VALLEY NATIONAL BANCORP
Form 10-Q
August 09, 2012
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(Mark One)

x **Quarterly Report Pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934**
For the Quarterly Period Ended June 30, 2012

OR

¨ **Transition Report Pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934**
For the transition period from ______ to ______

Commission File Number 1-11277

VALLEY NATIONAL BANCORP

(Exact name of registrant as specified in its charter)

New Jersey	**22-2477875**
(State or other jurisdiction of	**(I.R.S. Employer**
Incorporation or Organization)	**Identification Number)**
1455 Valley Road	
Wayne, NJ	**07470**
(Address of principal executive office)	**(Zip code)**

973-305-8800

(Registrant s telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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 for such shorter period that the registrant was required to submit and post such files.) Yesx 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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act (check one):

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date. Common Stock (no par value), of which 197,440,489 shares were outstanding as of August 2, 2012.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

VALLEY NATIONAL BANCORP

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION (Unaudited)

(in thousands, except for share data)

	June 30, 2012	December 31, 2011
Assets		
Cash and due from banks	$ 443,297	$ 372,566
Interest bearing deposits with banks	8,423	6,483
Investment securities:		
Held to maturity, fair value of $1,860,722 at June 30, 2012 and $2,027,197 at December 31, 2011	1,805,378	1,958,916
Available for sale	688,788	566,520
Trading securities	22,039	21,938
Total investment securities	2,516,205	2,547,374
Loans held for sale, at fair value	29,970	25,169
Non-covered loans	11,197,315	9,527,797
Covered loans	226,537	271,844
Less: Allowance for loan losses	(129,854)	(133,802)
Net loans	11,293,998	9,665,839
Premises and equipment, net	273,626	265,475
Bank owned life insurance	336,612	303,867
Accrued interest receivable	55,040	52,527
Due from customers on acceptances outstanding	5,356	5,903
FDIC loss-share receivable	59,741	74,390
Goodwill	420,443	317,962
Other intangible assets, net	26,817	20,818
Other assets	548,716	586,134
Total Assets	$ 16,018,244	$ 14,244,507
Liabilities		
Deposits:		
Non-interest bearing	$ 3,231,722	$ 2,781,597
Interest bearing:		
Savings, NOW and money market	4,991,834	4,390,121
Time	2,648,123	2,501,384
Total deposits	10,871,679	9,673,102
Short-term borrowings	523,122	212,849

Long-term borrowings	2,724,536	2,726,099
Junior subordinated debentures issued to capital trusts (includes fair value of $149,649 at June 30, 2012 and $160,478 at December 31, 2011 for VNB Capital Trust I)	190,495	185,598
Bank acceptances outstanding	5,356	5,903
Accrued expenses and other liabilities	199,983	174,708
Total Liabilities	14,515,171	12,978,259
Shareholders Equity*		
Preferred stock, no par value, authorized 30,000,000 shares; none issued	-	-
Common stock, no par value, authorized 232,023,233 shares; issued 197,262,005 shares at June 30, 2012 and 178,717,806 shares at December 31, 2011	69,308	59,955
Surplus	1,384,729	1,179,135
Retained earnings	92,925	90,011
Accumulated other comprehensive loss	(43,867)	(62,441)
Treasury stock, at cost (2,079 common shares at June 30, 2012 and 34,776 common shares at December 31, 2011)	(22)	(412)
Total Shareholders Equity	1,503,073	1,266,248
Total Liabilities and Shareholders Equity	$ 16,018,244	$ 14,244,507

* Share data reflects the five percent common stock dividend issued on May 25, 2012.

See accompanying notes to consolidated financial statements.

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VALLEY NATIONAL BANCORP

CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

(in thousands, except for share data)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Interest Income				
Interest and fees on loans	$ 143,812	$ 135,084	$ 292,272	$ 268,707
Interest and dividends on investment securities:				
Taxable	18,114	28,602	38,865	58,182
Tax-exempt	3,227	2,429	6,346	4,934
Dividends	1,674	1,591	3,425	3,647
Interest on federal funds sold and other short-term investments	31	88	86	143
Total interest income	166,858	167,794	340,994	335,613
Interest Expense				
Interest on deposits:				
Savings, NOW and money market	4,690	5,082	10,044	9,761
Time	9,276	12,616	19,461	24,782
Interest on short-term borrowings	369	276	622	617
Interest on long-term borrowings and junior subordinated debentures	30,452	32,150	61,337	65,891
Total interest expense	44,787	50,124	91,464	101,051
Net Interest Income	122,071	117,670	249,530	234,562
Provision for credit losses	7,405	6,026	13,102	30,188
Net Interest Income After Provision for Credit Losses	114,666	111,644	236,428	204,374
Non-Interest Income				
Trust and investment services	1,984	1,952	3,758	3,975
Insurance commissions	3,283	3,657	8,719	8,080
Service charges on deposit accounts	6,086	5,642	12,032	11,292
Gains on securities transactions, net	1,204	16,492	1,047	19,171
Other-than-temporary impairment losses on securities	-	-	-	-
Portion recognized in other comprehensive income (before taxes)	(550)	-	(550)	(825)
Net impairment losses on securities recognized in earnings	(550)	-	(550)	(825)
Trading gains (losses), net	1,609	(1,048)	621	2,334
Fees from loan servicing	1,149	1,170	2,308	2,367
Gains on sales of loans, net	3,141	1,561	6,307	5,170
Gains on sales of assets, net	256	146	288	203
Bank owned life insurance	1,632	1,880	3,591	3,586
Change in FDIC loss-share receivable	(7,022)	(2,669)	(7,112)	13,566
Other	11,258	4,752	15,616	9,403
Total non-interest income	24,030	33,535	46,625	78,322

Non-Interest Expense				
Salary and employee benefits expense	51,214	44,109	102,240	88,234
Net occupancy and equipment expense	16,903	15,467	34,265	32,653
FDIC insurance assessment	3,208	3,302	6,827	6,631
Amortization of other intangible assets	2,532	1,796	4,490	3,758
Professional and legal fees	3,345	3,020	6,969	6,793
Advertising	1,841	2,703	3,529	4,185
Other	12,467	12,683	27,738	24,655
Total non-interest expense	91,510	83,080	186,058	166,909
Income Before Income Taxes	47,186	62,099	96,995	115,787
Income tax expense	14,366	25,205	29,644	42,308
Net Income	$ 32,820	$ 36,894	$ 67,351	$ 73,479
Earnings Per Common Share*:				
Basic	$ 0.17	$ 0.21	$ 0.34	$ 0.41
Diluted	0.17	0.21	0.34	0.41
Cash Dividends Declared per Common Share*	0.16	0.16	0.33	0.33
Weighted Average Number of Common Shares Outstanding*:				
Basic	197,246,322	178,335,522	197,088,528	178,245,603
Diluted	197,250,168	178,345,558	197,105,638	178,254,714

* Share data reflects the five percent common stock dividend issued on May 25, 2012.

See accompanying notes to consolidated financial statements.

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VALLEY NATIONAL BANCORP

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

(in thousands)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Net income	$ 32,820	$ 36,894	$ 67,351	$ 73,479
Other comprehensive income (loss), net of tax:				
Unrealized gains and losses on available for sale securities				
Net gains arising during the period	2,891	6,074	7,117	7,886
Less reclassification adjustment for net gains included in net income	(699)	(10,043)	(604)	(11,721)
Total	2,192	(3,969)	6,513	(3,835)
Non-credit impairment losses on available for sale securities				
Net change in non-credit impairment losses on securities	4,547	491	11,617	593
Less reclassification adjustment for credit impairment losses included in net income	304	(58)	114	360
Total	4,851	433	11,731	953
Unrealized gains and losses on derivatives (cash flow hedges)				
Net losses on derivatives arising during the period	(3,069)	(3,792)	(2,170)	(2,960)
Less reclassification adjustment for net losses included in net income	811	355	1,619	690
Total	(2,258)	(3,437)	(551)	(2,270)
Defined benefit pension plan				
Amortization of prior service cost	103	93	206	185
Amortization of net loss	337	198	675	398
Total	440	291	881	583
Total other comprehensive income (loss)	5,225	(6,682)	18,574	(4,569)
Total comprehensive income	$ 38,045	$ 30,212	$ 85,925	$ 68,910

See accompanying notes to consolidated financial statements.

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VALLEY NATIONAL BANCORP

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(in thousands)

	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Cash flows from operating activities:		
Net income	$ 67,351	$ 73,479
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	8,955	8,077
Stock-based compensation	2,701	1,276
Provision for credit losses	13,102	30,188
Net amortization of premiums and accretion of discounts on securities and borrowings	10,420	5,102
Amortization of other intangible assets	4,490	3,758
Gains on securities transactions, net	(1,047)	(19,171)
Net impairment losses on securities recognized in earnings	550	825
Proceeds from sales of loans held for sale	198,128	173,081
Gains on sales of loans, net	(6,307)	(5,170)
Originations of loans held for sale	(196,622)	(137,338)
Gains on sales of assets, net	(288)	(203)
Net change in:		
FDIC loss-share receivable (excluding reimbursements)	7,112	(13,566)
Trading securities	(101)	9,793
Fair value of borrowings carried at fair value	(520)	(1,947)
Cash surrender value of bank owned life insurance	(3,591)	(3,586)
Accrued interest receivable	2,781	(305)
Other assets	95,567	25,298
Accrued expenses and other liabilities	(41,523)	(23,533)
Net cash provided by operating activities	161,158	126,058
Cash flows from investing activities:		
Net loan originations	(461,749)	(241,027)
Loans purchased	(117,255)	-
Investment securities held to maturity:		
Purchases	(135,332)	(272,825)
Maturities, calls and principal repayments	329,201	339,196
Investment securities available for sale:		
Purchases	(49,012)	(366,123)
Sales	58,585	390,861
Maturities, calls and principal repayments	133,496	102,250
Death benefit proceeds from bank owned life insurance	1,689	1,169
Proceeds from sales of real estate property and equipment	4,139	3,946
Purchases of real estate property and equipment	(8,407)	(7,513)
Reimbursements from the FDIC under loss-sharing agreements	7,537	22,746
Cash and cash equivalents acquired in acquisition	117,587	-
Net cash used in investing activities	(119,521)	(27,320)
Cash flows from financing activities:		
Net change in deposits	(181,716)	342,833
Net change in short-term borrowings	281,273	(21,258)
Repayments of long-term borrowings	(1,000)	(206,000)

Redemption of junior subordinated debentures	(10,000)	-
Dividends paid to common shareholders	(61,730)	(58,151)
Common stock issued, net	4,207	4,215
Net cash provided by financing activities	31,034	61,639
Net change in cash and cash equivalents	72,671	160,377
Cash and cash equivalents at beginning of year	379,049	366,286
Cash and cash equivalents at end of period	$ 451,720	$ 526,663

See accompanying notes to consolidated financial statements.

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VALLEY NATIONAL BANCORP

CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)

(in thousands)

	Six Months Ended June 30, 2012	2011
Supplemental disclosures of cash flow information:		
Cash payments for:		
Interest on deposits and borrowings	$ 91,592	$ 100,522
Federal and state income taxes	35,061	28,741
Supplemental schedule of non-cash investing activities:		
Acquisitions:		
Non-cash assets acquired:		
Investment securities available for sale	275,650	-
Loans	1,098,948	-
Premises and equipment, net	9,457	-
Accrued interest receivable	5,294	-
Goodwill	101,967	-
Other intangible assets, net	8,050	-
Other assets	67,715	-
Total non-cash assets acquired	$ 1,567,081	-
Liabilities assumed:		
Deposits	1,380,293	-
Short-term borrowings	29,000	-
Junior subordinated debentures issued to capital trusts	15,645	
Other liabilities	51,312	-
Total liabilities assumed	1,476,250	-
Net non-cash assets acquired	$ 90,831	$ -
Net cash and cash equivalents acquired	$ 117,587	$ -
Common stock issued in acquisition	$ 208,418	$ -

See accompanying notes to consolidated financial statements.

VALLEY NATIONAL BANCORP

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Basis of Presentation

The unaudited consolidated financial statements of Valley National Bancorp, a New Jersey Corporation (Valley), include the accounts of its commercial bank subsidiary, Valley National Bank (the Bank), and all of Valley s direct or indirect wholly-owned subsidiaries. All inter-company transactions and balances have been eliminated. The accounting and reporting policies of Valley conform to U.S. generally accepted accounting principles (U.S. GAAP) and general practices within the financial services industry. In accordance with applicable accounting standards, Valley does not consolidate statutory trusts established for the sole purpose of issuing trust preferred securities and related trust common securities. Certain prior period amounts have been reclassified to conform to the current presentation.

In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly Valley s financial position, results of operations and cash flows at June 30, 2012 and for all periods presented have been made. The results of operations for the three and six months ended June 30, 2012 are not necessarily indicative of the results to be expected for the entire fiscal year.

In preparing the unaudited consolidated financial statements in conformity with U.S. GAAP, management has made estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated statements of financial condition and results of operations for the periods indicated. Material estimates that are particularly susceptible to change are: the allowance for loan losses; the evaluation of goodwill and other intangible assets, and investment securities for impairment; fair value measurements of assets and liabilities (including the estimated fair values recorded for acquired assets and assumed liabilities - see discussion below); and income taxes. Estimates and assumptions are reviewed periodically and the effects of revisions are reflected in the consolidated financial statements in the period they are deemed necessary. While management uses its best judgment, actual amounts or results could differ significantly from those estimates. The current economic environment has increased the degree of uncertainty inherent in these material estimates.

Certain information and footnote disclosure normally included in financial statements prepared in accordance with U.S. GAAP and industry practice have been condensed or omitted pursuant to rules and regulations of the SEC. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in Valley s Annual Report on Form 10-K for the year ended December 31, 2011.

Effective January 1, 2012, Valley acquired State Bancorp, Inc. (State Bancorp), the holding company for State Bank of Long Island, a commercial bank. See Note 3 for further details regarding this acquisition.

On May 25, 2012, Valley paid a five percent common stock dividend to shareholders of record on May 11, 2012. All common share and per common share data presented in the consolidated financial statements and the accompanying notes below were adjusted to reflect the dividend.

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Note 2. Earnings Per Common Share

The following table shows the calculation of both basic and diluted earnings per common share for the three and six months ended June 30, 2012 and 2011:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
	(in thousands, except for share data)			
Net income	$ 32,820	$ 36,894	$ 67,351	$ 73,479
Basic weighted-average number of common shares outstanding	197,246,322	178,335,522	197,088,528	178,245,603
Plus: Common stock equivalents	3,846	10,036	17,110	9,111
Diluted weighted-average number of common shares outstanding	197,250,168	178,345,558	197,105,638	178,254,714
Earnings per common share:				
Basic	$ 0.17	$ 0.21	$ 0.34	$ 0.41
Diluted	0.17	0.21	0.34	0.41

Common stock equivalents, in the table above, represent the effect of outstanding common stock options and warrants to purchase Valley s common shares, excluding those with exercise prices that exceed the average market price of Valley s common stock during the periods presented and therefore, would have an anti-dilutive effect on the diluted earnings per common share calculation. Anti-dilutive common stock options and warrants totaled approximately 7.7 million shares for both the three and six months ended June 30, 2012, and 7.2 million shares for both the three and six months ended June 30, 2011.

Note 3. Business Combinations

Acquisition of State Bancorp, Inc.

On January 1, 2012, Valley acquired State Bancorp, the holding company for State Bank of Long Island, a commercial bank with approximately $1.7 billion in assets, after purchase accounting adjustments, and 16 branches in Nassau, Suffolk, Queens, and Manhattan. The shareholders of State Bancorp received a fixed one- for- one exchange ratio for Valley National Bancorp common stock. The total consideration for the acquisition was $208.4 million (approximately 17.7 million shares of Valley common stock). As a condition to the closing of the merger, State Bancorp redeemed $36.8 million of its outstanding Fixed Rate Cumulative Series A Preferred Stock from the U.S. Treasury. This stock redemption was funded by a $37.0 million short-term loan from Valley to State Bancorp. The outstanding loan, included in Valley s consolidated statement of financial condition at December 31, 2011, was subsequently eliminated as of the acquisition date and is no longer outstanding.

In connection with the acquisition, Valley acquired all of the voting and common shares of State Capital Trust I and State Capital Trust II, which are wholly-owned subsidiaries established for the sole purpose of issuing trust preferred securities and related trust common securities. Valley also assumed junior subordinated debentures issued to capital trusts with combined contractual principal balances totaling $20.6 million. Valley has the right to optionally redeem the debentures and related trust preferred securities at par prior to the maturity dates of November 7, 2032 and January 23, 2034 for each respective capital trust. These capital trusts, similar to our other capital trust subsidiaries, are not consolidated for financial statement purposes.

Additionally, a warrant issued by State Bancorp (in connection with its preferred stock issuance) to the U.S. Treasury in December 2008 was assumed by Valley as of the acquisition date. The ten-year warrant to purchase up to 489 thousand of Valley common shares has an exercise price of $11.30 per share, and is exercisable on a net exercise basis. Valley has calculated an internal value for the warrants, and may negotiate their redemption with the U.S. Treasury. However, if Valley elects not to negotiate or an agreement cannot be reached with the U.S. Treasury, the warrants will likely be sold at public auction and remain outstanding.

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Merger expenses totaled $109 thousand and $1.1 million for the three and six months ended June 30, 2012, respectively which were largely related to data processing conversion charges that are included in other non-interest expense on the consolidated statements of income.

The following table sets forth assets acquired and liabilities assumed in the State Bancorp acquisition at their estimated fair values as of the closing date of the transaction:

	January 1, 2012 (in thousands)
Assets acquired:	
Cash and cash equivalents	$ 117,587
Investment securities available for sale	275,650
Loans	1,098,948
Premises and equipment	9,457
Accrued interest receivable	5,294
Goodwill	101,967
Other intangible assets	8,050
Other assets	67,715
Total assets acquired	$ 1,684,668
Liabilities assumed:	
Deposits:	
Non-interest bearing	$ 371,151
Savings, NOW and money market	596,599
Time	412,543
Total deposits	1,380,293
Short-term borrowings	29,000
Junior subordinated debentures issued to capital trusts	15,645
Other liabilities	51,312
Total liabilities assumed	$ 1,476,250
Common stock issued in acquisition	$ 208,418

The fair value estimates are subject to change for up to one year after the closing date of the transaction if additional information relative to closing date fair values becomes available. As Valley continues to analyze the assets acquired and liabilities assumed, there may be adjustments to the recorded carrying values.

Fair Value Measurement of Assets Acquired and Liabilities Assumed

Described below are the methods used to determine the fair values of the significant assets acquired and liabilities assumed in the State Bancorp acquisition.

Cash and cash equivalents. The estimated fair values of cash and cash equivalents approximate their stated face amounts, as these financial instruments are either due on demand or have short-term maturities.

Investment securities available for sale. The estimated fair values of the investment securities available for sale were calculated utilizing Level 2 inputs. The prices for these instruments are obtained through an independent pricing service and are derived from market quotations and matrix pricing. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond s terms and conditions, among other things. Management reviewed the data and assumptions used in pricing the securities by its third party provider to ensure the highest level of significant inputs are derived from market observable data.

Loans. The acquired loan portfolio was segregated into categories for valuation purposes primarily based on loan type (commercial, mortgage, or consumer) and credit risk rating. The estimated fair values were computed by discounting

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the expected cash flows from the respective portfolios. Management estimated the cash flows expected to be collected at the acquisition date by using valuation models that incorporated estimates of current key assumptions, such as prepayment speeds, default rates, and loss severity rates. Prepayment assumptions were developed by reference to recent or historical prepayment speeds observed for loans with similar underlying characteristics. Prepayment assumptions were influenced by many factors including, but not limited to, forward interest rates, loan and collateral types, payment status, and current loan-to-value ratios. Default and loss severity rates were developed by reference to recent or historical default and loss rates observed for loans with similar underlying characteristics. Default and loss severity assumptions were influenced by many factors including, but not limited to, underwriting processes and documentation, vintages, collateral types, collateral locations, estimated collateral values, loan-to-value ratios, and debt-to-income ratios.

The expected cash flows from the acquired loan portfolios were discounted at estimated market rates. The market rates were estimated using a buildup approach which included assumptions with respect to funding cost and funding mix, estimated servicing cost, liquidity premium, and additional spreads, if warranted, to compensate for the uncertainty inherent in the acquired loans. The methods used to estimate the Level 3 fair values of loans are extremely sensitive to the assumptions and estimates used. While management attempted to use assumptions and estimates that best reflected the acquired loan portfolios and current market conditions, a greater degree of subjectivity is inherent in these values than in those determined in active markets.

The difference between the fair value and the expected cash flows from the acquired loans will be accreted to interest income over the remaining term of the loans in accordance with Accounting Standards Codification (ASC) Subtopic 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality. See Note 7 for further details.

Other intangible assets. Other intangible assets consisting of core deposit intangibles (CDI) are measures of the value of non-maturity checking, savings, NOW and money market deposits that are acquired in a business combination excluding any large relationships, for which Valley believes there is no customer related intangible asset. The fair value of the CDI stemming from any given business combination is based on the present value of the expected cost savings attributable to the core deposit funding, relative to an alternative source of funding. The CDI is being amortized over an estimated useful life of eleven years to approximate the existing deposit relationships acquired.

Deposits. The fair values of deposit liabilities with no stated maturity (i.e., NOW and money market accounts, savings accounts, and non-interest-bearing accounts) are equal to the carrying amounts payable on demand. The fair values of certificates of deposit represent contractual cash flows, discounted to present value using interest rates currently offered on deposits with similar characteristics and remaining maturities.

Short-term borrowings. The fair value of short-term borrowings approximates their contractual principal balances, as these borrowings matured in March 2012.

Junior subordinated debentures issued to capital trusts. There is no active market for the trust preferred securities issued by State Bancorp Capital Trust I and State Bancorp Capital Trust II; therefore, the fair value of junior subordinated debentures was estimated utilizing the income approach. Under the income approach, the expected cash flows over the remaining estimated life of the debentures were discounted using Valley s credit spread plus the three- month LIBOR (the contractual base index rate for these instruments). Valley s credit spread was calculated based on Valley s trust preferred securities issued by VNB Capital Trust I, which are publicly traded in an active market.

Note 4. New Authoritative Accounting Guidance

Accounting Standards Update (ASU) No. 2011-04, Fair Value Measurements (Topic 820) Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs, was issued as a result of the effort to develop common fair value measurement and disclosure requirements in U.S. GAAP and International Financial Reporting Standards (IFRS). While ASU No. 2011-04 is largely consistent with existing fair value measurement principles in U.S. GAAP, it expands the existing disclosure requirements for fair value measurements and clarifies the existing guidance or wording changes to align with IFRS No. 13. Many of the requirements for the amendments in ASU No. 2011-04 do not result in a change in the application of the requirements in Topic 820. ASU No. 2011-04 became effective for Valley on January 1, 2012 and did not to have a significant impact on its consolidated financial statements. See Note 5 for the related disclosures.

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ASU No. 2011-05, Comprehensive Income (Topic 220) Presentation of Comprehensive Income, requires an entity to present components of comprehensive income either in a single continuous statement of comprehensive income or in two separate consecutive statements. These amendments will make the financial statement presentation of other comprehensive income more prominent by eliminating the alternative to present comprehensive income within the statement of equity. As originally issued, ASU No. 2011-05 required entities to present reclassification adjustments out of accumulated other comprehensive income by component in the statement in which net income is presented and the statement in which other comprehensive income is presented (for both interim and annual financial statements). This requirement was deferred by ASU No. 2011-12, Comprehensive Income (Topic 220) Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards . ASU No. 2011-05 became effective for all interim and annual periods beginning on or after December 15, 2011 with early adoption permitted, and applied retrospectively. Valley early adopted ASU No. 2011-05 for the year ended December 31, 2011 and elected to present comprehensive income in a separate consolidated statement of comprehensive income.

ASU No. 2011-08, Intangibles Goodwill and Other (Topic 350) Testing Goodwill for Impairment, provides the option of performing a qualitative assessment of whether it is more likely than not that a reporting unit s fair value is less than its carrying amount, before applying the current two-step goodwill impairment test. If the conclusion is that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, the entity would be required to conduct the current two-step goodwill impairment test. Otherwise, the entity would not need to apply the two-step test. ASU No. 2011-08 is effective for annual and interim goodwill impairment tests performed by Valley during 2012. ASU No. 2011-08 did not have a significant impact on Valley s consolidated financial statements.

Note 5. Fair Value Measurement of Assets and Liabilities

ASC Topic 820, Fair Value Measurements and Disclosures, establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1	Unadjusted exchange quoted prices in active markets for identical assets or liabilities, or identical liabilities traded as assets that the reporting entity has the ability to access at the measurement date.
Level 2	Quoted prices in markets that are not active, or inputs that are observable either directly or indirectly (i.e., quoted prices on similar assets), for substantially the full term of the asset or liability.
Level 3	Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported by little or no market activity).

Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

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

The following tables present the assets and liabilities that are measured at fair value on a recurring and nonrecurring basis by level within the fair value hierarchy as reported on the consolidated statements of financial condition at June 30, 2012 and December 31, 2011. The assets presented under nonrecurring fair value measurements in the table below are not measured at fair value on an ongoing basis but are subject to fair value adjustments under certain circumstances (e.g., when an impairment loss is recognized).

		Fair Value Measurements at Reporting Date Using:		
Recurring fair value measurements:	**June 30, 2012**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
		(in thousands)		
Assets				
Investment securities:				
Available for sale:				
U.S. government agency securities	$ 54,902	$ -	$ 54,902	$ -
Obligations of states and political subdivisions	19,310	-	19,310	-
Residential mortgage-backed securities	430,019	-	386,849	43,170
Trust preferred securities	82,864	10,136	26,807	45,921
Corporate and other debt securities	52,180	28,499	23,681	
Equity securities	49,513	28,444	21,069	
Total available for sale	688,788	67,079	532,618	89,091
Trading securities	22,039	-	22,039	-
Loans held for sale [(1)]	29,970	-	29,970	-
Other assets [(2)]	8,097	-	8,097	-
Total assets	$ 748,894	$ 67,079	$ 592,724	$ 89,091
Liabilities				
Junior subordinated debentures issued to VNB Capital Trust I [(3)]	$ 149,649	$ 149,649	$ -	$ -
Other liabilities [(2)]	27,055	-	27,055	-
Total liabilities	$ 176,704	$ 149,649	$ 27,055	$ -
Non-recurring fair value measurements:				
Collateral dependent impaired loans [(4)]	$ 73,484	$ -	$ -	$ 73,484
Loan servicing rights	9,589	-	-	9,589
Foreclosed assets	18,358	-	-	18,358
Total	$ 101,431	$ -	$ -	$ 101,431

		Fair Value Measurements at Reporting Date Using:		
	December 31, 2011	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(in thousands)		
Recurring fair value measurements:				
Assets				
Investment securities:				
Available for sale:				
U.S. government agency securities	$ 90,748	$ -	$ 90,748	$ -
Obligations of states and political subdivisions	20,214	-	20,214	-
Residential mortgage-backed securities	310,137	-	259,977	50,160
Trust preferred securities	70,425	19,576	23,698	27,151
Corporate and other debt securities	33,043	30,603	2,440	-
Equity securities	41,953	23,506	18,447	-
Total available for sale	566,520	73,685	415,524	77,311
Trading securities	21,938	-	21,938	-
Loans held for sale [1]	25,169	-	25,169	-
Other assets [2]	5,211	-	5,211	-
Total assets	$ 618,838	$ 73,685	$ 467,842	$ 77,311
Liabilities				
Junior subordinated debentures issued to VNB Capital Trust I [3]	$ 160,478	$ 160,478	$ -	$ -
Other liabilities [2]	21,854	-	21,854	-
Total liabilities	$ 182,332	$ 160,478	$ 21,854	$ -
Non-recurring fair value measurements:				
Collateral dependent impaired loans [4]	$ 66,854	$ -	$ -	$ 66,854
Loan servicing rights	9,078	-	-	9,078
Foreclosed assets	15,874	-	-	15,874
Total	$ 91,806	$ -	$ -	$ 91,806

(1) Loans held for sale (which consist of residential mortgages) are carried at fair value and had contractual unpaid principal balances totaling approximately $28.7 million and $24.3 million at June 30, 2012 and December 31, 2011, respectively.
(2) Derivative financial instruments are included in this category.
(3) The junior subordinated debentures had contractual unpaid principal obligations totaling $146.7 million and $157.0 million at June 30, 2012 and December 31, 2011, respectively.
(4) Excludes covered loans acquired in the FDIC-assisted transactions completed in the first quarter of 2010 and other purchased credit-impaired loans acquired in the first quarter of 2012.

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The following table summarizes changes in Level 3 assets, consisting of available for sale securities, measured at fair value on a recurring basis for the three months ended June 30, 2012 and 2011:

	Three Months Ended June 30,	
	2012	2011
	(in thousands)	
Balance, beginning of the period	$ 84,720	$ 52,373
Total net (losses) gains for the period included in:		
Net income	(550)	-
Other comprehensive income	7,847	851
Settlements	(2,926)	(2,006)
Balance, end of the period	$ 89,091	$ 51,218
Change in unrealized losses for the period included in earnings for assets held at the end of the reporting period *	$ (550)	$ -

* Represents the net impairment losses on securities recognized in earnings for the period.

The following table summarizes changes in Level 3 assets, consisting of trading and available for sale securities, measured at fair value on a recurring basis for six months ended June 30, 2012 and 2011:

	Six Months Ended June 30,			
	2012		2011	
	Trading Securities	Available For Sale Securities	Trading Securities	Available For Sale Securities
	(in thousands)			
Balance, beginning of the period	$ -	$ 77,311	$ 21,903	$ 138,655
Transfers out of Level 3:				
Residential mortgage-backed securities	-	-	-	(44,771)
Trust preferred securities	-	-	(21,903)	(17,397)
Corporate and other debt securities	-	-	-	(12,914)
Equity securities	-	-	-	(9,353)
Total net (losses) gains for the period included in:				
Net income	-	(550)	-	(825)
Other comprehensive income	-	18,954	-	2,212
Settlements	-	(6,624)	-	(4,389)
Balance, end of the period	$ -	$ 89,091	$ -	$ 51,218
Change in unrealized losses for the period included in earnings for assets held at the end of the reporting period *	$ -	$ (550)	$ -	$ (825)

* Represents the net impairment losses on securities recognized in earnings for the period.

During the three and six months ended June 30, 2012 and 2011, there were no transfers of assets between Level 1 and Level 2.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following valuation techniques were used for financial instruments measured at fair value on a recurring basis. All the valuation techniques described below apply to the unpaid principal balance excluding any accrued interest or dividends at the measurement date. Interest income and expense are recorded within the consolidated statements of income depending on the nature of the instrument using the effective interest method based on acquired discount or premium.

Available for sale and trading securities. All U.S. Treasury securities, certain corporate and other debt securities, and certain common and preferred equity securities (including certain trust preferred securities) are reported at fair values

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utilizing Level 1 inputs. The majority of other investment securities are reported at fair value utilizing Level 2 inputs. The prices for these instruments are obtained through an independent pricing service or dealer market participants with whom Valley has historically transacted both purchases and sales of investment securities. Prices obtained from these sources include prices derived from market quotations and matrix pricing. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond s terms and conditions, among other things. Management reviews the data and assumptions used in pricing the securities by its third party provider to ensure the highest level of significant inputs are derived from market observable data. For certain securities, the inputs used by either dealer market participants or an independent pricing service, may be derived from unobservable market information (Level 3 inputs). In these instances, Valley evaluates the appropriateness and quality of the assumption and the resulting price. In addition, Valley reviews the volume and level of activity for all available for sale and trading securities and attempts to identify transactions which may not be orderly or reflective of a significant level of activity and volume. For securities meeting these criteria, the quoted prices received from either market participants or an independent pricing service may be adjusted, as necessary, to estimate fair value and this results in fair values based on Level 3 inputs. In determining fair value, Valley utilizes unobservable inputs which reflect Valley s own assumptions about the inputs that market participants would use in pricing each security. In developing its assertion of market participant assumptions, Valley utilizes the best information that is both reasonable and available without undue cost and effort.

In calculating the fair value for the available for sale securities under Level 3, Valley prepared present value cash flow models for certain private label mortgage-backed securities and trust preferred securities. The cash flows for the residential mortgage-backed securities incorporated the expected cash flow of each security adjusted for default rates, loss severities and prepayments of the individual loans collateralizing the security. The cash flows for trust preferred securities reflected the contractual cash flow, adjusted if necessary for potential changes in the amount or timing of cash flows due to the underlying credit worthiness of each issuer. The following table presents quantitative information about Level 3 inputs used to measure the fair value of these securities at June 30, 2012:

Security Type	Valuation Technique	Unobservable Input	Range	Weighted Average
Mortgage-backed securities	Discounted cash flow	Prepayment rate	8.1 - 32.7%	18.0%
		Default rate	3.4 - 18.9	7.6
		Loss severity	39.7 - 59.2	50.7
Single issuer trust preferred securities	Discounted cash flow	Loss severity	0.0 - 100.0%	17.6%
		Market credit spreads	6.4 - 7.0	6.7
		Discount rate	6.8 - 8.6	7.9

Significant increases or decreases in any of the unobservable inputs in the table above in isolation would result in a significantly lower or higher fair value measurement of the securities. Generally, a change in the assumption used for the default rate is accompanied by a directionally similar change in the assumption used for the loss severity and a directionally opposite change in the assumption used for prepayment rates.

For the Level 3 available for sale private label mortgage-backed securities, cash flow assumptions incorporated independent third party market participant data based on vintage year for each security. The discount rate utilized in determining the present value of cash flows for the mortgage-backed securities was arrived at by combining the yield on orderly transactions for similar maturity government sponsored mortgage-backed securities with (i) the historical average risk premium of similar structured private label securities, (ii) a risk premium reflecting current market conditions, including liquidity risk and (iii) if applicable, a forecasted loss premium derived from the expected cash flows of each security. The estimated cash flows for each private label mortgage-backed security were then discounted at the aforementioned effective rate to determine the fair value. The quoted prices received from either market participants or independent pricing services are weighted with the internal price estimate to determine the fair value of each instrument.

For two single issuer trust preferred securities in the Level 3 available for sale trust preferred securities, the resulting estimated future cash flows were discounted at a yield, comprised of market rates applicable to the index of the underlying security, estimated market credit spread for similar non-rated securities and an illiquidity premium, if appropriate. The discount rate for each security was applied to three alternative cash flow scenarios, and subsequently weighted based on management s expectations. The three cash flow alternatives for each security assume a scenario with full issuer repayment, a scenario with a partial issuer repayment and a scenario with a full issuer default.

For two pooled securities in the Level 3 available for sale trust preferred securities, the resulting estimated future cash flows were discounted at a yield determined by reference to similarly structured securities for which observable orderly transactions occurred. The discount rate for each security was applied using a pricing matrix based on credit, security type and maturity characteristics to determine the fair value. The fair value calculations for both securities are received from an independent valuation advisor. In validating the fair value calculation from an independent valuation advisor, Valley reviews accuracy of the inputs and the appropriateness of the unobservable inputs utilized in the valuation to ensure the fair value calculation is reasonable from a market participant perspective.

Loans held for sale. The conforming residential mortgage loans originated for sale are reported at fair value using Level 2 inputs. The fair values were calculated utilizing quoted prices for similar assets in active markets. To determine these fair values, the mortgages held for sale are put into multiple tranches, or pools, based on the coupon rate and maturity of each mortgage. The market prices for each tranche are obtained from both Fannie Mae and Freddie Mac. The market prices represent a delivery price, which reflects the underlying price each institution would pay Valley for an immediate sale of an aggregate pool of mortgages. The market prices received from Fannie Mae and Freddie Mac are then averaged and interpolated or extrapolated, where required, to calculate the fair value of each tranche. Depending upon the time elapsed since the origination of each loan held for sale, non-performance risk and changes therein were addressed in the estimate of fair value based upon the delinquency data provided to both Fannie Mae and Freddie Mac for market pricing and changes in market credit spreads. Non-performance risk did not materially impact the fair value of mortgage loans held for sale at June 30, 2012 and December 31, 2011 based on the short duration these assets were held, and the high credit quality of these loans.

Junior subordinated debentures issued to capital trusts. The junior subordinated debentures issued to VNB Capital Trust I are reported at fair value using Level 1 inputs. The fair value was estimated using quoted prices in active markets for similar assets, specifically the quoted price of the VNB Capital Trust I preferred stock traded under ticker symbol VLYPRA on the New York Stock Exchange. The preferred stock and Valley s junior subordinated debentures issued to the Trust have identical financial terms and therefore, the preferred stock s quoted price moves in a similar manner to the estimated fair value and current settlement price of the junior subordinated debentures. The preferred stock s quoted price includes market considerations for Valley s credit and non-performance risk and is deemed to represent the transfer price that would be used if the junior subordinated debenture were assumed by a third party. Valley s potential credit risk and changes in such risk did not materially impact the fair value measurement of the junior subordinated debentures at June 30, 2012 and December 31, 2011.

Derivatives. Derivatives are reported at fair value utilizing Level 2 inputs. The fair value of Valley s derivatives are determined using third party prices that are based on discounted cash flow analyses using observed market interest rate curves and volatilities. The fair values of most of the derivatives incorporate credit valuation adjustments, which consider the impact of any credit enhancements to the contracts, to account for potential nonperformance risk of Valley and its counterparties. On January 1, 2012, Valley made an accounting policy election to use the exception within ASU No. 2011-04 regarding the measurement of the exposure to the counterparty credit risk (i.e., calculating credit valuation adjustments on a net basis by counterparty portfolio). The credit valuation adjustments were not significant to the overall valuation of Valley s derivatives at June 30, 2012 and December 31, 2011.

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Assets and Liabilities Measured at Fair Value on a Non-recurring Basis

The following valuation techniques were used for certain non-financial assets measured at fair value on a nonrecurring basis, including impaired loans reported at the fair value of the underlying collateral, loan servicing rights, other real estate owned and other repossessed assets (upon initial recognition or subsequent impairment) as described below.

Impaired loans. Certain impaired loans are reported at the fair value of the underlying collateral if repayment is expected solely from the collateral and are commonly referred to as collateral dependent impaired loans. Collateral values are estimated using Level 3 inputs, consisting of individual appraisals that are significantly adjusted based on customized discounting criteria. At June 30, 2012, non-current appraisals were discounted up to 27.1 percent based on specific market data by location and property type. During the six months ended June 30, 2012, collateral dependent impaired loans were individually re-measured and reported at fair value through direct loan charge-offs to the allowance for loan losses and/or a specific valuation allowance allocation based on the fair value of the underlying collateral. The direct collateral dependent loan charge-offs to the allowance for loan losses totaled $7.7 million and $11.6 million for the three and six months ended June 30, 2012, respectively. At June 30, 2012, collateral dependent impaired loans with a total recorded investment of $77.0 million were reduced by specific valuation allowance allocations totaling $3.6 million to a reported total net carrying amount of $73.4 million.

Loan servicing rights. Fair values for each risk-stratified group of loan servicing rights are calculated using a fair value model from a third party vendor that requires inputs that are both significant to the fair value measurement and unobservable (Level 3). The fair value model is based on various assumptions, including but not limited to, prepayment speeds, internal rate of return (discount rate), servicing cost, ancillary income, float rate, tax rate, and inflation. The prepayment speed and the discount rate are considered two of the most significant inputs in the model. At June 30, 2012, the fair value model used prepayment speeds (stated as constant prepayment rates) from 6.0 percent up to 25.8 percent and a discount rate of 8 percent for the valuation of the loan servicing rights. A significant degree of judgment is involved in valuing the loan servicing rights using Level 3 inputs. The use of different assumptions could have a significant positive or negative effect on the fair value estimate. Impairment charges are recognized on loan servicing rights when the amortized cost of a risk-stratified group of loan servicing rights exceeds the estimated fair value. Valley recognized net impairment charges of $401 thousand for the three months ended June 30, 2012 and net recoveries of impairment charges of $19 thousand for the six months ended June 30, 2012.

Foreclosed assets. Certain foreclosed assets (consisting of other real estate owned and other repossessed assets), upon initial recognition and transfer from loans, are re-measured and reported at fair value through a charge-off to the allowance for loan losses based upon the fair value of the foreclosed assets. The fair value of a foreclosed asset, upon initial recognition, is typically estimated using Level 3 inputs, consisting of an appraisal that is adjusted based on customized discounting criteria, similar to the criteria used for impaired loans described above. The discounts on appraisals of foreclosed assets were immaterial at June 30, 2012. During the six months ended June 30, 2012, foreclosed assets measured at fair value upon initial recognition totaled $18.3 million. In connection with the measurement and the initial recognition of the foreclosed assets, Valley recognized charge-offs to the allowance for loan losses totaling $1.2 million and $4.1 million for the three and six months ended June 30, 2012, respectively.

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Other Fair Value Disclosures

The following table presents the amount of gains and losses from fair value changes included in income before income taxes for financial assets and liabilities carried at fair value for the three and six months ended June 30, 2012 and 2011:

Reported in Consolidated Statements of Financial Condition	Reported in Consolidated Statements of Income	Gains (Losses) on Change in Fair Value			
		Three Months Ended June 30,		Six Months Ended June 30,	
		2012	2011	2012	2011
		(in thousands)			
Assets:					
Available for sale securities	Net impairment losses on securities	$ (550)	$ -	$ (550)	$ (825)
Trading securities	Trading (losses) gains, net	(151)	(106)	101	387
Loans held for sale	Gains on sales of loans, net	3,141	1,561	6,307	5,170
Liabilities:					
Junior subordinated debentures issued to capital trusts	Trading gains (losses), net	1,760	(942)	520	1,947
		$ 4,200	$ 513	$ 6,378	$ 6,679

ASC Topic 825, Financial Instruments, requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis.

The fair value estimates presented in the following table were based on pertinent market data and relevant information on the financial instruments available as of the valuation date. These estimates do not reflect any premium or discount that could result from offering for sale at one time the entire portfolio of financial instruments. Because no market exists for a portion of the financial instruments, fair value estimates may be 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.

Fair value estimates are based on existing balance sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. For instance, Valley has certain fee-generating business lines (e.g., its mortgage servicing operation, trust and investment management departments) that were not considered in these estimates since these activities are not financial instruments. In addition, the tax implications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of the estimates.

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The carrying amounts and estimated fair values of financial instruments not measured and not reported at fair value on the consolidated statements of financial condition at June 30, 2012 and December 31, 2011 were as follows:

		June 30, 2012		December 31, 2011	
	Fair Value Hierarchy	Carrying Amount	Fair Value	Carrying Amount	Fair Value
		(in thousands)			
Financial assets					
Cash and due from banks	Level 1	$ 443,297	$ 443,297	$ 372,566	$ 372,566
Interest bearing deposits with banks	Level 1	8,423	8,423	6,483	6,483
Investment securities held to maturity:					
U.S. Treasury securities	Level 1	99,945	115,991	100,018	113,859
Obligations of states and political subdivisions	Level 2	470,133	490,592	433,284	453,201
Residential mortgage-backed securities	Level 2	989,820	1,023,629	1,180,104	1,230,993
Trust preferred securities	Level 2	193,287	174,469	193,312	174,753
Corporate and other debt securities	Level 2	52,193	56,041	52,198	54,391
Total investment securities held to maturity		1,805,378	1,860,722	1,958,916	2,027,197
Net loans	Level 3	11,293,998	11,286,189	9,665,839	9,645,517
Accrued interest receivable	Level 1	55,040	55,040	52,527	52,527
Federal Reserve Bank and Federal Home Loan Bank stock[(1)]	Level 2	146,498	146,498	129,669	129,669
Financial liabilities					
Deposits without stated maturities	Level 1	8,223,556	8,223,556	7,171,718	7,171,718
Deposits with stated maturities	Level 2	2,648,123	2,705,541	2,501,384	2,557,119
Short-term borrowings	Level 1	523,122	523,122	212,849	215,179
Long-term borrowings	Level 2	2,724,536	3,157,469	2,726,099	3,154,150
Junior subordinated debentures issued to capital trusts	Level 2	40,846	40,757	25,120	25,620
Accrued interest payable[(2)]	Level 1	3,670	3,670	3,798	3,798

(1) Included in other assets.

(2) Included in accrued expenses and other liabilities.

The following methods and assumptions were used to estimate the fair value of the financial assets and financial liabilities in the table above:

Cash and due from banks and interest bearing deposits with banks. The carrying amount is considered to be a reasonable estimate of fair value because of the short maturity of these items.

Investment securities held to maturity. Fair values are based on prices obtained through an independent pricing service or dealer market participants with whom Valley has historically transacted both purchases and sales of investment securities. Prices obtained from these sources include prices derived from market quotations and matrix pricing. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond s terms and conditions, among other things (Level 2 inputs). Additionally, Valley reviews the volume and level of activity for all classes of held to maturity securities and attempts to identify transactions which may not be orderly or reflective of a significant level of activity and volume. For securities meeting these criteria, the quoted prices received from either market participants or an independent pricing service may be adjusted, as necessary. If applicable, the adjustment to fair value is derived based on present value cash flow model projections prepared by Valley utilizing assumptions similar to those incorporated by market participants.

Loans. Fair values of non-covered loans (i.e., loans which are not subject to loss-sharing agreements with the FDIC) and covered loans (i.e., loans subject to loss-sharing agreements with the FDIC) are estimated by discounting the projected future cash flows using market discount rates that reflect the credit and interest-rate risk inherent in the loan. Projected future cash flows are calculated based upon contractual maturity or call dates, projected repayments and prepayments of principal. Fair values estimated in this manner do not fully incorporate an exit-price approach to fair value, but instead are based on a comparison to current market rates for comparable loans.

Accrued interest receivable and payable. The carrying amounts of accrued interest approximate their fair value due to the short-term nature of these items.

Federal Reserve Bank and Federal Home Loan Bank stock. FRB and FHLB stock are non-marketable equity securities and are reported at their redeemable carrying amounts, which approximate their fair value.

Deposits. The carrying amounts of deposits without stated maturities (i.e., non-interest bearing, savings, NOW, and money market deposits) approximate their estimated fair value. The fair value of time deposits is based on the discounted value of contractual cash flows using estimated rates currently offered for alternative funding sources of similar remaining maturity.

Short-term and long-term borrowings. The carrying amounts of certain short-term borrowings, including securities sold under agreement to repurchase (and from time to time, federal funds purchased and overnight FHLB borrowings) approximate their fair values because they frequently re-price to a market rate. The fair values of other short-term and long-term borrowings are estimated by obtaining quoted market prices of the identical or similar financial instruments when available. When quoted prices are unavailable, the fair values of the borrowings are estimated by discounting the estimated future cash flows using current market discount rates of financial instruments with similar characteristics, terms and remaining maturity.

Junior subordinated debentures issued to capital trusts (excluding VNB Capital Trust I). There is no active market for the trust preferred securities issued by Valley capital trusts, except for the securities issued by VNB Capital Trust I whose related debentures are carried at fair value. Therefore, the fair value of debentures not carried at fair value is estimated utilizing the income approach, whereby the expected cash flows, over the remaining estimated life of the security, are discounted using Valley s credit spread over the current yield on a similar maturity of U.S. Treasury security or the three-month LIBOR for the variable rate indexed debentures (Level 2 inputs). Valley s credit spread was calculated based on the exchange quoted price for Valley s trust preferred securities issued by VNB Capital Trust I.

Note 6. Investment Securities

As of June 30, 2012, Valley had approximately $1.8 billion, $688.8 million, and $22.0 million in held to maturity, available for sale, and trading investment securities, respectively. Valley s investment portfolios include private label mortgage-backed securities, trust preferred securities principally issued by bank holding companies (including three pooled trust preferred securities), corporate bonds primarily issued by banks, and perpetual preferred and common equity securities issued by banks. These investments may pose a higher risk of future impairment charges by Valley as a result of the unpredictable nature of the U.S. economy and its potential negative effect on the future performance of the security issuers and, if applicable, the underlying mortgage loan collateral of the security. See the Other-Than-Temporary Impairment Analysis section below for further discussion.

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Held to Maturity

The amortized cost, gross unrealized gains and losses and fair value of securities held to maturity at June 30, 2012 and December 31, 2011 were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(in thousands)			
June 30, 2012				
U.S. Treasury securities	$ 99,945	$ 16,046	$ -	$ 115,991
Obligations of states and political subdivisions	470,133	20,697	(238)	490,592
Residential mortgage-backed securities	989,820	33,887	(78)	1,023,629
Trust preferred securities	193,287	4,026	(22,844)	174,469
Corporate and other debt securities	52,193	4,122	(274)	56,041
Total investment securities held to maturity	$ 1,805,378	$ 78,778	$ (23,434)	$ 1,860,722
December 31, 2011				
U.S. Treasury securities	$ 100,018	$ 13,841	$ -	$ 113,859
Obligations of states and political subdivisions	433,284	19,931	(14)	453,201
Residential mortgage-backed securities	1,180,104	51,041	(152)	1,230,993
Trust preferred securities	193,312	4,308	(22,867)	174,753
Corporate and other debt securities	52,198	3,799	(1,606)	54,391
Total investment securities held to maturity	$ 1,958,916	$ 92,920	$ (24,639)	$ 2,027,197

The age of unrealized losses and fair value of related securities held to maturity at June 30, 2012 and December 31, 2011 were as follows:

	Less than Twelve Months		More than Twelve Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(in thousands)					
June 30, 2012						
Obligations of states and political subdivisions	$ 15,027	$ (238)	$ -	$ -	$ 15,027	$ (238)
Residential mortgage-backed securities	33,248	(78)	-	-	33,248	(78)
Trust preferred securities	28,694	(678)	55,587	(22,166)	84,281	(22,844)
Corporate and other debt securities	-	-	23,659	(274)	23,659	(274)
Total	$ 76,969	$ (994)	$ 79,246	$ (22,440)	$ 156,215	$ (23,434)
December 31, 2011						
Obligations of states and political subdivisions	$ 1,854	$ (13)	$ 50	$ (1)	$ 1,904	$ (14)
Residential mortgage-backed securities	33,520	(152)	-	-	33,520	(152)
Trust preferred securities	35,527	(730)	55,612	(22,137)	91,139	(22,867)
Corporate and other debt securities	14,756	(192)	7,560	(1,414)	22,316	(1,606)
Total	$ 85,657	$ (1,087)	$ 63,222	$ (23,552)	$ 148,879	$ (24,639)

The total number of security positions in the securities held to maturity portfolio in an unrealized loss position at June 30, 2012 was 33 as compared to 28 at December 31, 2011.

At June 30, 2012, the unrealized losses reported for trust preferred securities mostly related to 10 single-issuer securities, issued by bank holding companies. Of the 10 trust preferred securities, 3 were investment grade, 2 were non-investment grade, and 5 were not rated. All single-issuer bank trust preferred securities classified as held to maturity are paying in accordance with their terms, have no deferrals of interest or defaults and, if applicable, the issuers meet the regulatory capital requirements to be considered well-capitalized institutions at June 30, 2012.

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Management does not believe that any individual unrealized loss as of June 30, 2012 included in the table above represents other-than-temporary impairment as management mainly attributes the declines in fair value to changes in interest rates, widening credit spreads, and lack of liquidity in the market place, not credit quality or other factors. Based on a comparison of the present value of expected cash flows to the amortized cost, management believes there are no credit losses on these securities. Valley does not have the intent to sell, nor is it more likely than not that Valley will be required to sell, the securities contained in the table above before the recovery of their amortized cost basis or maturity.

As of June 30, 2012, the fair value of investments held to maturity that were pledged to secure public deposits, repurchase agreements, lines of credit, and for other purposes required by law, was $1.0 billion.

The contractual maturities of investments in debt securities held to maturity at June 30, 2012 are set forth in the table below. Maturities may differ from contractual maturities in residential mortgage-backed securities because the mortgages underlying the securities may be prepaid without any penalties. Therefore, residential mortgage-backed securities are not included in the maturity categories in the following summary.

	June 30, 2012	
	Amortized Cost	Fair Value
	(in thousands)	
Due in one year	$ 125,089	$ 125,207
Due after one year through five years	43,210	44,738
Due after five years through ten years	232,085	256,224
Due after ten years	415,174	410,924
Residential mortgage-backed securities	989,820	1,023,629
Total investment securities held to maturity	$ 1,805,378	$ 1,860,722

Actual maturities of debt securities may differ from those presented above since certain obligations provide the issuer the right to call or prepay the obligation prior to scheduled maturity without penalty.

The weighted-average remaining expected life for residential mortgage-backed securities held to maturity was 3.2 years at June 30, 2012.

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Available for Sale

The amortized cost, gross unrealized gains and losses and fair value of securities available for sale at June 30, 2012 and December 31, 2011 were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(in thousands)			
June 30, 2012				
U.S. government agency securities	$ 53,712	$ 1,252	$ (62)	$ 54,902
Obligations of states and political subdivisions	18,447	1,212	(349)	19,310
Residential mortgage-backed securities	424,524	10,107	(4,612)	430,019
Trust preferred securities*	96,874	1,808	(15,818)	82,864
Corporate and other debt securities	47,738	4,612		