2,052,941
Other mortgage	157,333	161,770	158,187	101,802	155,483
Total real estate loans	8,519,907	8,467,628	8,344,546	8,227,551	8,141,591
Commercial and industrial	1,801,465	1,793,195	1,832,670	1,822,526	1,858,910
Consumer	815,008	864,238	941,986	998,007	1,070,290
Lease financing	300,047	316,912	330,713	335,515	332,644
Other	186,067	198,068	195,084	137,084	119,610
Total loans and leases not covered by loss share agreements	11,622,494	11,640,041	11,644,999	11,520,683	11,523,045
Total loans and leases	13,989,584	14,242,302	12,818,019	12,778,161	11,523,045
Less allowance for loan and lease losses	188,169	176,273	172,282	165,282	162,282
Net loans and leases	$ 13,801,415	$ 14,066,029	$ 12,645,737	$ 12,612,879	$ 11,360,763

	June 30, 2010		
	Impaired at acquisition date	All other acquired loans (thousands)	Total
Loans covered by loss share agreements:			
Real estate:			
Construction and land development	$ 172,256	$ 561,002	$ 733,258
Commercial mortgage	121,134	947,197	1,068,331
Residential mortgage	33,853	40,144	73,997
Revolving mortgage	128	25,041	25,169
Other mortgage	35,346	197,740	233,086
Total real estate loans	362,717	1,771,124	2,133,841
Commercial and industrial	9,195	211,669	220,864
Consumer	133	7,441	7,574
Other	72	4,739	4,811
Total loans covered by loss share agreements	$ 372,117	$ 1,994,973	$ 2,367,090

Construction and land development loans not covered by loss share agreements totaled $627.9 million or 5.4 percent of total loans at June 30, 2010, an increase of $5.5 million or 0.9 percent since December 31, 2009 and a decrease of $50.0 million or 7.4 percent since June 30, 2009. Of the $627.9 million of noncovered construction loans outstanding as of June 30, 2010, $59.0 million was in the Atlanta, Georgia and southwest Florida markets. Both of these market areas experienced significant reductions in real estate values during the continuing recession. The majority of the remaining $568.9 million of noncovered construction and land development loans are in North Carolina and Virginia where real estate values have declined more modestly.

Consumer loans not covered by loss share agreements totaled $815.0 million at June 30, 2010, down $127.0 million or 13.5 percent since December 31, 2009 and $255.3 million or 23.9 percent from June 30, 2009. This decline results from our decision during 2008 to discontinue originations of sales finance loans through our dealer network and the general decline in consumer borrowing in 2009 and early 2010 due to recessionary economic conditions.

Among loans covered by loss share agreements, commercial real estate loans totaled $1.07 billion at June 30, 2010, representing 45.1 percent of the total covered portfolio compared to $590.4 million or 50.3 percent of total covered loans as of December 31, 2009. Construction and land development loans totaled $733.3 million, or 31.0 percent of total covered loans at June 30, 2010, an increase of $427.3 million from the December 31, 2009 total of $306.0 million, which represented 26.1 percent of the total covered loans. Commercial and industrial loans totaled $220.9 million or 9.3 percent of total covered loans at June 30, 2010, an increase of $125.7 million from the December 31, 2009 total of $95.2 million, which represented 8.1 percent of total covered loans. Residential mortgage loans covered by the FDIC totaled $74.0 million or 3.1 percent of the covered portfolio as of June 30, 2010 compared to $152.3 million or 13.0 percent of total covered loans at December 31, 2009.

We expect non-acquisition loan growth for 2010 to be extremely limited due to the generally weak demand for loans and widespread customer desire to deleverage. Loan projections are subject to change due to further economic deterioration or improvement and other external factors.

Investment securities. Investment securities available for sale equaled $3.77 billion at June 30, 2010, compared to $2.93 billion at December 31, 2009 and $3.75 billion at June 30, 2009. Available for sale securities are reported at their aggregate fair value, and unrealized gains and losses are included as a component of other comprehensive income, net of deferred taxes. Investment securities held to maturity totaled $3.1 million at June 30, 2010, compared to $3.6 million at December 31, 2009 and $4.1 million at June 30, 2009.

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Investment Securities Table 6

	June 30, 2010				December 31, 2009			
	Cost	Fair Value	Average Maturity (1) (Yrs./Mos.)	Taxable Equivalent Yield	Cost	Fair Value	Average Maturity (1) (Yrs./Mos.)	Taxable Equivalent Yield
				(thousands)				
Investment securities available for sale:								
U. S. Government:								
Within one year	$ 2,316,540	$ 2,325,573	0/5	1.46%	$ 1,543,760	$ 1,554,353	0/6	1.91%
One to five years	752,566	755,139	1/4	0.73	730,324	733,070	1/3	1.12
Over ten years	4,028	4,005	14/4	4.18				