Blueknight Energy Partners, L.P.
Form 10-Q
May 09, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2012

OR

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

For the transition period from __________ to _________

Commission File Number 001-33503

BLUEKNIGHT ENERGY PARTNERS, L.P.
(Exact name of registrant as specified in its charter)

| Delaware<br>(State or other jurisdiction of incorporation or organization) | 20-8536826<br>(IRS Employer Identification No.) |
|---|---|

201 NW 10th, Suite 200
Oklahoma City, Oklahoma 73103
(Address of principal executive offices, zip code)

Registrant's telephone number, including area code: (405) 278-6400

Two Warren Place
6120 South Yale Avenue, Suite 500
Tulsa, Oklahoma 74136
(Former name, former address and former fiscal year, if changed since last report)

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

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

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

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

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

As of May 7, 2012, there were 30,159,958 Series A Preferred Units and 22,670,137 common units outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

BLUEKNIGHT ENERGY PARTNERS, L.P.
CONSOLIDATED BALANCE SHEET
(in thousands, except per unit data)

| | As of December 31, 2011 (unaudited) | As of March 31, 2012 |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $1,239 | $4,935 |
| Accounts receivable, net of allowance for doubtful accounts of $476 for both dates | 14,191 | 11,052 |
| Receivables from related parties, net of allowance for doubtful accounts of $0 for both dates | 4,397 | 2,643 |
| Prepaid insurance | 1,725 | 1,002 |
| Assets held for sale | 603 | 1,395 |
| Other current assets | 1,838 | 3,034 |
| Total current assets | 23,993 | 24,061 |
| Property, plant and equipment, net of accumulated depreciation of $135,302 and $139,381 at December 31, 2011 and March 31, 2012, respectively | 266,355 | 263,504 |
| Goodwill | 7,216 | 7,216 |
| Debt issuance costs, net | 5,000 | 4,556 |
| Intangibles and other assets, net | 2,191 | 2,006 |
| Total assets | $304,755 | $301,343 |
| LIABILITIES AND PARTNERS' CAPITAL (DEFICIT) | | |
| Current liabilities: | | |
| Accounts payable | $10,138 | $7,501 |
| Accrued loss contingency (see Note 13) | 1,090 | 1,090 |
| Accrued interest payable | 231 | 226 |
| Accrued interest payable to related parties | 362 | 161 |
| Accrued property taxes payable | 1,813 | 1,249 |
| Unearned revenue | 790 | 3,686 |
| Unearned revenue with related parties | 1,149 | 2,125 |
| Accrued payroll | 5,226 | 2,920 |
| Other accrued liabilities | 3,740 | 3,998 |
| Current portion of long-term payable to related parties | 1,636 | 1,694 |
| Total current liabilities | 26,175 | 24,650 |
| Long-term payable to related parties | 2,681 | 2,235 |
| Other long-term liabilities | 100 | 146 |
| Long-term debt (including $15.0 million with related parties for both dates) | 218,000 | 212,000 |
| Commitments and contingencies (Notes 5 and 13) | | |
| Partners' capital (deficit): | | |
| Series A Preferred Units (30,159,958 units issued and outstanding for both dates) | 202,746 | 204,599 |
| | 465,483 | 468,049 |

| | | |
|---|---|---|
| Common unitholders (22,657,638 and 22,660,137 units issued and outstanding at December 31, 2011 and March 31, 2012, respectively) | | |
| General partner interest (2.1% with 1,127,755 general partner units outstanding for both dates) | (610,430) | (610,336) |
| Total Partners' capital | 57,799 | 62,312 |
| Total liabilities and Partners' capital | $304,755 | $301,343 |

See accompanying notes to unaudited consolidated financial statements.

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BLUEKNIGHT ENERGY PARTNERS, L.P.
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per unit data)

| | Three months ended March 31, | |
|---|---|---|
| | 2011 | 2012 |
| | (unaudited) | |
| Service revenue: | | |
| Third party revenue | $31,954 | $33,134 |
| Related party revenue | 9,569 | 11,443 |
| Total revenue | 41,523 | 44,577 |
| Expenses: | | |
| Operating | 28,636 | 29,288 |
| General and administrative | 4,608 | 5,103 |
| Total expenses | 33,244 | 34,391 |
| Gain on sale of assets | 22 | 4,955 |
| Operating income: | 8,301 | 15,141 |
| Other (income) expenses: | | |
| Interest expense | 9,052 | 3,071 |
| Change in fair value of embedded derivative within convertible debt | (8,297) | — |
| Change in fair value of rights offering liability | 4,842 | — |
| Income before income taxes | 2,704 | 12,070 |
| Provision for income taxes | 70 | 76 |
| Net income | $2,634 | $11,994 |
| Allocation of net income for calculation of earnings per unit: | | |
| General partner interest in net income | $156 | $308 |
| Preferred interest in net income | $5,174 | $5,391 |
| Beneficial conversion feature attributable to preferred units | $10,899 | $1,853 |
| Income (loss) available to common and subordinated unitholders | $(13,595) | $4,442 |
| | | |
| Basic and diluted net income (loss) per common unit | $(0.39) | $0.20 |
| Basic and diluted net income (loss) per subordinated unit | $(0.39) | $— |
| | | |
| Weighted average common units outstanding - basic and diluted | 21,890 | 22,660 |
| Weighted average subordinated units outstanding - basic and diluted | 12,571 | — |

See accompanying notes to unaudited consolidated financial statements.

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BLUEKNIGHT ENERGY PARTNERS, L.P.
CONSOLIDATED STATEMENTS OF CHANGES IN PARTNERS' CAPITAL (DEFICIT)
(in thousands)

| | Common Unitholders | Series A Preferred Unitholders | General Partner Interest | Total Partners' Capital |
|---|---|---|---|---|
| | (unaudited) | | | |
| Balance, December 31, 2011 | $465,483 | $202,746 | $(610,430) | $57,799 |
| Net income | 6,672 | 5,071 | 251 | 11,994 |
| Equity-based incentive compensation | 270 | — | 5 | 275 |
| Amortization of beneficial conversion feature of Preferred units | (1,853) | 1,853 | — | — |
| Distributions | (2,523) | (5,071) | (162) | (7,756) |
| Balance, March 31, 2012 | $468,049 | $204,599 | $(610,336) | $62,312 |

See accompanying notes to unaudited consolidated financial statements.

BLUEKNIGHT ENERGY PARTNERS, L.P.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

| | Three months ended March 31, | |
|---|---|---|
| | 2011 | 2012 |
| | (unaudited) | |
| Cash flows from operating activities: | | |
| Net income | $2,634 | $11,994 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 5,705 | 5,655 |
| Amortization and write-off of debt issuance costs | 473 | 444 |
| Amortization of subordinated debenture discount | 4,354 | — |
| Change in fair value of embedded derivative within convertible debt | (8,297) | — |
| Change in fair value of rights offering liability | 4,842 | — |
| Gain on sale of assets | (22) | (4,955) |
| Equity-based incentive compensation | 42 | 275 |
| Changes in assets and liabilities | | |
| Decrease (increase) in accounts receivable | (853) | 3,139 |
| Decrease in receivables from related parties | 88 | 1,754 |
| Decrease (increase) in prepaid insurance | (22) | 858 |
| Decrease (increase) in other current assets | 533 | (1,196) |
| Decrease in other assets | 1,039 | 29 |
| Decrease in accounts payable | (1,519) | (1,868) |
| Decrease in accrued interest payable | (66) | (5) |
| Increase (decrease) in accrued interest payable to related parties | 1,113 | (201) |
| Decrease in accrued property taxes | (718) | (564) |
| Increase in unearned revenue | 79 | 2,896 |
| Increase (decrease) in unearned revenue from related parties | (29) | 976 |
| Increase (decrease) in accrued payroll | 574 | (2,306) |
| Increase in other accrued liabilities | 355 | 446 |
| Net cash provided by operating activities | 10,305 | 17,371 |
| Cash flows from investing activities: | | |
| Acquisitions | (133) | — |
| Capital expenditures | (5,762) | (6,207) |
| Proceeds from sale of assets | 22 | 6,818 |
| Net cash provided by (used in) investing activities | (5,873) | 611 |
| Cash flows from financing activities: | | |
| Payment on insurance premium financing agreement | (58) | (142) |
| Payments on long-term payable to related party | (98) | (388) |
| Borrowings under credit facility | 1,000 | 12,000 |
| Payments under credit facility | (5,000) | (18,000) |
| Distributions | — | (7,756) |
| Net cash used in financing activities | (4,156) | (14,286) |
| Net increase in cash and cash equivalents | 276 | 3,696 |
| Cash and cash equivalents at beginning of period | 4,840 | 1,239 |
| Cash and cash equivalents at end of period | $5,116 | $4,935 |
| Supplemental disclosure of cash flow information: | | |
| Increase (decrease) in accounts payable related to purchase of property, plant and equipment | $445 | $(769) |

See accompanying notes to unaudited consolidated financial statements.

BLUEKNIGHT ENERGY PARTNERS, L.P.
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION AND NATURE OF BUSINESS

Blueknight Energy Partners, L.P. (formerly SemGroup Energy Partners, L.P.) and subsidiaries (the "Partnership") is a publicly traded master limited partnership with operations in twenty-three states. The Partnership provides integrated terminalling, storage, processing, gathering and transportation services for companies engaged in the production, distribution and marketing of crude oil and asphalt products. The Partnership manages its operations through four operating segments: (i) crude oil terminalling and storage services, (ii) crude oil pipeline services, (iii) crude oil trucking and producer field services and (iv) asphalt services. The Partnership's common units and preferred units, which represent limited partnership interests in the Partnership, are listed on the NASDAQ Global Market under the symbols "BKEP" and "BKEPP," respectively. The Partnership was formed in February of 2007 as a Delaware master limited partnership initially to own, operate and develop a diversified portfolio of complementary midstream energy assets.

2. BASIS OF PRESENTATION

The financial statements have been prepared in accordance with accounting principles and practices generally accepted in the United States of America ("GAAP"). The consolidated statements of operations for the three months ended March 31, 2011 and 2012, the consolidated statement of changes in partners' capital (deficit) for the three months ended March 31, 2012, the statement of cash flows for the three months ended March 31, 2011 and 2012, and the consolidated balance sheet as of March 31, 2012 are unaudited. In the opinion of management, the unaudited consolidated financial statements have been prepared on the same basis as the audited financial statements and include all adjustments necessary to state fairly the financial position and results of operations for the respective interim periods. All adjustments are of a recurring nature unless otherwise disclosed herein. The 2011 year-end consolidated balance sheet data was derived from audited financial statements but does not include all disclosures required by GAAP. These consolidated financial statements and notes should be read in conjunction with the consolidated financial statements and notes thereto included in the Partnership's annual report on Form 10-K for the year ended December 31, 2011 filed with the Securities and Exchange Commission (the "SEC") on March 13, 2012 (the "2011 Form 10-K"). Interim financial results are not necessarily indicative of the results to be expected for an annual period. The Partnership's significant accounting policies are consistent with those disclosed in Note 4 of the Notes to Consolidated Financial Statements in our 2011 Form 10-K. A reclassification has been made in the consolidated financial statements for the three months ended March 31, 2011 to conform to the 2012 financial statement presentation. This was a reclassification of gain on sale of assets from operating expenses to a separate component of operating income. The reclassification has no impact on net income.

3. RECENT EVENTS

On January 10, 2012, the Partnership announced the planned retirement of the Chief Executive Officer of the Partnership's general partner, Mr. James Dyer, who will remain as Chief Executive Officer until his successor is appointed.

On June 1, 2012, the Partnership's crude oil storage contract with Vitol will expire according to its terms. In anticipation of such expiration, the Partnership has entered into two new crude oil storage services agreements with Vitol under which the Partnership will provide additional crude oil storage services to Vitol effective June 1, 2012. Service revenues under the first agreement are based on the one million barrels of storage capacity of the crude oil storage tanks that are dedicated to Vitol under the service agreement. The initial term of the first agreement is from June 1, 2012 through June 1, 2013. Service revenues under the second agreement are based on the 500,000 barrels of

storage capacity of the crude oil storage tanks that are dedicated to Vitol under the service agreement. The initial term of the second agreement is from June 1, 2012 through December 1, 2012. The Partnership believes that the rates it will charge to Vitol under both of these agreements are fair and reasonable to the Partnership and its unitholders and are comparable with the rates the Partnership charges third parties. The Board's conflicts committee has reviewed and approved each of these agreements in accordance with the Partnership's procedures for approval of related party transactions and the provisions of the partnership agreement.

4. PROPERTY, PLANT AND EQUIPMENT

| | Estimated Useful Lives (Years) | December 31, 2011 | March 31, 2012 |
|---|---|---|---|
| | | (dollars in thousands) | |
| Land | N/A | $16,601 | $16,355 |
| Land improvements | 10-20 | 5,671 | 5,561 |
| Pipelines and facilities | 5-30 | 152,733 | 153,949 |
| Storage and terminal facilities | 10-35 | 169,139 | 169,793 |
| Transportation equipment | 3-10 | 20,615 | 20,303 |
| Office property and equipment and other | 3-20 | 22,901 | 23,060 |
| Pipeline linefill and tank bottoms | N/A | 7,458 | 5,993 |
| Construction-in-progress | N/A | 6,539 | 7,871 |
| Property, plant and equipment, gross | | 401,657 | 402,885 |
| Accumulated depreciation | | (135,302) | (139,381) |
| Property, plant and equipment, net | | $266,355 | $263,504 |

Depreciation expense for the three months ended March 31, 2011 and 2012 was $5.7 million and $5.6 million, respectively.

5. DEBT

On October 25, 2010, the Partnership entered into a new credit agreement, which includes a $200.0 million term loan facility and a $75.0 million revolving loan facility.  On April 5, 2011, the Partnership entered into a Joinder Agreement whereby the Partnership's revolving credit facility was increased from $75.0 million to $95.0 million.  As of May 7, 2012, approximately $206.7 million of revolver borrowings and letters of credit were outstanding under the credit facility, leaving the Partnership with approximately $88.3 million available capacity for additional revolver borrowings and letters of credit under the credit facility. Vitol is a lender under the credit agreement and has committed to loan the Partnership $15.0 million pursuant to such agreement.  The proceeds of loans made under the credit agreement may be used for working capital and other general corporate purposes of the Partnership.

The credit agreement is guaranteed by all of the Partnership's existing subsidiaries. Obligations under the credit agreement are secured by first priority liens on substantially all of the Partnership's assets and those of the guarantors, including all material pipeline, gathering and processing assets, all material storage tanks and asphalt facilities, all material working capital assets and a pledge of all of the Partnership's equity interests in its subsidiaries.

The credit agreement includes procedures for additional financial institutions to become revolving lenders, or for any existing lender to increase its revolving commitment thereunder, subject to an aggregate maximum of $200.0 million for all revolving loan commitments under the credit agreement.

The credit agreement will mature on October 25, 2014, and all amounts outstanding under the credit agreement will become due and payable on such date.  The Partnership may prepay all loans under the credit agreement at any time without premium or penalty (other than customary LIBOR breakage costs), subject to certain notice requirements. The credit agreement requires mandatory prepayments of amounts outstanding thereunder with the net proceeds of certain asset sales, casualty events and debt incurrences, and, in certain circumstances, with a portion of the Partnership's excess cash flow (as defined in the credit agreement).  These mandatory prepayments will be applied to the term loan under the credit agreement until it is repaid in full, then applied to reduce commitments under the revolving loan facility.

Until approximately May 15, 2011, borrowings under the credit agreement bore interest, at the Partnership's option, at either (i) the ABR (the highest of the administrative agent's prime rate, the federal funds rate plus 0.5%, or the one-month eurodollar rate (as defined in the credit agreement) plus 1%), plus an applicable margin of 3.25%, or (ii) the eurodollar rate plus an applicable margin of 4.25%. After approximately May 15, 2011, the applicable margin for loans accruing interest based on the ABR ranges from 3.0% to 3.5%, and the applicable margin for loans accruing interest based on the eurodollar rate ranges

from 4.0% to 4.5%, in each case depending on the Partnership's consolidated total leverage ratio (as defined in the credit agreement). The Partnership pays a per annum fee on all letters of credit issued under the credit agreement, which fee equals the applicable margin for loans accruing interest based on the eurodollar rate, and the Partnership pays a commitment fee of 0.5% per annum on the unused availability under the credit agreement. The credit agreement does not have a floor for the ABR or the eurodollar rate. In connection with entering into the credit agreement, the Partnership paid certain upfront fees to the lenders thereunder, and the Partnership paid certain arrangement and other fees to the arranger and administrative agent of the credit agreement. Vitol received its pro rata portion of such fees as a lender under the credit agreement.

The credit agreement includes financial covenants that will be tested on a quarterly basis, based on the rolling four-quarter period that ends on the last day of each fiscal quarter (except for the consolidated interest coverage ratio, which builds to a four-quarter test).

The maximum permitted consolidated total leverage ratio is 4.50 to 1.00 for each future fiscal quarter.

The minimum permitted consolidated interest coverage ratio (as defined in the credit agreement) is 3.00 to 1.00 for each future fiscal quarter.

In addition, the credit agreement contains various covenants that, among other restrictions, limit the Partnership's ability to:

- create, incur or assume liens;
- engage in mergers or acquisitions;
- repurchase the Partnership's equity, make distributions to unitholders and make certain other restricted payments;
- make investments;
- modify the terms of the convertible subordinated debentures (as defined below) and certain other indebtedness, or prepay certain indebtedness;
- engage in transactions with affiliates;
- enter into certain burdensome contracts;
- change the nature of the Partnership's business;
- enter into operating leases; and
- make certain amendments to the Partnership's partnership agreement.

At March 31, 2012, the Partnership's leverage ratio was 2.90 and the interest coverage ratio was 6.41. The Partnership was in compliance with all covenants of its credit agreement as of March 31, 2012.

The credit agreement permits the Partnership to make quarterly distributions of available cash (as defined in the Partnership's partnership agreement) to unitholders so long as: (i) no default or event of default exists under the credit agreement, (ii) the Partnership has, on a pro forma basis after giving effect to such distribution, at least $10.0 million of availability under the revolving loan facility, and (iii) the Partnership's consolidated total leverage ratio, on a pro forma basis, would not be greater than 4.00 to 1.00 for any future fiscal quarter. The Partnership is currently allowed to make distributions to its unitholders in accordance with these covenants; however, the Partnership will only make distributions to the extent it has sufficient cash from operations after establishment of cash reserves as determined by the General Partner in accordance with the Partnership's cash distribution policy, including the establishment of any reserves for the proper conduct of the Partnership's business. See Note 6 for additional information regarding distributions.

Each of the following is an event of default under the credit agreement:

- failure to meet the quarterly financial covenants;

- failure to observe any other agreement, obligation or covenant in the credit agreement or any related loan document, subject to cure periods for certain failures;
- the Partnership's, or any of its subsidiaries', default under other indebtedness that exceeds a threshold amount;
- judgments against the Partnership or any of its subsidiaries, in excess of a threshold amount;
- certain ERISA events involving the Partnership or any of its subsidiaries, in excess of a threshold amount;
- bankruptcy or other insolvency events involving the Partnership or any of its subsidiaries; and

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• a change in control (as defined in the credit agreement).

If an event of default relating to bankruptcy or other insolvency events occurs, all indebtedness under the credit agreement will immediately become due and payable. If any other event of default exists under the credit agreement, the lenders may accelerate the maturity of the obligations outstanding under the credit agreement and exercise other rights and remedies. In addition, if any event of default exists under the credit agreement, the lenders may commence foreclosure or other actions against the collateral.

If any default occurs under the credit agreement, or if the Partnership is unable to make any of the representations and warranties in the credit agreement, the Partnership will be unable to borrow funds or have letters of credit issued under the credit agreement.

It will constitute a change of control under the credit agreement if either Vitol or Charlesbank ceases to own, directly or indirectly, exactly 50% of the membership interests of the General Partner or if the General Partner ceases to be controlled by both Vitol and Charlesbank.

Interest expense related to debt issuance cost amortization for the three months ended March 31, 2012 and 2011 was $0.4 million and $0.5 million, respectively. The Partnership did not capitalize any debt issuance costs for either period.

During the three months ended March 31, 2012, the weighted average interest rate under the credit agreement incurred by the Partnership was 4.69% and the total weighted average interest rate, including interest associated with the Vitol Throughput Capacity Agreement, was 5.67% resulting in interest expense of approximately $3.1 million.

In October 2010 the Partnership issued the convertible subordinated debentures in a private placement in the aggregate principal amount of $50.0 million. If not previously redeemed, the convertible subordinated debentures, including all outstanding principal and unpaid interest, would have converted to Preferred Units on December 31, 2011. Upon issuance, this conversion feature was considered an embedded derivative, which the Partnership was required to bifurcate and carry at its face value each reporting period. In connection with the establishment of the conversion price for the Preferred Units following the special meeting of the Partnership's unitholders in September 2011, the conversion option was deemed to meet the scope exception for certain contracts involving an entity's own equity in ACS 815-Derivatives and Hedging, and, therefore, the Partnership reclassified the embedded derivative as partners' capital in the third quarter of 2011. The Partnership redeemed the convertible subordinated debentures on November 9, 2011.

The Partnership estimated the fair value of the embedded derivative liability to be $27.6 million at December 31, 2010. At September 14, 2011 the fair value of this derivative liability was estimated to be $7.3 million, and subsequently, as noted above, the embedded derivative was reclassified as partners’ capital in the third quarter of 2011.

Changes to the fair value of the embedded derivative are reflected on the Partnership’s consolidated statements of operations as “Change in fair value of embedded derivative within convertible debt.” The value of the embedded derivative is contingent on changes in the expected fair value of the Partnership's preferred units. The Partnership recorded other income of $8.3 million due to the change in the fair value of this embedded derivative in the three months ended March 31, 2011.

In addition, the recording of the embedded derivative liability related to the convertible subordinated debentures resulted in the Partnership recording a $20.9 million debt discount on the convertible subordinated debentures. The debt discount was being amortized to interest expense through the mandatory conversion date of December 31, 2011 using the effective interest rate method until the redemption of the convertible subordinated debentures on November

9, 2011. Upon redemption, the remaining unamortized debt discount was considered in the calculation of the $2.4 million extinguishment gain, which was determined to represent a capital transaction and, therefore, was recorded as a capital contribution to the Partnership by the Partnership's general partner. For the purpose of calculating net income per limited partner unit, this amount was added back to net loss available to limited partners as it represents the recovery of a portion of the additional financing costs resulting from bifurcation of the conversion option and related discount on the convertible subordinated debentures. The Partnership recognized non-cash interest expense of $4.4 million in the three months ended March 31, 2011 due to the amortization of the debt discount.

## 6. DISTRIBUTIONS

The Partnership did not make a cash distribution to its common unitholders from May 15, 2008 to February 14, 2012 due, in part, to the events of default that existed under its former credit agreement, restrictions under such credit agreement, and the uncertainty of its future cash flows relating to SemCorp's bankruptcy filings ("SemCorp" refers to SemGroup Corporation and

its predecessors including SemGroup, L.P., subsidiaries and affiliates other than the Partnership and the General Partner during periods in which the Partnership and the General Partner were affiliated with SemGroup, L.P.). As a result of the approval of the Partnership Agreement Amendment Proposal (as defined in the Partnership's Proxy Statement dated July 28, 2011) on September 14, 2011, all cumulative common unit arrearages were eliminated. The Partnership's common unitholders will be required to pay taxes on their share of the Partnership's taxable income even though they did not receive a cash distribution for the quarters ended June 30, 2008 through September 30, 2011. The Partnership is currently allowed to make distributions to its unitholders in accordance with its debt covenants; however, the Partnership will only make distributions to the extent it has sufficient cash from operations after establishment of cash reserves as determined by the General Partner in accordance with the Partnership's cash distribution policy, including the establishment of any reserves for the proper conduct of the Partnership's business. The Partnership resumed distributions for common units on February 14, 2012 for the quarter ended December 31, 2011.

On April 24, 2012, the Board approved a distribution of $0.17875 per Preferred Unit, or a total distribution of $5.4 million. The Partnership will pay this distribution on the preferred units on May 15, 2012 to Preferred Unitholders of record as of May 4, 2012.

In addition, the Partnership declared a cash distribution of $0.11 per unit on its outstanding common units. The distribution will be paid on May 15, 2012 to unitholders of record on May 4, 2012. The distribution is for the three months ended March 31, 2012. The total distribution to be paid will be approximately $2.6 million, with approximately $2.5 million and $0.1 million to be paid to the Partnership's common unitholders and general partner, respectively, and $0.1 million to be paid to phantom and restricted unitholders pursuant to awards granted under the Partnership's long-term incentive plan.

## 7. NET INCOME PER LIMITED PARTNER UNIT

For purposes of calculating earnings per unit, the excess of distributions over earnings or excess of earnings over distributions for each period are allocated to the entities' general partner based on the general partner's ownership interest at the time. The following sets forth the computation of basic and diluted net loss per common and subordinated unit (in thousands, except per unit data):

| | Three months ended March 31, | | |
|---|---|---|---|
| | 2011 | 2012 | |
| Net income | $2,634 | $11,994 | |
| Less: Beneficial conversion feature attributable to preferred units | 10,899 | 1,853 | |
| Less: Preferred interest in net income | 5,174 | 5,391 | |
| Less: General partner interest in net income | 156 | 308 | |
| Net income (loss) available to common and subordinated unitholders | $(13,595) | $4,442 | |
| | | | |
| Basic and diluted weighted average number of units: | | | |
| Common units | 21,890 | 22,660 | |
| Subordinated units | 12,571 | — | (1) |
| Restricted and phantom units | 228 | 398 | |
| | | | |
| Basic and diluted net income (loss) per common unit | $(0.39) | $0.20 | |
| Basic and diluted net income (loss) per subordinated unit | $(0.39) | $— | (1) |

(1)

On September 14, 2011, Vitol and Charlesbank transferred all of the Partnership's outstanding subordinated units to the Partnership and the Partnership canceled such subordinated units.

8. RELATED PARTY TRANSACTIONS

The Partnership provides crude oil gathering, transportation, terminalling and storage services to Vitol. For the three months ended March 31, 2011, the Partnership recognized revenues of $9.6 million for services provided to Vitol. For the three months ended March 31, 2012, the Partnership recognized revenues of $11.4 million for services provided to Vitol. As of March 31, 2012, the Partnership had receivables from Vitol of $2.6 million.

Vitol Omnibus Agreement

On February 15, 2010, the Partnership entered into an Omnibus Agreement (the "Vitol Omnibus Agreement") with Vitol. Pursuant to the Vitol Omnibus Agreement, the Partnership agreed to provide certain of its employees, consultants and agents (the "Designated Persons") to Vitol for use by Vitol's crude oil marketing division. In return, Vitol agreed to reimburse the Partnership in an amount equal to (i) the wages, salaries, bonuses, make whole payments, payroll taxes and the cost of all employee benefits of each Designated Person, in each case as adjusted to properly reflect the time spent by such Designated Person in the performance services for Vitol, (ii) all direct expenses, including, without limitation, any travel and entertainment expenses, incurred by each Designated Person in connection with such Designated Person's provision of services for Vitol, (iii) a monthly charge of $1,500.00 per Designated Person for each Designated Person that performs services for Vitol during any portion of such month, plus (iv) the sum of subsections (i) through (iii) above multiplied by 0.10. In addition, the Vitol Omnibus Agreement provides that if during any month any Designated Person has spent more than 80% of his time performing services for Vitol, then Vitol will have the right for the succeeding three months to request that such individual be transitioned directly to the employment of Vitol. During the three months ended March 31, 2011, we received payments of $0.6 million pursuant to the Vitol Omnibus Agreement. The Vitol Omnibus Agreement was reviewed and approved by the Conflicts Committee in accordance with our procedures for approval of related party transactions and the provisions of our partnership agreement. The Partnership and Vitol terminated the Vitol Omnibus Agreement on March 27, 2012.

Vitol Storage Agreements

In connection with the Partnership's acquisition of certain of its crude oil storage assets from SemCorp in May 2008, the Partnership was assigned from SemCorp a storage agreement with Vitol under which the Partnership provides crude oil storage services to Vitol (the "2008 Vitol Storage Agreement"). The initial term of the 2008 Vitol Storage Agreement was from June 1, 2008 through June 30, 2010. This agreement was amended in 2010 to extend the term of the agreement until June 1, 2011 and again in 2011 to extend the term of the agreement to June 1, 2012. Because Vitol was a third party (and not a related or affiliated party) at the time of entering into the 2008 Vitol Storage Agreement, such agreement was not approved by the Board or the Board's conflicts committee in accordance with the Partnership's procedures for approval of related party transactions. Vitol became a related party when it acquired the Partnership's General Partner in November 2009. Since the amendments occurred subsequent to the Vitol Change of Control, they were reviewed and approved by the Board's conflicts committee in accordance with the Partnership's procedures for approval of related party transactions and the provisions of the partnership agreement. The Partnership earned revenues of approximately $3.3 million and $3.3 million from Vitol with respect to services provided pursuant to the 2008 Vitol Storage Agreement for the three months ended March 31, 2011 and 2012, respectively. The Partnership believes that the rates it charges Vitol under the 2008 Vitol Storage Agreement are fair and reasonable to the Partnership and its unitholders and are comparable with the rates the Partnership charges third parties.

In March of 2010, the Partnership entered into a second crude oil storage services agreement with Vitol under which the Partnership began providing additional crude oil storage services to Vitol effective May 1, 2010 (the "2010 Vitol Storage Agreement"). The initial term of the 2010 Vitol Storage Agreement is five years commencing on May 1, 2010, subject to automatic renewal periods for successive one year periods until terminated by either party with ninety days prior notice. The 2010 Vitol Storage Agreement was reviewed and approved by the Board's conflicts committee in accordance with the Partnership's procedures for approval of related party transactions and the provisions of the partnership agreement. The Partnership generated revenues under this agreement of approximately $3.1 million and $3.1 million during the three months ended March 31, 2011 and 2012, respectively. The Partnership believes that the rates it charges Vitol under the 2010 Vitol Storage Agreement are fair and reasonable to the Partnership and its unitholders and are comparable with the rates the Partnership charges third parties.

On June 1, 2012, the 2008 Vitol Storage Agreement will expire according to its terms. In anticipation of such expiration, the Partnership has entered into two new crude oil storage services agreements with Vitol. See Note 3 for additional information regarding the new agreements with Vitol.

Vitol Master Lease Agreement

In July of 2010, the Partnership and Vitol entered into a Master Agreement (the "Master Agreement") relating to the lease of certain vehicles by the Partnership from Vitol. Pursuant to the Master Agreement, the Partnership may lease certain vehicles, including light duty trucks, tractors, tank trailers and bobtail tank trucks, from Vitol for periods ranging from 36 months to 84 months depending on the type of vehicle. The Partnership will have the opportunity to purchase each vehicle at the end of the lease at the estimated residual value of such vehicle. Leases under the Master Agreement are accounted for as operating leases. During the three months ended March 31, 2011, the Partnership recorded expenses under this agreement of

approximately $0.2 million. The Master Agreement was approved by the Board's conflicts committee in accordance with the Partnership's procedures for approval of related party transactions and the provisions of its partnership agreement. In September of 2011, the Partnership entered into a new master lease agreement with an unrelated third party and terminated the Master Agreement with Vitol.

Vitol Throughput Capacity Agreement

In August of 2010, the Partnership and Vitol entered into a Throughput Capacity Agreement (the "ENPS Throughput Agreement"). Pursuant to the ENPS Throughput Agreement, Vitol purchased 100% of the throughput capacity on the Partnership's Eagle North Pipeline System ("ENPS"). The Partnership put ENPS in service in December of 2010. In September 2010, Vitol paid the Partnership a prepaid fee equal to $5.5 million and Vitol will pay additional usage fees for every barrel delivered by or on behalf of Vitol on ENPS. This $5.5 million fee received from Vitol is accounted for as a long-term payable to a related party and is reflected as such on the Partnership's consolidated balance sheet as of March 31, 2012. In addition, if the payments made by Vitol in any contract year under the ENPS Throughput Agreement are in the aggregate less than $2.4 million, then Vitol will pay the Partnership a deficiency payment equal to $2.4 million minus the aggregate amount of all payments made by Vitol during such contract year. In March 2012, the Partnership received a deficiency payment of $0.3 million from Vitol in relation to the 2011 contract year. The ENPS Throughput Agreement has a term that extends for four years after ENPS is completed and may be extended by mutual agreement of the parties for additional one-year terms. If the capacity on ENPS is unavailable for use by Vitol for more than 60 days, whether consecutive or nonconsecutive, during the term of the ENPS Throughput Agreement, then Vitol shall have the right to terminate the ENPS Throughput Agreement within six months after such lack of capacity. The Partnership has previously contracted to provide throughput services on ENPS to a third party and Vitol's rights to the capacity of ENPS are subordinate to the rights of such third party. In addition, for so long as a default by Vitol relating to payments under the ENPS Throughput Agreement has not occurred and is continuing, the Partnership will remit to Vitol any and all tariffs and deficiency payments received by the Partnership or its affiliates from such third party pursuant to its agreement with the Partnership. The ENPS Throughput Agreement was approved by the Board's conflicts committee in accordance with the Partnership's procedures for approval of related party transactions and the provisions of its partnership agreement.

During the three months ended March 31, 2011 and 2012, the Partnership incurred interest expense under this agreement of approximately $0.2 million and $0.1 million, respectively. The agreement has an effective annual interest rate of 14.1% and matures on December 31, 2014.

Vitol's Commitment under the Partnership's Credit Agreement

Vitol is a lender under the Partnership's current credit agreement and has committed to loan the Partnership $15.0 million pursuant to such agreement. During the three months ended March 31, 2011 and 2012, Vitol received its pro rata portion of the interest payments in connection with being a lender under the credit agreement and received approximately $0.2 million and $0.2 million, respectively, in connection therewith.

9. LONG-TERM INCENTIVE PLAN

In July of 2007, the General Partner adopted the Blueknight Energy Partners G.P., L.L.C. Long-Term Incentive Plan (the "Plan"). The compensation committee of the Board administers the Plan. The Plan authorizes the grant of an aggregate of 2.6 million common units deliverable upon vesting. On September 14, 2011, the Partnership's unitholders approved an amendment to the Plan to increase the number of common units issuable under such plan by 1.35 million common units from 1.25 million common units to 2.6 million common units. Although other types of awards are contemplated under the Plan, currently outstanding awards include "phantom" units, which convey the right to receive common units upon vesting, and "restricted" units, which are grants of common units restricted until the time

of vesting. The phantom unit awards also include distribution equivalent rights ("DERs").

Subject to applicable earning criteria, a DER entitles the grantee to a cash payment equal to the cash distribution paid on an outstanding common unit prior to the vesting date of the underlying award. Recipients of restricted units are entitled to receive cash distributions paid on common units during the vesting period which distributions are reflected initially as a reduction of partners' capital. Distributions paid on units which ultimately do not vest are reclassified as compensation expense. Awards granted to date are equity awards and, accordingly, the fair value of the awards as of the grant date is expensed over the vesting period.

In March 2011 and March 2012, grants for 299,900 and 351,300 phantom common units, respectively, were made, which vest on January 1, 2014 and January 1, 2015, respectively. These grants are equity awards under ASC 718 – Stock

Compensation, and, accordingly, the fair value of the awards as of the grant date is expensed over the vesting period. The weighted average grant date fair-value of the awards is $8.25 and $6.76 per unit, respectively, which is the closing market price on the grant date of the awards. The value of these award grants was approximately $2.5 million and $2.4 million, respectively, on their grant date, and the unrecognized estimated compensation cost at March 31, 2012 was $3.4 million, which will be recognized over the remaining vesting period. As of March 31, 2012, the Partnership expects approximately 87% of these awards will vest. The Partnership's equity-based incentive compensation expense for the three months ended March 31, 2012 was $0.3 million.

Activity pertaining to phantom common units and restricted common unit awards granted under the Plan is as follows:

| | Number of Units | Weighted Average Grant Date Fair Value |
|---|---|---|
| Nonvested at December 31, 2011 | 307,151 | $8.17 |
| Granted | 351,300 | 6.76 |
| Vested | 10,000 | 8.25 |
| Forfeited | 6,200 | 8.25 |
| Nonvested at March 31, 2012 | 642,251 | $7.40 |

## 10. EMPLOYEE BENEFIT PLAN

Under the Partnership's 401(k) Plan, which was formed in 2009, employees who meet specified service requirements may contribute a percentage of their total compensation, up to a specified maximum, to the plan. The Partnership may match each employee's contribution, up to a specified maximum, in full or on a partial basis. The Partnership recognized expense of $0.4 million and $0.3 million, respectively, for the three months ended March 31, 2011 and 2012, respectively, for discretionary contributions under the plan.

The Partnership may also make annual lump-sum contributions to the 401(k) Plan irrespective of the employee's contribution match. The Partnership may make a discretionary annual contribution in the form of profit sharing calculated as a percentage of an employee's eligible compensation. This contribution is retirement income under the qualified Plan. Annual profit sharing contributions to the Plan are submitted to and approved by the Board. The Partnership recognized expense of $0.2 million and $0.2 million for the three months ended March 31, 2011 and 2012, respectively, for discretionary profit sharing contributions under the Plan.

## 11. FAIR VALUE MEASUREMENTS

The Partnership utilizes a three-tier framework for assets and liabilities required to be measured at fair value. In addition, the Partnership uses valuation techniques, such as the market approach (comparable market prices), the income approach (present value of future income or cash flow), and the cost approach (cost to replace the service capacity of an asset or replacement cost) to value these assets and liabilities as appropriate. The Partnership uses an exit price when determining the fair value. The exit price represents amounts that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants.

The Partnership utilizes a three-tier fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The following is a brief description of those three levels:

Level 1 Observable inputs such as quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 Inputs other than quoted prices that are observable for these assets or liabilities, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.

| Level 3 | Unobservable inputs in which there is little market data, which requires the reporting entity to develop its own assumptions |
|---|---|

This hierarchy requires the use of observable market data, when available, and to minimize the use of unobservable inputs when determining fair value.

The Partnership had no recurring financial assets or liabilities subject to fair value measurements as of December 31, 2011 or March 31, 2012.

The fair value of the embedded derivative within the subordinated convertible debentures was derived using a valuation model and has been classified as Level 3. The valuation model used is a discounted cash flow model (income approach) that assumes future distribution payments by the Partnership and utilizes interest rates and credit spreads for subordinated debt to preferred equity to determine the fair value of the derivative embedded within the subordinated convertible debentures. The change in fair value of the derivative liability for the three months ended March 31, 2011 of $8.3 million is included in other (income) expense in the Partnership's consolidated statements of operations. In connection with the establishment of the conversion price for the Preferred Units following the special meeting of the Partnership's unitholders in September 2011, the number of Preferred Units issuable upon conversion of the subordinated convertible debentures was an amount equal to (i) the sum of the outstanding principal and any accrued and unpaid interest being converted, divided by (ii) 6.50. The establishment of the conversion rate resulted in the embedded derivative meeting the scope exception in ASC 815-15 – Embedded Derivatives, and, therefore, the Partnership reclassified the embedded derivative as partners' capital on September 14, 2011.

The fair value of the rights offering liability related to certain rights that have been offered to common unitholders under the approved Global Transaction Agreement was derived using a valuation model and has been classified as Level 3. The valuation model used is a probability-weighted model (income approach) and assumes the number of rights that are exercised as well as the expected fair value of the Preferred Units at the time such rights are exercised. The change in fair value of the rights offering liability for the three months ended March 31, 2011 of $4.8 million is included in other (income) expense in the Partnership's consolidated statements of operations.

The following table sets forth a reconciliation of changes in the fair value of the Partnership's financial liabilities classified as Level 3 in the fair value hierarchy (in thousands):

| | Measurements Using Significant Unobservable Inputs (Level 3) For the Three Months Ended March 31, 2011 |
|---|---|
| Beginning Balance | $39,511 |
| Total gains or losses (realized/unrealized): | |
| Included in earnings | (3,455) |
| Included in other comprehensive income | — |
| Purchases, issuances, and settlements[1] | — |
| Transfers in and/or out of Level 3 | — |
| Balance at March 31, 2011 | $36,056 |
| The amount of total income for the period included in earnings attributable to the change in unrealized gains for liabilities still held at the reporting date | $(3,455) |

(1) As noted above, the Partnership reclassified the embedded derivative within subordinated convertible debentures to partners' capital as of September 14, 2011.

Fair Value of Other Financial Instruments

The following disclosure of the estimated fair value of financial instruments is made in accordance with accounting guidance for financial instruments. The Partnership has determined the estimated fair values by using available market information and valuation methodologies. Considerable judgment is required in interpreting market data to develop the estimates of fair value. The use of different market assumptions or valuation methodologies may have a material effect on the estimated fair value amounts.

At March 31, 2012, the carrying values on the unaudited condensed consolidated balance sheets for cash and cash equivalents (classified as Level 1), accounts receivable and accounts payable approximate their fair value because of their short term nature.



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Based on the borrowing rates currently available to the Partnership for credit agreement debt with similar terms and maturities and consideration of the Partnership's non-performance risk, long-term debt associated with the Partnership's credit agreement at March 31, 2012 approximates its fair value. The fair value of the Partnership's long-term debt was calculated using observable inputs (LIBOR for the risk free component) and unobservable company-specific credit spread information. As such, the Partnership considers this debt to be Level 3.

| | | |
|---|---|---|
| Proceeds from issuance of common stock upon exercise of stock options | 312 | 836 |
| Cash dividends paid | (11,747) | (11,885) |
| Net cash provided by financing activities | 264,623 | 50,618 |
| Net decrease in cash and cash equivalents | (97) | (19,623) |
| Cash and cash equivalents, beginning of period | 40,425 | 55,721 |
| Cash and cash equivalents, end of period | $40,328 | $36,098 |
| SUPPLEMENTAL CASH FLOW DISCLOSURE | | |
| Interest paid | $40,944 | $48,365 |
| Income taxes paid | 11,996 | 15,520 |
| Taxes paid if excess tax benefits were not tax deductible | 12,335 | 15,631 |
| Non-cash activities: | | |
| Loans transferred to real estate owned | 4,543 | 3,541 |
| Loans provided for the sale of real estate owned | 3,011 | 1,646 |
| Loans held for investment transferred to held for sale | 13,008 | 8,780 |
| Loans held for sale transferred to held for investment | 2,214 | - |

The accompanying notes are an integral part of these consolidated financial statements.

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PART I – FINANCIAL INFORMATION
FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
Consolidated Statements of Changes in Stockholders' Equity
(Unaudited)

| (Dollars in thousands, except per share data) | For the nine months ended September 30, 2013 | 2012 |
|---|---|---|
| Common Stock | | |
| Balance, beginning of period | $ 315 | $ 315 |
| No activity | - | - |
| Balance, end of period | $ 315 | $ 315 |
| Additional Paid-In Capital | | |
| Balance, beginning of period | $ 198,314 | $ 195,628 |
| Award of common shares released from Employee Benefit Trust (141,059 and 154,543 common shares for the nine months ended September 30, 2013 and 2012, respectively) | 1,608 | 1,442 |
| Shares issued upon vesting of restricted stock unit awards (120,014 and 113,272 common shares for the nine months ended September 30, 2013 and 2012, respectively) | 161 | 317 |
| Issuance upon exercise of stock options (235,025 and 154,543 common shares for the nine months ended September 30, 2013 and 2012, respectively) | 849 | 160 |
| Stock-based compensation activity, net | (284) | 670 |
| Stock-based income tax benefit | 339 | 111 |
| Balance, end of period | $ 200,987 | $ 198,328 |
| Treasury Stock | | |
| Balance, beginning of period | $ (10,257) | $ (7,355) |
| Purchases of shares outstanding (836,092 and 181,000 common shares for the nine months ended September 30, 2013, and 2012, respectively) | (13,152) | (2,444) |
| Shares issued upon vesting of restricted stock unit awards (176,656 and 142,222 common shares for the nine months ended September 30, 2013 and 2012, respectively) | 2,338 | 1,686 |
| Issuance upon exercise of stock options (300,195 and 138,025 common shares for the nine months ended September 30, 2013 and 2012, respectively) | 4,262 | 1,665 |
| Purchases of shares to fund options exercised (233,933 and 60,571 common shares for the nine months ended September 30, 2013 and 2012, respectively) | (4,075) | (835) |
| Repurchase of shares to satisfy tax obligations (57,411 and 38,723 common shares for the nine months ended September 30, 2013 and 2012, respectively) | (912) | (511) |
| Balance, end of period | $ (21,796) | $ (7,794) |
| Retained Earnings | | |
| Balance, beginning of period | $ 241,856 | $ 223,510 |
| Net income | 25,804 | 25,131 |
| Cash dividends declared and paid on common shares ($0.39 per common share for the nine months ended September 30, 2013 and 2012, respectively) | (11,747) | (11,885) |
| Issuance upon exercise of stock options (65,170 and 10,480 common shares for the nine months ended September 30, 2013 and 2012, respectively) | (126) | (37) |
| Shares issued upon vesting of restricted stock unit awards (56,642 and 28,950 common shares for the nine months ended September 30, 2013 and 2012, respectively) | (100) | (97) |
| Balance, end of period | $ 255,687 | $ 236,622 |
| Accumulated Other Comprehensive Income (Loss) | | |
| Balance, beginning of period | $ 12,137 | $ 4,813 |
| | (19,947) | 8,303 |

| | | |
|---|---|---|
| Change in net unrealized gains (losses) on securities available for sale, net of taxes of approximately $15,482 and ($6,401) for the nine months ended September 30, 2013 and 2012, respectively | | |
| Amortization of actuarial losses, net of taxes of approximately ($405) and ($347) for the nine months ended September 30, 2013 and 2012, respectively | 522 | 447 |
| Amortization of prior service credits, net of taxes of approximately $15 and $10 for the nine month periods ended September 30, 2013 and 2012, respectively | (19 ) | (19 ) |
| OTTI charges included in income, net of taxes of approximately ($620) and ($339) for the nine months ended September 30, 2013 and 2012, respectively) | 799 | 437 |
| Reclassification adjustment for gains included in net income, net of tax of approximately $1,299 and $42 for the nine months ended September 30, 2013 and 2012, respectively | (1,673 ) | (54 ) |
| Balance, end of period | $ (8,181 ) | $ 13,927 |
| | | |
| Total Stockholders' Equity | $ 427,012 | $ 441,398 |

The accompanying notes are an integral part of these consolidated financial statements.

PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
Notes to Consolidated Financial Statements
(Unaudited)

## 1. Basis of Presentation

Flushing Financial Corporation (the "Holding Company"), a Delaware corporation, is a bank holding company. On February 28, 2013 the Holding Company's wholly owned subsidiary Flushing Savings Bank, FSB (the "Savings Bank"), merged with and into Flushing Commercial Bank (the "Merger"). Flushing Commercial Bank was the surviving entity of the Merger and its name was changed to Flushing Bank. References herein to the "Bank" mean the Savings Bank (including its wholly owned subsidiary, Flushing Commercial Bank) prior to the Merger and the surviving entity after the Merger. The Holding Company and its direct and indirect wholly-owned subsidiaries, including the Bank, Flushing Preferred Funding Corporation, Flushing Service Corporation, and FSB Properties Inc., are collectively herein referred to as "we," "us," "our" and the "Company."

The Merger was the result of the combination of two entities under common control, and in accordance with ASC 805-50-30-5, the Bank measured the recognized assets and liabilities transferred at their carrying amounts (historical cost) for this transaction.

The primary business of the Holding Company is the operation of its wholly-owned subsidiary, the Bank. The unaudited consolidated financial statements presented in this Quarterly Report on Form 10-Q ("Quarterly Report") include the collective results of the Company on a consolidated basis.

The Holding Company also owns Flushing Financial Capital Trust II, Flushing Financial Capital Trust III, and Flushing Financial Capital Trust IV (the "Trusts"), which are special purpose business trusts. The Trusts are not included in the Company's consolidated financial statements as the Company would not absorb the losses of the Trusts if losses were to occur.

The accompanying unaudited consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") and general practices within the banking industry. The information furnished in these interim statements reflects all adjustments which are, in the opinion of management, necessary for a fair statement of the results for such presented periods of the Company. Such adjustments are of a normal recurring nature, unless otherwise disclosed in this Quarterly Report. All inter-company balances and transactions have been eliminated in consolidation. The results of operations in the interim statements are not necessarily indicative of the results that may be expected for the full year.

The accompanying unaudited consolidated financial statements have been prepared in conformity with the instructions to Quarterly Report on Form 10-Q and Article 10, Rule 10-01 of Regulation S-X for interim financial statements. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). The unaudited consolidated interim financial information should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2012.

## 2. Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenue and expenses during the reporting period. Estimates that are particularly susceptible to change in the near term are used in connection with the determination of

the allowance for loan losses (“ALLL”), the evaluation of goodwill for impairment, the evaluation of the need for a valuation allowance of the Company’s deferred tax assets, the evaluation of other-than-temporary impairment (“OTTI”) on securities and the valuation of certain financial instruments. The current economic environment has increased the degree of uncertainty inherent in these material estimates. Actual results could differ from these estimates.

## 3. Earnings Per Share

Earnings per share is computed in accordance with Accounting Standards Codification (“ASC”) Topic 260 “Earnings Per Share,” which provides that unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and as such should be included in the calculation of earnings per share. Basic earnings per common share is computed by dividing net income available to common shareholders by the total weighted average number of common shares outstanding, which includes unvested participating securities. The Company’s unvested restricted stock unit awards are considered participating securities. Therefore, weighted average common shares outstanding used for computing basic earnings per common share includes common shares outstanding plus unvested restricted stock unit awards. The computation of diluted earnings per share includes the additional dilutive effect of stock options outstanding during the period. Common stock equivalents that are anti-dilutive are not included in the computation of diluted earnings per common share. The numerator for calculating basic and diluted earnings per common share is net income available to common shareholders.

PART I – FINANCIAL INFORMATION
FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
Notes to Consolidated Financial Statements
(Unaudited)

Earnings per common share has been computed based on the following:

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| | (In thousands, except per share data) | | | |
| Net income, as reported | $9,421 | $9,365 | $ 25,804 | $ 25,131 |
| Divided by: | | | | |
| Weighted average common shares outstanding | 29,773 | 30,432 | 30,143 | 30,434 |
| Weighted average common stock equivalents | 32 | 30 | 25 | 30 |
| Total weighted average common shares outstanding and common stock equivalents | 29,805 | 30,462 | 30,168 | 30,464 |
| | | | | |
| Basic earnings per common share | $0.32 | $0.31 | $ 0.86 | $ 0.83 |
| Diluted earnings per common share (1) | $0.32 | $0.31 | $ 0.86 | $ 0.82 |
| Dividend payout ratio | 40.6 % | 41.9 % | 45.3 % | 47.0 % |

(1) For the three months ended September 30, 2013, options to purchase 111,050 shares at an average exercise price of $19.56 were not included in the computation of diluted earnings per common share as they are anti-dilutive. For the nine months ended September 30, 2013, options to purchase 320,200 shares at an average exercise price of $18.33 were not included in the computation of diluted earnings per common share as they are anti-dilutive. For the three and nine months ended September 30, 2012, options to purchase 557,140 shares at an average exercise price of $17.62 were not included in the computation of diluted earnings per common share as they are anti-dilutive.

4. Debt and Equity Securities

The Company's investments in equity securities that have readily determinable fair values and all investments in debt securities are classified in one of the following three categories and accounted for accordingly: (1) trading securities, (2) securities available for sale and (3) securities held-to-maturity.

The Company did not hold any trading securities or securities held-to-maturity during the three and nine months ended September 30, 2013 and 2012. Securities available for sale are recorded at fair value.

The following table summarizes the Company's portfolio of securities available for sale at September 30, 2013:

| | Amortized Cost | Fair Value | Gross Unrealized Gains | Gross Unrealized Losses |
|---|---|---|---|---|
| | | | (In thousands) | |
| Corporate | $122,883 | $125,922 | $ 3,982 | $ 943 |
| Municipals | 116,105 | 112,164 | 213 | 4,154 |
| Mutual funds | 21,631 | 21,631 | - | - |
| Other | 17,422 | 13,627 | - | 3,795 |

| | | | | |
|---|---|---|---|---|
| Total other securities | 278,041 | 273,344 | 4,195 | 8,892 |
| REMIC and CMO | 524,071 | 525,819 | 10,464 | 8,716 |
| GNMA | 41,334 | 43,431 | 2,458 | 361 |
| FNMA | 204,573 | 201,909 | 3,089 | 5,753 |
| FHLMC | 13,899 | 14,051 | 272 | 120 |
| Total mortgage-backed securities | 783,877 | 785,210 | 16,283 | 14,950 |
| Total securities available for sale | $1,061,918 | $1,058,554 | $ 20,478 | $ 23,842 |

PART I – FINANCIAL INFORMATION
FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
Notes to Consolidated Financial Statements
(Unaudited)

Mortgage-backed securities shown in the table above include three private issue collateralized mortgage obligations ("CMOs") that are collateralized by commercial real estate mortgages with amortized cost and market values totaling $14.6 million and $14.7 million, respectively, at September 30, 2013. The remaining private issue mortgage-backed securities are backed by one-to-four family residential mortgage loans.

The following table shows the Company's available for sale securities with gross unrealized losses and their fair value aggregated by category and length of time the individual securities have been in a continuous unrealized loss position at September 30, 2013:

| | Total | | Less than 12 months | | 12 months or more | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | (In thousands) | | | | | |
| Corporate | $39,057 | $ 943 | $39,057 | $ 943 | $- | $ - |
| Municipals | 83,204 | 4,154 | 83,204 | 4,154 | - | - |
| Other | 5,767 | 3,795 | - | - | 5,767 | 3,795 |
| Total other securities | 128,028 | 8,892 | 122,261 | 5,097 | 5,767 | 3,795 |
| REMIC and CMO | 244,699 | 8,716 | 226,568 | 7,669 | 18,131 | 1,047 |
| GNMA | 9,524 | 361 | 9,524 | 361 | - | - |
| FNMA | 104,550 | 5,753 | 104,550 | 5,753 | - | - |
| FHLMC | 7,786 | 120 | 7,786 | 120 | - | - |
| | | | | | | |
| Total mortgage-backed securities | 366,559 | 14,950 | 348,428 | 13,903 | 18,131 | 1,047 |
| Total securities available for sale | $494,587 | $ 23,842 | $470,689 | $ 19,000 | $23,898 | $ 4,842 |

OTTI losses on impaired securities must be fully recognized in earnings if an investor has the intent to sell the debt security or if it is more likely than not that the investor will be required to sell the debt security before recovery of its amortized cost. However, even if an investor does not expect to sell a debt security, the investor must evaluate the expected cash flows to be received and determine if a credit loss has occurred. In the event that a credit loss has occurred, only the amount of impairment associated with the credit loss is recognized in earnings in the Consolidated Statements of Income. Amounts relating to factors other than credit losses are recorded in accumulated other comprehensive income (loss) ("AOCI") within Stockholders' Equity. Additional disclosures regarding the calculation of credit losses as well as factors considered by the investor in reaching a conclusion that an investment is not other-than-temporarily impaired are required.

The Company reviewed each investment that had an unrealized loss at September 30, 2013. An unrealized loss exists when the current fair value of an investment is less than its amortized cost basis. Unrealized losses on available for sale securities, that are deemed to be temporary, are recorded in AOCI, net of tax. Unrealized losses that are considered to be other-than-temporary are split between credit related and noncredit related impairments, with the credit related impairment being recorded as a charge against earnings and the noncredit related impairment being recorded in AOCI, net of tax.

The Company evaluates its pooled trust preferred securities, included in the table above in the row labeled "Other", using an impairment model through an independent third party, which includes evaluating the financial condition of each counterparty. For single issuer trust preferred securities, the Company evaluates the issuer's financial condition.

The Company evaluates its mortgage-backed securities by reviewing the characteristics of the securities and related collateral, including delinquency and foreclosure levels, projected losses at various loss severity levels and credit enhancement and coverage. In addition, private issue CMOs are evaluated using an impairment model through an independent third party. When an OTTI is identified, the portion of the impairment that is credit related is determined by management using the following methods: (1) for pooled trust preferred securities, the credit related impairment is determined by using a discounted cash flow model from an independent third party, with the difference between the present value of the projected cash flows and the amortized cost basis of the security recorded as a credit related loss against earnings; (2) for mortgage-backed securities, credit related impairment is determined for each security by estimating losses based on a set of assumptions of the related collateral, which includes delinquency and foreclosure levels, projected losses at various loss severity levels, credit enhancement and coverage; and (3) for private issue CMOs, through an impairment model from an independent third party and then recording those estimated losses as a credit related loss against earnings.

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Corporate:

The unrealized losses in Corporate securities at September 30, 2013 consist of losses on four Corporate securities. The unrealized losses were caused by movements in interest rates. It is not anticipated that these securities would be settled at a price that is less than the amortized cost of the Company's investment. Each of these securities is performing according to its terms and, in the opinion of management, will continue to perform according to its terms. The Company does not have the intent to sell these securities and it is more likely than not the Company will not be required to sell the securities before recovery of the securities' amortized cost basis. This conclusion is based upon considering the Company's cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the securities. Therefore, the Company did not consider these investments to be other-than-temporarily impaired at September 30, 2013.

Municipals:

The unrealized losses in Municipal securities at September 30, 2013, consist of losses on 27 municipal securities. The unrealized losses were caused by movements in interest rates. It is not anticipated that these securities would be settled at a price that is less than the amortized cost of the Company's investment. Each of these securities is performing according to its terms and, in the opinion of management, will continue to perform according to its terms. The Company does not have the intent to sell these securities and it is more likely than not the Company will not be required to sell the securities before recovery of the securities' amortized cost basis. This conclusion is based upon considering the Company's cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the securities. Therefore, the Company did not consider these investments to be other-than-temporarily impaired at September 30, 2013.

Other Securities:

The unrealized losses in Other Securities at September 30, 2013, consist of losses on one single issuer trust preferred security and two pooled trust preferred securities. The unrealized losses on such securities were caused by market interest volatility, a significant widening of credit spreads across markets for these securities and illiquidity and uncertainty in the financial markets. These securities are currently rated below investment grade. The pooled trust preferred securities do not have collateral that is subordinate to the classes the Company owns. The Company's management evaluates these securities using an impairment model, through an independent third party, that is applied to debt securities. In estimating OTTI losses, management considers: (1) the length of time and the extent to which the fair value has been less than amortized cost; (2) the current interest rate environment; (3) the financial condition and near-term prospects of the issuer, if applicable; and (4) the intent and ability of the Company to retain its investment in the security for a period of time sufficient to allow for any anticipated recovery in fair value. Additionally, management reviews the financial condition of the single issuer trust preferred security and each individual issuer within the pooled trust preferred securities. All of the issuers of the underlying collateral of the pooled trust preferred securities we reviewed are banks.

For each bank, our review included the following performance items:

§ Ratio of tangible equity to assets
§ Tier 1 Risk Weighted Capital
§ Net interest margin
§ Efficiency ratio for most recent two quarters
§ Return on average assets for most recent two quarters
§ Texas Ratio (ratio of non-performing assets plus assets past due over 90 days divided by tangible equity plus the reserve for loan losses)

- Credit ratings (where applicable)
- Capital issuances within the past year (where applicable)
- Ability to complete Federal Deposit Insurance Corporation ("FDIC") assisted acquisitions (where applicable)

Based on the review of the above factors, we concluded that:

- All of the performing issuers in our pools are well capitalized banks and do not appear likely to be closed by their regulators.

- All of the performing issuers in our pools will continue as a going concern and will not default on their securities.

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In order to estimate potential future defaults and deferrals, we segregated the performing underlying issuers by their Texas Ratio. We then reviewed performing issuers with Texas Ratios in excess of 50%. The Texas Ratio is a key indicator of the health of the institution and the likelihood of failure. This ratio compares the problem assets of the institution to the institution's available capital and reserves to absorb losses that are likely to occur in these assets. There was one issuer in our pooled trust preferred securities which had a Texas Ratio in excess of 50%. We assigned a 25% default rate to this issuer. All other issuers in our pooled trust preferred securities had a Texas Ratio below 50%. We assigned a zero percent default rate to these issuers. Our analysis also assumed that issuers currently deferring would default with no recovery, and issuers that have defaulted will have no recovery.

We had an independent third party prepare a discounted cash flow analysis for each of these pooled trust preferred securities based on the assumptions discussed above. Other significant assumptions were: (1) two issuers totaling $21.5 million will prepay in the second quarter of 2015; (2) senior classes will not call the debt on their portions; and (3) use of the forward London Interbank Offered Rate ("LIBOR") curve. The cash flows were discounted at the effective rate for each security.

One of the pooled trust preferred securities is over 90 days past due and the Company has stopped accruing interest. The remaining pooled trust preferred security as well as the single issuer trust preferred security are both performing according to their terms. The Company also owns a pooled trust preferred security that is carried under the fair value option, where the unrealized losses are included in the Consolidated Statements of Income – Net gain (loss) from fair value adjustments. This security is over 90 days past due and the Company has stopped accruing interest.

It is not anticipated at this time that the one single issuer trust preferred security and the two pooled trust preferred securities would be settled at a price that is less than the amortized cost of the Company's investment. Each of these securities is performing according to its terms; except for the pooled trust preferred securities for which the Company has stopped accruing interest as discussed above and, in the opinion of management based on the review performed at September 30, 2013, will continue to perform according to its terms. The Company does not have the intent to sell these securities and it is more likely than not the Company will not be required to sell the securities before recovery of the securities' amortized cost basis. This conclusion is based upon considering the Company's cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the securities. Therefore, the Company did not consider the one single issuer trust preferred security and the two pooled trust preferred securities to be other-than-temporarily impaired at September 30, 2013.

At September 30, 2013, the Company held five trust preferred issues which had a current credit rating of at least one rating below investment grade. Two of those issues are carried under the fair value option and therefore, changes in fair value are included in the Consolidated Statement of Income – Net gain (loss) from fair value adjustments.

The following table details the remaining three trust preferred issues that were evaluated to determine if they were other-than-temporarily impaired at September 30, 2013. The class the Company owns in pooled trust preferred securities does not have any excess subordination.

| | | | | | | Deferrals/Defaults (1) | |
|---|---|---|---|---|---|---|---|
| Issuer Type | Class | Performing Banks | Amortized Cost | Fair Value | Cumulative Credit Related OTTI | Actual as a Percentage of Original Security | Expected Percentage of Performing Collateral |

(Dollars in thousands)

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Single issuer | n/a | 1 | $300 | $287 | $- | None | | None |
| Pooled issuer | B1 | 17 | 5,617 | 2,880 | 2,196 | 23.4% | 0.0% | |
| Pooled issuer | C1 | 16 | 3,645 | 2,600 | 1,542 | 21.3% | 1.5% | |
| Total | | | $9,562 | $5,767 | $3,738 | | | |

(1) Represents deferrals/defaults as a percentage of the original security and expected deferrals/defaults as a percentage of performing issuers.

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REMIC and CMO:
The unrealized losses in Real Estate Mortgage Investment Conduit ("REMIC") and CMO securities at September 30, 2013 consist of 11 issues from the Federal Home Loan Mortgage Corporation ("FHLMC"), 15 issues from the Federal National Mortgage Association ("FNMA"), three issues from the Government National Mortgage Association ("GNMA") and six private issues.

The unrealized losses on the REMIC and CMO securities issued by FHLMC, FNMA, GNMA and one private issue were caused by movements in interest rates. It is not anticipated that these securities would be settled at a price that is less than the amortized cost of the Company's investment. Each of these securities is performing according to its terms and, in the opinion of management, will continue to perform according to its terms. The Company does not have the intent to sell these securities and it is more likely than not the Company will not be required to sell the securities before recovery of the securities' amortized cost basis. This conclusion is based upon considering the Company's cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the securities. Therefore, the Company did not consider these investments to be other-than-temporarily impaired at September 30, 2013.

The unrealized losses at September 30, 2013 on the remaining five REMIC and CMO securities issued by private issuers were caused by movements in interest rates, a significant widening of credit spreads across markets for these securities and illiquidity and uncertainty in the financial markets. Each of these securities has some level of credit enhancements and none are collateralized by sub-prime loans. Currently, one of these securities is performing according to its terms, with four of these securities remitting less than the full principal amount due. The principal loss for these four securities totaled $0.7 million for the nine months ended September 30, 2013. These losses were anticipated in the cumulative credit related OTTI charges recorded for these four securities.

Credit related impairment for mortgage-backed securities are determined for each security by estimating losses based on the following set of assumptions: (1) delinquency and foreclosure levels; (2) projected losses at various loss severity levels; and (3) credit enhancement and coverage. Based on these reviews, an OTTI charge was recorded during the three and nine months ended September 30, 2013. During the three months ended September 30, 2013, an OTTI charge was recorded on three private issue CMOs of $1.6 million before tax, of which $0.9 million was charged against earnings in the Consolidated Statements of Income and $0.7 million before tax ($0.4 million after-tax) was recorded in AOCI. During the nine months ended September 30, 2013, an OTTI charge was recorded on four private issue CMOs of $2.5 million before tax, of which $1.4 million was charged against earnings in the Consolidated Statements of Income and $1.1 million before tax ($0.6 million after-tax) was recorded in AOCI.

The portion of the above mentioned OTTI, recorded during the three and nine ended September 30, 2013, that was related to credit losses was calculated using the following significant assumptions: (1) delinquency and foreclosure levels of 7% - 24%; (2) projected loss severity of 40% - 50%; (3) assumed default rates of 6% - 12% for the first 12 months, 2% - 10% for the next 12 months, 2% - 8% for the next six months, 2% - 6% for the next six months and 2% - 4% for the next 12 months and 2% thereafter; and (4) prepayment speeds of 6% - 10%.

It is not anticipated at this time that the one private issue CMO, for which an OTTI charge during the three and nine months ended September 30, 2013 was not recorded, would be settled at a price that is less than the current amortized cost of the Company's investment. The security is performing according to its terms and in the opinion of management, will continue to perform according to its terms. The Company does not have the intent to sell this security and it is more likely than not the Company will not be required to sell the security before recovery of the

security's amortized cost basis. This conclusion is based upon considering the Company's cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the security. Therefore, the Company did not consider this investment to be other-than-temporarily impaired at September 30, 2013.

At September 30, 2013, the Company held five private issue CMOs which had a current credit rating of at least one rating below investment grade.

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The following table details the five private issue CMOs that were evaluated to determine if they were other-than-temporarily impaired at September 30, 2013:

| Security | Amortized Cost | Fair Value | Outstanding Principal | Cumulative OTTI Charges Recorded | Year of Issuance | Maturity | Current Lowest Rating | Collateral Located in: CA | FL | VA | NY | NJ | TX | CO | Avera FIC Scor |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | (Dollars in thousands) | | | | | | | | | | | | | | |
| 1 | $8,287 | $8,179 | $9,541 | $3,966 | 2006 | 05/25/36 | Caa3 | 42% | | | 16% | | | | 718 |
| 2 | 3,206 | 2,822 | 3,447 | 931 | 2006 | 08/19/36 | D | 55% | | | | | | 11% | 740 |
| 3 | 3,956 | 3,723 | 4,425 | 1,341 | 2006 | 08/25/36 | D | 36% | 15% | | | | | | 711 |
| 4 | 2,538 | 2,173 | 3,492 | 1,266 | 2006 | 08/25/36 | D | 41% | 13% | | 13% | | 10% | | 687 |
| 5 | 3,678 | 3,297 | 3,954 | 222 | 2006 | 05/25/36 | CC | 23% | | 17% | 13% | 14% | | | 709 |
| Total | $21,665 | $20,194 | $24,859 | $7,726 | | | | | | | | | | | |

GNMA, FNMA and FHLMC:

The unrealized losses in GNMA, FNMA and FHLMC securities at September 30, 2013 consist of losses on one GNMA security, 14 FNMA securities and one FHLMC security. The unrealized losses were caused by movements in interest rates. It is not anticipated that these securities would be settled at a price that is less than the amortized cost of the Company's investment. Each of these securities is performing according to its terms and, in the opinion of management, will continue to perform according to its terms. The Company does not have the intent to sell these securities and it is more likely than not the Company will not be required to sell the securities before recovery of the securities' amortized cost basis. This conclusion is based upon considering the Company's cash and working capital requirements, and contractual and regulatory obligations, none of which the Company believes would cause the sale of the securities. Therefore, the Company did not consider these investments to be other-than-temporarily impaired at September 30, 2013.

The following table details gross unrealized losses recorded in AOCI and the ending credit loss amount on debt securities, as of September 30, 2013, for which the Company has recorded a credit related OTTI charge in the Consolidated Statements of Income:

| (in thousands) | Amortized Cost | Fair Value | Gross Unrealized Losses Recorded In AOCI | Cumulative Credit OTTI Losses |
|---|---|---|---|---|
| Private issued CMO's (1) | $ 21,665 | $ 20,194 | $ 1,471 | $ 3,185 |
| Trust preferred securities (1) | 9,262 | 5,480 | 3,782 | 3,738 |
| | | | | |
| Total | $ 30,927 | $ 25,674 | $ 5,253 | $ 6,923 |

(1) The Company has recorded OTTI charges in the Consolidated Statements of Income on five private issue CMOs and two pooled trust preferred securities for which a portion of the OTTI is currently recorded in AOCI.

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The following table represents the activity related to the credit loss component recognized in earnings on debt securities held by the Company for which a portion of OTTI was recognized in AOCI for the period indicated:

| (in thousands) | For the three months ended September 30, 2013 | For the three months ended September 30, 2012 | For the nine months ended September 30, 2013 | For the nine months ended September 30, 2012 |
|---|---|---|---|---|
| Beginning balance | $ 6,193 | $ 6,938 | $ 6,178 | $ 6,922 |
| Recognition of actual losses | (186 ) | (185 ) | (674 ) | (945 ) |
| OTTI charges due to credit loss recorded in earnings | 916 | - | 1,419 | 776 |
| Securities sold during the period | - | - | - | - |
| Securities where there is an intent to sell or requirement to sell | - | - | - | - |
| Ending balance | $ 6,923 | $ 6,753 | $ 6,923 | $ 6,753 |

The following table details the amortized cost and estimated fair value of the Company's securities classified as available for sale at September 30, 2013, by contractual maturity. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | Amortized Cost (In thousands) | Fair Value (In thousands) |
|---|---|---|
| Due in one year or less | $22,631 | $22,631 |
| Due after one year through five years | 59,412 | 62,140 |
| Due after five years through ten years | 64,132 | 63,450 |
| Due after ten years | 131,866 | 125,123 |
| Total other securities | 278,041 | 273,344 |
| Mortgage-backed securities | 783,877 | 785,210 |
| Total securities available for sale | $1,061,918 | $1,058,554 |

During the three months ended September 30, 2013, the Company sold $5.9 million in corporate securities and recorded gross gains of $0.1 million. During the nine months ended September 30, 2013, the Company sold $68.5 million in mortgage-backed securities and $5.9 million in corporates securities and recorded gross gains of $3.3 million and gross losses of $0.5 million. During the three and nine months ended September 30, 2012, the Company sold $6.8 million in mortgage-backed securities and recorded gross gains of $119,000 and gross losses of $23,000. The Company used the specific identification method to calculate gross gains and losses from the sale of securities during the three and nine months ended September 30, 2013 and 2012.

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The following table summarizes the Company's portfolio of securities available for sale at December 31, 2012:

| | Amortized Cost | Fair Value | Gross Unrealized Gains | Gross Unrealized Losses |
|---|---|---|---|---|
| | | | (In thousands) | |
| U.S. government agencies | $31,409 | $ 31,513 | $ 104 | $ - |
| Corporate | 83,389 | 87,485 | 4,096 | - |
| Municipals | 74,228 | 75,297 | 1,152 | 83 |
| Mutual funds | 21,843 | 21,843 | - | - |
| Other | 17,797 | 13,315 | 17 | 4,499 |
| Total other securities | 228,666 | 229,453 | 5,369 | 4,582 |
| REMIC and CMO | 453,468 | 474,050 | 23,690 | 3,108 |
| GNMA | 43,211 | 46,932 | 3,721 | - |
| FNMA | 168,040 | 175,929 | 7,971 | 82 |
| FHLMC | 22,562 | 23,202 | 640 | - |
| Total mortgage-backed securities | 687,281 | 720,113 | 36,022 | 3,190 |
| Total securities available for sale | $915,947 | $ 949,566 | $ 41,391 | $ 7,772 |

Mortgage-backed securities shown in the table above include two private issue CMOs that are collateralized by commercial real estate mortgages with amortized cost and market values of $15.2 million and $15.7 million, respectively, at December 31, 2012. The remaining private issue mortgage-backed securities are backed by one-to-four family residential mortgage loans.

The following table shows the Company's available for sale securities with gross unrealized losses and their fair value, aggregated by category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2012.

| | Total | | Less than 12 months | | 12 months or more | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | | | (In thousands) | | | |
| Municipals | $9,782 | $ 83 | $9,782 | $ 83 | $- | $ - |
| Other | 5,064 | 4,499 | - | - | 5,064 | 4,499 |
| Total other securities | 14,846 | 4,582 | 9,782 | 83 | 5,064 | 4,499 |
| | | | | | | |
| REMIC and CMO | 64,126 | 3,108 | 40,651 | 155 | 23,475 | 2,953 |
| FNMA | 10,331 | 82 | 10,331 | 82 | - | - |
| Total mortgage-backed securities | 74,457 | 3,190 | 50,982 | 237 | 23,475 | 2,953 |
| Total securities available for sale | $89,303 | $ 7,772 | $60,764 | $ 320 | $28,539 | $ 7,452 |

5. Loans

Loans are reported at their outstanding principal balance, net of any unearned income, charge-offs, deferred loan fees and costs on originated loans and unamortized premiums or discounts on purchased loans. Interest on loans is recognized on the accrual basis. The accrual of income on loans is generally discontinued when certain factors, such

as contractual delinquency of 90 days or more, indicate reasonable doubt as to the timely collectability of such income. Uncollected interest previously recognized on non-accrual loans is reversed from interest income at the time the loan is placed on non-accrual status. A non-accrual loan can be returned to accrual status when contractual delinquency returns to less than 90 days delinquent. Subsequent cash payments received on non-accrual loans that do not bring the loan to less than 90 days delinquent are recorded on a cash basis. Subsequent cash payments can also be applied first as a reduction of principal until all principal is recovered and then subsequently to interest, if in management's opinion, it is evident that recovery of all principal due is unlikely to occur. Net loan origination costs and premiums or discounts on loans purchased are amortized into interest income over the contractual life of the loans using the level-yield method. Prepayment penalties received on loans which pay in full prior to their scheduled maturity are included in interest income in the period they are collected.

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The Company maintains an allowance for loan losses at an amount, which in management's judgment, is adequate to absorb probable estimated losses inherent in the loan portfolio. Management's judgment in determining the adequacy of the allowance is based on evaluations of the collectability of loans. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revisions as more information becomes available. In assessing the adequacy of the Company's allowance for loan losses, management considers various factors such as, the current fair value of collateral for collateral dependent loans, the Company's historical loss experience, recent trends in losses, collection policies and collection experience, trends in the volume of non-performing and classified loans, changes in the composition and volume of the gross loan portfolio and local and national economic conditions. The Company's Board of Directors (the "Board of Directors") reviews and approves management's evaluation of the adequacy of the allowance for loan losses on a quarterly basis.

The allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. Increases and decreases in the allowance for loan losses other than charge-offs and recoveries are included in the provision for loan losses. When a loan or a portion of a loan is determined to be uncollectible, the portion deemed uncollectible is charged against the allowance and subsequent recoveries, if any, are credited to the allowance.

The Company recognizes a loan as non-performing when the borrower has indicated the inability to bring the loan current, or due to other circumstances which, in the Company's opinion, indicate the borrower will be unable to bring the loan current within a reasonable time. All loans classified as non-performing, which includes all loans past due 90 days or more, are classified as non-accrual unless there is, in the Company's opinion, compelling evidence the borrower will bring the loan current in the immediate future. The Company's management considers all non-accrual loans impaired. Appraisals and/or updated internal evaluations are obtained as soon as practical and before the loan become 90 days delinquent.

A loan is considered impaired when, based upon the most current information, the Company believes it is probable that it will be unable to collect all amounts due, both principal and interest, according to the contractual terms of the loan. Impaired loans are measured based on the present value of the expected future cash flows discounted at the loan's effective interest rate, or at the loan's observable market price, or the fair value of the collateral if the loan is collateral dependent. The Company considers fair value of collateral dependent loans to be 85% of the appraised or internally estimated value of the property. Interest income on impaired loans is recorded on a cash basis. The loan balances of collateral dependent impaired loans are compared to the loan's updated fair value. The balance which exceeds fair value is generally charged-off.

The Company reviews each impaired loan to determine if a charge-off is to be recorded or if a valuation allowance is to be allocated to the loan. The Company does not allocate a valuation allowance to loans for which we have concluded the current value of the underlying collateral will allow for recovery of the loan balance either through the sale of the loan or by foreclosure and sale of the property.

The Company evaluates the underlying collateral through a third party appraisal, or when a third party appraisal is not available, the Company will use an internal evaluation. The internal evaluations are performed using an income approach or a sales approach. The income approach is used for income producing properties and uses current revenues less operating expenses to determine the net cash flow of the property. Once the net cash flow is determined, the value of the property is calculated using an appropriate capitalization rate for the property. The sales approach uses comparable sales prices in the market.  When an internal evaluation is used, we place greater reliance on the income approach to value the collateral.

In preparing internal evaluations of property values, the Company seeks to obtain current data on the subject property from various sources, including: (1) the borrower; (2) copies of existing leases; (3) local real estate brokers and appraisers; (4) public records (such as for real estate taxes and water and sewer charges); (5) comparable sales and rental data in the market; (6) an inspection of the property; and (7) interviews with tenants. These internal evaluations primarily focus on the income approach and comparable sales data to value the property.

As of September 30, 2013, the Company utilized recent third party appraisals of the collateral to measure impairment for $75.0 million, or 82.8%, of collateral dependent impaired loans and used internal evaluations of the property's value for $15.1 million, or 17.2%, of collateral dependent impaired loans.

The Company may restructure a loan to enable a borrower to continue making payments when it is deemed to be in the Company's best long-term interest. This restructure may include reducing the interest rate or amount of the monthly payment for a specified period of time, after which the interest rate and repayment terms revert to the original terms of the loan. We classify these loans as Troubled Debt Restructured ("TDR") when the Bank grants a concession to a borrower who is experiencing financial difficulties.

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These restructurings have not included a reduction of principal balance. The Company believes that restructuring these loans in this manner will allow certain borrowers to become and remain current on their loans. All loans classified as TDR are considered impaired, however TDR loans which have been current for six consecutive months at the time they are restructured as TDR remain on accrual status and are not included as part of non-performing loans. Loans which were delinquent at the time they are restructured as a TDR are placed on non-accrual status and reported as non-performing loans until they have made timely payments for six consecutive months. Loans that are restructured as TDR but are not performing in accordance with the restructured terms are placed on non-accrual status and reported as non-performing loans.

The allocation of a portion of the allowance for loan losses for a performing TDR loan is based upon the present value of the future expected cash flows discounted at the loan's original effective rate, or for a non-performing TDR which is collateral dependent, the fair value of the collateral. At September 30, 2013, there were no commitments to lend additional funds to borrowers whose loans were modified as TDRs. The modification of loans to a TDR did not have a significant effect on our operating results, nor did it require a significant allocation of the allowance for loan losses.

There were no loans modified and classified as TDR during the three months ended September 30, 2013.

The following table shows loans modified and classified as TDR during the period incicated:

| | For the thee months ended September 30, 2012 | | |
|---|---|---|---|
| (Dollars in thousands) | Number | Balance | Modification description |
| One-to-four family - residential | 1 | $400 | Received a below market interest rate |
| Commercial business and other | 2 | 1,900 | Received a below market interest rate and the loan amortization was extended |
| Total | 3 | $2,300 | |

The following table shows loans modified and classified as TDR during the periods indicated:

| | For the nine months ended September 30, 2013 | | |
|---|---|---|---|
| (Dollars in thousands) | Number | Balance | Modification description |
| Multi-family residential | 1 | $ 413 | Received a below market interest rate and the loan amortization was extended |
| Commercial real estate | 2 | 761 | Received a below market interest rate and the loan amortization was extended |
| One-to-four family - mixed-use property | 1 | 390 | Received a below market interest rate and the loan amortization was extended |
| One-to-four family - residential | - | - | |

| | | | |
|---|---|---|---|
| Commercial business and other | 1 | 615 | Received a below market interest rate and the loan amortization was extended |
| Total | 5 | $ 2,179 | |

| | | For the nine months ended September 30, 2012 | |
|---|---|---|---|
| (Dollars in thousands) | Number | Balance | Modification description |
| Multi-family residential | - | $ - | |
| Commercial real estate | 3 | 5,300 | Received a below market interest rate and the loan amortization was extended |
| One-to-four family - mixed-use property | 3 | 1,200 | Received a below market interest rate |
| One-to-four family - residential | 1 | 400 | Received a below market interest rate |
| Commercial business and other | 2 | 1,900 | Received a below market interest rate and the loan amortization was extended |
| Total | 9 | $ 8,800 | |

The recorded investment of each of the loans modified and classified to a TDR, presented in the table above, was unchanged as there was no principal forgiven in any of these modifications.

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The following table shows our recorded investment for loans classified as TDR that are performing according to their restructured terms at the periods indicated:

| (Dollars in thousands) | September 30, 2013 Number of contracts | September 30, 2013 Recorded investment | December 31, 2012 Number of contracts | December 31, 2012 Recorded investment |
|---|---|---|---|---|
| Multi-family residential | 9 | $ 2,812 | 8 | $ 2,347 |
| Commercial real estate | 6 | 8,652 | 5 | 8,499 |
| One-to-four family - mixed-use property | 8 | 2,704 | 7 | 2,336 |
| One-to-four family - residential | 1 | 367 | 1 | 374 |
| Construction | 1 | 1,916 | 1 | 3,805 |
| Commercial business and other | 3 | 3,082 | 2 | 2,540 |
| Total performing troubled debt restructured | 28 | $ 19,533 | 24 | $ 19,901 |

The following table shows our recorded investment for loans classified as TDR that are not performing according to their restructured terms at the periods indicated:

| (Dollars in thousands) | September 30, 2013 Number of contracts | September 30, 2013 Recorded investment | December 31, 2012 Number of contracts | December 31, 2012 Recorded investment |
|---|---|---|---|---|
| Multi-family residential | - | $ - | 2 | $ 323 |
| Commercial real estate | 2 | 2,705 | 2 | 3,075 |
| One-to-four family - mixed-use property | - | - | 2 | 816 |
| Construction | 1 | 5,000 | 1 | 7,368 |
| Total troubled debt restructurings that subsequently defaulted | 3 | $ 7,705 | 7 | $ 11,582 |

During the nine months ended September 30, 2013, there were no loans classified as performing TDR transferred to non-performing TDR.

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The following table shows our non-performing loans at the periods indicated:

| (Dollars in thousands) | September 30, 2013 | December 31, 2012 |
|---|---|---|
| Loans ninety days or more past due and still accruing: | | |
| Multi-family residential | $ 479 | $ - |
| Commercial real estate | 298 | - |
| One-to-four family - residential | 15 | - |
| Commercial Business and other | 502 | 644 |
| Total | 1,294 | 644 |
| | | |
| Non-accrual mortgage loans: | | |
| Multi-family residential | 17,999 | 13,095 |
| Commercial real estate | 10,653 | 15,640 |
| One-to-four family - mixed-use property | 9,854 | 16,553 |
| One-to-four family - residential | 13,229 | 13,726 |
| Co-operative apartments | 160 | 234 |
| Construction | 367 | 7,695 |
| Total | 52,262 | 66,943 |
| | | |
| Non-accrual non-mortgage loans: | | |
| Small Business Administration | - | 283 |
| Commercial Business and other | 2,564 | 16,860 |
| Total | 2,564 | 17,143 |
| | | |
| Total non-accrual loans | 54,826 | 84,086 |
| | | |
| Total non-accrual loans and loans ninety days or more past due and still accruing | $ 56,120 | $ 84,730 |

The table above does not include $5.0 million and $5.3 million of Substandard loans held for sale at September 30, 2013 and December 31, 2012, respectively.

The following is a summary of interest foregone on non-accrual loans and loans classified as TDR for the periods indicated:

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| | (In thousands) | | | |
| Interest income that would have been recognized had the loans performed in accordance with their original terms | $ 1,507 | $ 2,177 | $ 4,520 | $ 6,650 |
| | 225 | 251 | 959 | 1,136 |

| | | | | |
|---|---|---|---|---|
| Less: Interest income included in the results of operations | | | | |
| Total foregone interest | $ 1,282 | $ 1,926 | $ 3,561 | $ 5,514 |

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The following table shows an aged analysis of our recorded investment in loans at September 30, 2013:

| (in thousands) | 30 - 59 Days Past Due | 60 - 89 Days Past Due | Greater than 90 Days | Total Past Due | Current | Total Loans |
|---|---|---|---|---|---|---|
| Multi-family residential | $ 15,471 | $ 2,864 | $ 17,999 | $ 36,334 | $ 1,647,943 | $ 1,684,277 |
| Commercial real estate | 9,378 | 5,015 | 10,653 | 25,046 | 491,268 | 516,314 |
| One-to-four family - mixed-use property | 19,497 | 685 | 9,854 | 30,036 | 565,399 | 595,435 |
| One-to-four family - residential | 2,276 | 1,200 | 13,018 | 16,494 | 180,165 | 196,659 |
| Co-operative apartments | - | - | 160 | 160 | 10,005 | 10,165 |
| Construction loans | - | - | 367 | 367 | 4,278 | 4,645 |
| Small Business Administration | 148 | - | - | 148 | 7,855 | 8,003 |
| Taxi medallion | - | - | - | - | 5,088 | 5,088 |
| Commercial business and other | - | - | 773 | 773 | 363,296 | 364,069 |
| Total | $ 46,770 | $ 9,764 | $ 52,824 | $ 109,358 | $ 3,275,297 | $ 3,384,655 |

The following table shows an aged analysis of our recorded investment in loans at December 31, 2012:

| (in thousands) | 30 - 59 Days Past Due | 60 - 89 Days Past Due | Greater than 90 Days | Total Past Due | Current | Total Loans |
|---|---|---|---|---|---|---|
| | | | (in thousands) | | | |
| Multi-family residential | $ 24,059 | $ 4,828 | $ 13,095 | $ 41,982 | $ 1,492,456 | $ 1,534,438 |
| Commercial real estate | 9,764 | 3,622 | 15,639 | 29,025 | 486,413 | 515,438 |
| One-to-four family - mixed-use property | 21,012 | 3,368 | 16,554 | 40,934 | 596,419 | 637,353 |
| One-to-four family - residential | 3,407 | 2,010 | 13,602 | 19,019 | 179,949 | 198,968 |
| Co-operative apartments | - | - | 234 | 234 | 6,069 | 6,303 |
| Construction loans | 2,462 | - | 7,695 | 10,157 | 4,224 | 14,381 |
| Small Business Administration | 404 | - | 283 | 687 | 8,809 | 9,496 |
| Taxi medallion | - | - | - | - | 9,922 | 9,922 |
| Commercial business and other | 2 | 5 | 15,601 | 15,608 | 279,468 | 295,076 |
| Total | $ 61,110 | $ 13,833 | $ 82,703 | $ 157,646 | $ 3,063,729 | $ 3,221,375 |

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The following table shows the activity in the allowance for loan losses for the three months ended September 30, 2013:

| (in thousands) | Multi-family residential | Commercial real estate | One-to-four family - mixed-use property | One-to-four family - residential | Co-operative apartments | Construction loans | Small Business Administration | Taxi medallion | Commercial business and other | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Allowance for credit losses: | | | | | | | | | | |
| Beginning balance | $12,958 | $5,884 | $6,434 | $2,099 | $99 | $196 | $497 | $4 | $4,184 | $32,355 |
| Charge-off's | (710) | (171) | (645) | (4) | - | (2,374) | (89) | - | (1,193) | (5,186) |
| Recoveries | 90 | - | 58 | 11 | - | - | 17 | - | 36 | 212 |
| Provision | (561) | (603) | 76 | (152) | - | 2,443 | 71 | (4) | 2,165 | 3,435 |
| Ending balance | $11,777 | $5,110 | $5,923 | $1,954 | $99 | $265 | $496 | $- | $5,192 | $30,816 |
| Ending balance: individually evaluated for impairment | $265 | $270 | $649 | $59 | $- | $17 | $- | $- | $166 | $1,426 |
| Ending balance: collectively evaluated for impairment | $11,512 | $4,840 | $5,274 | $1,895 | $99 | $248 | $496 | $- | $5,026 | $29,390 |
| | | | | | | | | | | |
| Financing Receivables: | | | | | | | | | | |
| Ending balance | $1,684,277 | $516,314 | $595,435 | $196,659 | $10,165 | $4,645 | $8,003 | $5,088 | $364,069 | $3,384,655 |
| Ending balance: individually evaluated for impairment | $26,068 | $24,738 | $16,980 | $15,120 | $164 | $2,341 | $- | $- | $5,110 | $90,521 |
| Ending balance: collectively evaluated for impairment | $1,658,209 | $491,576 | $578,455 | $181,539 | $10,001 | $2,304 | $8,003 | $5,088 | $358,959 | $3,294,134 |

The following table shows the activity in the allowance for loan losses for the three months ended September 30, 2012:

| (in thousands) | Multi-family residential | Commercial real estate | One-to-four family - mixed-use property | One-to-four family - residential | Co-operative apartments | Construction loans | Small Business Administration | Taxi medallion | Commercial business and other | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Allowance for credit losses: | | | | | | | | | | |
| Beginning balance | $12,065 | $6,329 | $5,786 | $1,821 | $100 | $727 | $656 | $28 | $3,387 | $30,899 |
| Charge-off's | (3,090) | (179) | (1,072) | (198) | (19) | (59) | (59) | - | (965) | (5,641 |
| Recoveries | 9 | 124 | 258 | - | - | - | 36 | - | 2 | 429 |
| Provision | 3,596 | (397) | 983 | 340 | (33) | (602) | (54) | (18) | 1,185 | 5,000 |
| Ending balance | $12,580 | $5,877 | $5,955 | $1,963 | $48 | $66 | $579 | $10 | $3,609 | $30,687 |
| Ending balance: individually evaluated for impairment | $62 | $385 | $713 | $95 | $- | $50 | $- | $- | $304 | $1,609 |
| Ending balance: collectively evaluated for impairment | $12,518 | $5,492 | $5,242 | $1,868 | $48 | $16 | $579 | $10 | $3,305 | $29,078 |
| | | | | | | | | | | |
| Financing Receivables: | | | | | | | | | | |
| Ending balance | $1,482,765 | $527,337 | $653,151 | $202,291 | $6,632 | $16,319 | $10,764 | $13,103 | $260,998 | $3,173,360 |
| Ending balance: individually evaluated for impairment | $23,049 | $25,368 | $31,208 | $15,429 | $237 | $16,319 | $1,404 | $- | $25,300 | $138,314 |
| Ending balance: collectively evaluated for impairment | $1,459,716 | $501,969 | $621,943 | $186,862 | $6,395 | $- | $9,360 | $13,103 | $235,698 | $3,035,046 |

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The following table shows the activity in the allowance for loan losses for the nine months ended September 30, 2013:

| (in thousands) | Multi-family residential | Commercial real estate | One-to-four family - mixed-use property | One-to-four family - residential | Co-operative apartments | Construction loans | Small Business Administration | Taxi medallion | Commercial business and other | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Allowance for credit losses: | | | | | | | | | | |
| Beginning balance | $13,001 | $5,705 | $5,960 | $1,999 | $46 | $66 | $505 | $7 | $3,815 | $31,104 |
| Charge-off's | (3,459) | (905) | (3,780) | (695) | (74) | (2,678) | (426) | - | (2,057) | (14,074) |
| Recoveries | 155 | 293 | 169 | 117 | 4 | - | 77 | - | 36 | 851 |
| Provision | 2,080 | 17 | 3,574 | 533 | 123 | 2,877 | 340 | (7) | 3,398 | 12,935 |
| Ending balance | $11,777 | $5,110 | $5,923 | $1,954 | $99 | $265 | $496 | $- | $5,192 | $30,816 |
| Ending balance: individually evaluated for impairment | $265 | $270 | $649 | $59 | $- | $17 | $- | $- | $166 | $1,426 |
| Ending balance: collectively evaluated for impairment | $11,512 | $4,840 | $5,274 | $1,895 | $99 | $248 | $496 | $- | $5,026 | $29,390 |
| Financing Receivables: | | | | | | | | | | |
| Ending balance | $1,684,277 | $516,314 | $595,435 | $196,659 | $10,165 | $4,645 | $8,003 | $5,088 | $364,069 | $3,384,655 |
| Ending balance: individually evaluated for impairment | $26,068 | $24,738 | $16,980 | $15,120 | $164 | $2,341 | $- | $- | $5,110 | $90,521 |
| Ending balance: collectively evaluated for impairment | $1,658,209 | $491,576 | $578,455 | $181,539 | $10,001 | $2,304 | $8,003 | $5,088 | $358,959 | $3,294,134 |

The following table shows the activity in the allowance for loan losses for the nine months ended September 30, 2012:

| (in thousands) | Multi-family residential | Commercial real estate | One-to-four family - mixed-use property | One-to-four family - residential | Co-operative apartments | Construction loans | Small Business Administration | Taxi medallion | Commercial business and other | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Allowance for credit losses: | | | | | | | | | | |
| Beginning balance | $11,267 | $5,210 | $5,314 | $1,649 | $80 | $668 | $987 | $41 | $5,128 | $30,344 |
| Charge-off's | (5,252 ) | (2,401 ) | (3,401 ) | (1,096 ) | (62 ) | (2,500 ) | (324 ) | - | (1,488 ) | (16,524 |
| Recoveries | 89 | 249 | 337 | 29 | - | - | 59 | - | 104 | 867 |
| Provision | 6,476 | 2,819 | 3,705 | 1,381 | 30 | 1,898 | (143 ) | (31 ) | (135 ) | 16,000 |
| Ending balance | $12,580 | $5,877 | $5,955 | $1,963 | $48 | $66 | $579 | $10 | $3,609 | $30,687 |
| Ending balance: individually evaluated for impairment | $62 | $385 | $713 | $95 | $- | $50 | $- | $- | $304 | $1,609 |
| Ending balance: collectively evaluated for impairment | $12,518 | $5,492 | $5,242 | $1,868 | $48 | $16 | $579 | $10 | $3,305 | $29,078 |
| | | | | | | | | | | |
| Financing Receivables: | | | | | | | | | | |
| Ending balance | $1,482,765 | $527,337 | $653,151 | $202,291 | $6,632 | $16,319 | $10,764 | $13,103 | $260,998 | $3,173,360 |
| Ending balance: individually evaluated for impairment | $23,049 | $25,368 | $31,208 | $15,429 | $237 | $16,319 | $1,404 | $- | $25,300 | $138,314 |
| Ending balance: collectively evaluated for impairment | $1,459,716 | $501,969 | $621,943 | $186,862 | $6,395 | $- | $9,360 | $13,103 | $235,698 | $3,035,046 |

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The following table shows our recorded investment, unpaid principal balance and allocated allowance for loan losses, average recorded investment and interest income recognized for loans that were considered impaired at or for the nine month period ended September 30, 2013:

| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment | Interest Income Recognized |
|---|---|---|---|---|---|
| | | | (Dollars in thousands) | | |
| With no related allowance recorded: | | | | | |
| Mortgage loans: | | | | | |
| Multi-family residential | $23,043 | $ 26,245 | $ - | $ 23,219 | $ 208 |
| Commercial real estate | 16,836 | 17,786 | - | 20,887 | 205 |
| One-to-four family mixed-use property | 13,210 | 15,685 | - | 14,305 | 149 |
| One-to-four family residential | 14,753 | 18,840 | - | 14,697 | 330 |
| Co-operative apartments | 164 | 282 | - | 232 | - |
| Construction | 425 | 651 | - | 5,351 | - |
| Non-mortgage loans: | | | | | |
| Small Business Administration | - | - | - | 329 | - |
| Taxi Medallion | - | - | - | - | - |
| Commercial Business and other | 2,028 | 4,328 | - | 6,003 | 110 |
| Total loans with no related allowance recorded | 70,459 | 83,817 | - | 85,023 | 1,002 |
| With an allowance recorded: | | | | | |
| Mortgage loans: | | | | | |
| Multi-family residential | 3,025 | 3,026 | 265 | 2,839 | 109 |
| Commercial real estate | 7,902 | 7,968 | 270 | 7,506 | 232 |
| One-to-four family mixed-use property | 3,770 | 3,769 | 649 | 3,991 | 165 |
| One-to-four family residential | 367 | 367 | 59 | 369 | 11 |
| Co-operative apartments | - | - | - | - | - |
| Construction | 1,916 | 1,916 | 17 | 2,323 | 48 |
| Non-mortgage loans: | | | | | |
| Small Business Administration | - | - | - | - | - |
| Taxi Medallion | - | - | - | - | - |
| Commercial Business and other | 3,082 | 3,082 | 166 | 4,174 | 111 |
| Total loans with an allowance recorded | 20,062 | 20,128 | 1,426 | 21,202 | 676 |
| Total Impaired Loans: | | | | | |
| Total mortgage loans | $85,411 | $ 96,535 | $ 1,260 | $ 95,719 | $ 1,457 |

| | | | | | |
|---|---|---|---|---|---|
| Total non-mortgage loans | $5,110 | $ 7,410 | $ 166 | $ 10,506 | $ 221 |

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The following table shows our recorded investment, unpaid principal balance and allocated allowance for loan losses, average recorded investment and interest income recognized for loans that were considered impaired at or for the year ended December 31, 2012:

| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment | Interest Income Recognized |
|---|---|---|---|---|---|
| | | | (Dollars in thousands) | | |
| With no related allowance recorded: | | | | | |
| Mortgage loans: | | | | | |
| Multi-family residential | $ 19,753 | $ 22,889 | $ - | $ 27,720 | $ 429 |
| Commercial real estate | 34,672 | 38,594 | - | 43,976 | 536 |
| One-to-four family mixed-use property | 23,054 | 25,825 | - | 27,018 | 485 |
| One-to-four family residential | 15,328 | 18,995 | - | 15,047 | 186 |
| Co-operative apartments | 237 | 299 | - | 174 | 2 |
| Construction | 10,598 | 15,182 | - | 14,689 | 173 |
| Non-mortgage loans: | | | | | |
| Small Business Administration | 850 | 1,075 | - | 1,042 | 25 |
| Taxi Medallion | - | - | - | - | - |
| Commercial Business and other | 4,391 | 5,741 | - | 5,102 | 53 |
| Total loans with no related allowance recorded | 108,883 | 128,600 | - | 134,768 | 1,889 |
| With an allowance recorded: | | | | | |
| Mortgage loans: | | | | | |
| Multi-family residential | 1,922 | 1,937 | 183 | 3,174 | 124 |
| Commercial real estate | 7,773 | 7,839 | 359 | 6,530 | 400 |
| One-to-four family mixed-use property | 3,314 | 3,313 | 571 | 4,385 | 205 |
| One-to-four family residential | 374 | 374 | 94 | 188 | 19 |
| Co-operative apartments | - | - | - | 101 | - |
| Construction | 3,805 | 3,805 | 38 | 4,275 | 140 |
| Non-mortgage loans: | | | | | |
| Small Business Administration | - | - | - | - | - |
| Taxi Medallion | - | - | - | - | - |
| Commercial Business and other | 2,539 | 2,540 | 249 | 2,273 | 116 |
| Total loans with an allowance recorded | 19,727 | 19,808 | 1,494 | 20,926 | 1,004 |
| Total Impaired Loans: | | | | | |
| Total mortgage loans | $ 120,830 | $ 139,052 | $ 1,245 | $ 147,277 | $ 2,699 |

| | | | | | |
|---|---|---|---|---|---|
| Total non-mortgage loans | $7,780 | $ 9,356 | $ 249 | $ 8,417 | $ 194 |

In accordance with our policy and the current regulatory guidelines, we designate loans as “Special Mention,” which is considered “Criticized Loans,” and “Substandard,” “Doubtful,” or “Loss,” which are considered “Classified Loans”. If a lo does not fall within one of the previous mentioned categories then the loan would be considered “Pass.” We designate a loan as Substandard when a well-defined weakness is identified that jeopardizes the orderly liquidation of the debt. We designate a loan as Doubtful when it displays the inherent weakness of a Substandard loan with the added provision that collection of the debt in full, on the basis of existing facts, is highly improbable. We designate a loan as Loss if it is deemed the debtor is incapable of repayment. Loans that are designated as Loss are charged to the Allowance for Loan Losses. Loans that are non-accrual are designated as Substandard, Doubtful or Loss. We designate a loan as Special Mention if the asset does not warrant classification within one of the other classifications, but does contain a potential weakness that deserves closer attention.

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The following table sets forth the recorded investment in loans designated as Criticized and Classified at September 30, 2013:

| (In thousands) | Special Mention | Substandard (1) | Doubtful | Loss | Total |
|---|---|---|---|---|---|
| Multi-family residential | $ 10,847 | $ 23,250 | $ - | $ - | $ 34,097 |
| Commercial real estate | 12,885 | 21,300 | - | - | 34,185 |
| One-to-four family - mixed-use property | 9,656 | 14,931 | - | - | 24,587 |
| One-to-four family - residential | 1,714 | 14,753 | - | - | 16,467 |
| Co-operative apartments | - | 164 | - | - | 164 |
| Construction loans | 1,916 | 425 | - | - | 2,341 |
| Small Business Administration | 336 | - | - | - | 336 |
| Commercial business and other | 2,000 | 5,939 | 50 | - | 7,989 |
| Total loans | $ 39,354 | $ 80,762 | $ 50 | $ - | $ 120,166 |

The following table sets forth the recorded investment in loans designated as Criticized and Classified at December 31, 2012:

| (In thousands) | Special Mention | Substandard (1) | Doubtful | Loss | Total |
|---|---|---|---|---|---|
| Multi-family residential | $ 16,345 | $ 19,327 | $ - | $ - | $ 35,672 |
| Commercial real estate | 11,097 | 27,877 | - | - | 38,974 |
| One-to-four family - mixed-use property | 13,104 | 24,635 | - | - | 37,739 |
| One-to-four family - residential | 5,223 | 15,328 | - | - | 20,551 |
| Co-operative apartments | 103 | 237 | - | - | 340 |
| Construction loans | 3,805 | 10,598 | - | - | 14,403 |
| Small Business Administration | 323 | 212 | 244 | - | 779 |
| Commercial business and other | 3,044 | 18,419 | 1,080 | - | 22,543 |
| Total loans | $ 53,044 | $ 116,633 | $ 1,324 | $ - | $ 171,001 |

(1) The tables above do not include $5.0 million and $5.3 million of Substandard loans held for sale at September 30, 2013 and December 31, 2012, respectively.

The following table shows the changes in the allowance for loan losses for the periods indicated:

| | For the three months ended September 30 | | For the nine months ended September 30 | |
|---|---|---|---|---|
| (In thousands) | 2013 | 2012 | 2013 | 2012 |
| Balance, beginning of period | $ 32,355 | $ 30,899 | $ 31,104 | $ 30,344 |
| Provision for loan losses | 3,435 | 5,000 | 12,935 | 16,000 |
| Charge-off's | (5,186) | (5,641) | (14,074) | (16,524) |
| Recoveries | 212 | 429 | 851 | 867 |

| | | | | |
|---|---|---|---|---|
| Balance, end of period | $ 30,816 | $ 30,687 | $ 30,816 | $ 30,687 |

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The following table shows net loan charge-offs (recoveries) for the periods indicated:

| (In thousands) | Three Months Ended September 30, 2013 | Three Months Ended September 30, 2012 | Nine Months Ended September 30, 2013 | Nine Months Ended September 30, 2012 |
|---|---|---|---|---|
| Multi-family residential | $ 620 | $ 3,081 | $ 3,304 | $ 5,163 |
| Commercial real estate | 171 | 55 | 612 | 2,152 |
| One-to-four family – mixed-use property | 587 | 814 | 3,611 | 3,064 |
| One-to-four family – residential | (7 ) | 198 | 578 | 1,067 |
| Co-operative apartments | - | 19 | 70 | 62 |
| Construction | 2,374 | 59 | 2,678 | 2,500 |
| Small Business Administration | 72 | 23 | 349 | 265 |
| Commercial business and other | 1,157 | 963 | 2,021 | 1,384 |
| Total net loan charge-offs | $ 4,974 | $ 5,212 | $ 13,223 | $ 15,657 |

Commitments to extend credit (principally real estate mortgage loans) and lines of credit (principally home equity lines of credit and business lines of credit) amounted to $66.8 million and $152.1 million, respectively, at September 30, 2013.

6. Loans held for sale

The following table shows our loans held for sale at the lower of cost or estimated fair value for the periods indicated:

| (Dollars in thousands) | September 30, 2013 Number of loans | September 30, 2013 Carrying Value | December 31, 2012 Number of loans | December 31, 2012 Carrying Value |
|---|---|---|---|---|
| Multi-family residential | 1 | $ 485 | 4 | $ 3,442 |
| One-to-four family - mixed-use property | - | - | 4 | 1,871 |
| Construction | 1 | 5,000 | - | - |
| Total | 2 | $ 5,485 | 8 | $ 5,313 |

The Company has implemented a strategy of selling certain delinquent and non-performing loans. Once the Company has decided to sell a loan, the sale usually closes in a short period of time, generally within the same quarter. Loans designated held for sale are reclassified from loans held for investment to loans held for sale. Terms of sale include cash due upon the closing of the sale, no contingencies or recourse to the Company and servicing is released to the buyer.

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The following table shows delinquent and non-performing loans sold during the period indicated:

| | For the three months ended September 30, 2013 | | | |
|---|---|---|---|---|
| (Dollars in thousands) | Loans sold | Proceeds | Net (charge-offs) recoveries | Net gain (loss) |
| Multi-family residential | 2 | $ 2,079 | $ 65 | $ - |
| Commercial real estate | 1 | 760 | - | 6 |
| One-to-four family - mixed-use property | 4 | 1,487 | (243) | (5) |
| Total | 7 | $ 4,326 | $ (178) | $ 1 |

The following table shows delinquent and non-performing loans sold during the period indicated:

| | For the three months ended September 30, 2012 | | | |
|---|---|---|---|---|
| (Dollars in thousands) | Loans sold | Proceeds | Net charge-offs | Net gain (loss) |
| Multi-family residential | 14 | $ 11,031 | $ (2,295) | $ (8) |
| Commercial real estate | 2 | 750 | (65) | - |
| One-to-four family - mixed-use property | 12 | 3,642 | (939) | - |
| Total | 28 | $ 15,423 | $ (3,299) | $ (8) |

The table above does not include $0.7 million of performing Small Business Administration loans that were sold for a net gain of $60,000 during the three months ended September 30, 2012.

The following table shows delinquent and non-performing loans sold during the period indicated:

| | For the nine months ended September 30, 2013 | | | |
|---|---|---|---|---|
| (Dollars in thousands) | Loans sold | Proceeds | Net charge-offs | Net gain (loss) |
| Multi-family residential | 17 | $ 9,138 | $ (1,036) | $ 6 |
| Commercial real estate | 8 | 4,223 | (564) | 6 |
| One-to-four family - mixed-use property | 34 | 9,449 | (2,773) | (52) |
| Commercial business and other | 2 | 66 | (185) | - |
| Total | 61 | $ 22,876 | $ (4,558) | $ (40) |

The above table does not include the sale of one performing commercial real estate loan for $2.4 million, resulting in a net gain of $184,000 during the nine months ended September 30, 2013.

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The following table shows delinquent and non-performing loans sold during the period indicated:

| | For the nine months ended September 30, 2012 | | | |
|---|---|---|---|---|
| (Dollars in thousands) | Loans sold | Proceeds | Net charge-offs | Net gain (loss) |
| Multi-family residential | 26 | $ 18,102 | $ (2,683) | $ 23 |
| Commercial real estate | 8 | 4,619 | (432) | - |
| One-to-four family - mixed-use property | 21 | 7,085 | (1,736) | - |
| Construction | 3 | 2,540 | (57) | - |
| Commercial business and other | 2 | 714 | (136) | 8 |
| Total | 60 | $ 33,060 | $ (5,044) | $ 31 |

The table above does not include $0.7 million of performing Small Business Administration loans that were sold for a net gain of $60,000 during the nine months ended September 30, 2012.

7. Other Real Estate Owned

The following represents Other Real Estate Owned ("OREO") activity during the periods indicated:

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| | (In thousands) | | | |
| Balance at beginning of period | $2,591 | $2,094 | $ 5,278 | $ 3,179 |
| Acquisitions | 1,785 | 1,910 | 4,543 | 3,541 |
| Write-down of carrying value | (63) | (82) | (243) | (285) |
| Sales | (810) | (262) | (6,075) | (2,775) |
| Balance at end of period | $3,503 | $3,660 | $ 3,503 | $ 3,660 |

The following table shows the gross gains, gross losses and write-downs of OREO reported in the Consolidated Statements of Income during the periods indicated:

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| | (In thousands) | | | |
| Gross gains | $192 | $12 | $ 433 | $ 57 |
| Gross losses | - | - | (89) | (189) |

| | | | | |
|---|---|---|---|---|
| Write-down of carrying value | (63) | (82) | (243) | (285) |
| Total | $129 | $(70) | $101 | $(417) |

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8. Stock-Based Compensation

For the three months ended September 30, 2013 and 2012, the Company's net income, as reported, included $0.4 million and $0.6 million, respectively, of stock-based compensation costs and $0.2 million and $0.3 million, respectively, of income tax benefits related to the stock-based compensation plans. For the nine months ended September 30, 2013 and 2012, the Company's net income, as reported, included $2.9 million of stock-based compensation costs and $1.1 million of income tax benefits related to the stock-based compensation plans.

The Company estimates the fair value of stock options using the Black-Scholes valuation model. Key assumptions used to estimate the fair value of stock options include the exercise price of the award, the expected option term, the expected volatility of the Company's stock price, the risk-free interest rate over the options' expected term and the annual dividend yield. The Company uses the fair value of the common stock on the date of award to measure compensation cost for restricted stock unit awards. Compensation cost is recognized over the vesting period of the award using the straight line method. During the three months ended September 30, 2013, the Company granted 2,400 restricted stock units. There were no restricted stock units granted during the three months ended September 30, 2012. During the nine months ended September 30, 2013 and 2012, the Company granted 246,045 and 230,675 restricted stock units, respectively. There were no stock options granted during the three and nine months ended September 30, 2013 and 2012.

The 2005 Omnibus Incentive Plan ("Omnibus Plan") became effective on May 17, 2005 after approval by the stockholders. The Omnibus Plan authorizes the Compensation Committee of the Company's Board of Directors (the "Compensation Committee") to grant a variety of equity compensation awards as well as long-term and annual cash incentive awards, all of which can be structured so as to comply with Section 162(m) of the Internal Revenue Code of 1986, as amended (the "Internal Revenue Code"). On May 17, 2011, stockholders of the Company approved an amendment to the Omnibus Plan authorizing an additional 625,000 shares for use for full value awards. As of September 30, 2013, there were 361,330 shares available for full value awards and 56,860 shares available for non-full value awards. To satisfy stock option exercises or fund restricted stock and restricted stock unit awards, shares are issued from treasury stock, if available, otherwise new shares are issued. The Company will maintain separate pools of available shares for full value as opposed to non-full value awards, except that shares can be moved from the non-full value pool to the full value pool on a 3-for-1 basis. The exercise price per share of a stock option grant may not be less than the fair market value of the common stock of the Company, as defined in the Omnibus Plan, on the date of grant and may not be re-priced without the approval of the Company's stockholders. Options, stock appreciation rights, restricted stock, restricted stock units and other stock based awards granted under the Omnibus Plan are generally subject to a minimum vesting period of three years with stock options having a 10-year contractual term. Other awards do not have a contractual term of expiration. Restricted stock unit awards include participants who have reached or are close to reaching retirement eligibility, at which time such awards fully vest. These amounts are included in stock-based compensation expense.

Full Value Awards: The first pool is available for full value awards, such as restricted stock unit awards. The pool will be decreased by the number of shares granted as full value awards. The pool will be increased from time to time by: (1) the number of shares that are returned to or retained by the Company as a result of the cancellation, expiration, forfeiture or other termination of a full value award (under the Omnibus Plan); (2) the settlement of such an award in cash; (3) the delivery to the award holder of fewer shares than the number underlying the award, including shares which are withheld from full value awards; or (4) the surrender of shares by an award holder in payment of the exercise price or taxes with respect to a full value award. The Omnibus Plan will allow the Company to transfer shares

from the non-full value pool to the full value pool on a 3-for-1 basis, but does not allow the transfer of shares from the full value pool to the non-full value pool.

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The following table summarizes the Company's full value awards at or for the nine months ended September 30, 2013:

| Full Value Awards | Shares | | Weighted-Average Grant-Date Fair Value |
|---|---|---|---|
| Non-vested at December 31, 2012 | 318,051 | $ | 13.35 |
| Granted | 246,045 | | 15.30 |
| Vested | (185,530) | | 14.46 |
| Forfeited | (17,695 ) | | 14.25 |
| Non-vested at September 30, 2013 | 360,871 | $ | 14.06 |
| | | | |
| Vested but unissued at September 30, 2013 | 217,435 | $ | 14.15 |

As of September 30, 2013, there was $4.0 million of total unrecognized compensation cost related to non-vested full value awards granted under the Omnibus Plan. That cost is expected to be recognized over a weighted-average period of 3.2 years. The total fair value of awards vested for the three months ended September 30, 2013 and 2012 were $4,000 and $2,000, respectively. The total fair value of awards vested for the nine months ended September 30, 2013 and 2012 were $2.8 million and $2.7 million, respectively. The vested but unissued full value awards consist of awards made to employees and directors who are eligible for retirement. According to the terms of the Omnibus Plan, these employees and directors have no risk of forfeiture. These shares will be issued at the original contractual vesting dates.

Non-Full Value Awards: The second pool is available for non-full value awards, such as stock options. The pool will be increased from time to time by the number of shares that are returned to or retained by the Company as a result of the cancellation, expiration, forfeiture or other termination of a non-full value award (under the Omnibus Plan or the 1996 Stock Option Incentive Plan). The second pool will not be replenished by shares withheld or surrendered in payment of the exercise price or taxes, retained by the Company as a result of the delivery to the award holder of fewer shares than the number underlying the award or the settlement of the award in cash.

The following table summarizes certain information regarding the non-full value awards, all of which have been granted as stock options, at or for the nine months ended September 30, 2013:

| Non-Full Value Awards | Shares | | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term | | Aggregate Intrinsic Value ($000) * |
|---|---|---|---|---|---|---|
| Outstanding at December 31, 2012 | 770,355 | $ | 15.92 | | | |
| Granted | - | | - | | | |
| Exercised | (300,195) | | 14.62 | | | |
| Forfeited | (420 ) | | 16.25 | | | |
| Outstanding at September 30, 2013 | 469,740 | $ | 16.76 | 2.7 | $ | 918 |
| Exercisable shares at September 30, 2013 | 447,440 | $ | 17.17 | 2.6 | $ | 695 |

| | | | | | |
|---|---|---|---|---|---|
| Vested but unexercisable shares at September 30, 2013 | 8,100 | $ | 8.44 | 5.3 | $ 81 |

* The intrinsic value of a stock option is the difference between the market value of the underlying stock and the exercise price of the option.

As of September 30, 2013, there was $6,000 of total unrecognized compensation cost related to unvested non-full value awards granted under the Omnibus Plan. That cost is expected to be recognized over a weighted-average period of 0.3 years. The vested but unexercisable non-full value awards were made to employees who are eligible for retirement. According to the terms of the Omnibus Plan, these employees have no risk of forfeiture. These awards will be exercisable at the original contractual vesting dates.

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Cash proceeds, fair value received, tax benefits, intrinsic value related to stock options exercised and the weighted average grant date fair value for options granted during the nine months ended September 30, 2013 are provided in the following table:

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|---|---|---|---|
| (In thousands) | 2013 | 2012 | 2013 | 2012 |
| Proceeds from stock options exercised | $ 77 | $ 21 | $ 312 | $ 836 |
| Fair value of shares received upon exercised of stock options | 2,323 | 287 | 4,074 | 835 |
| Tax (expense) benefit related to stock options exercised | (71) | 3 | 97 | 30 |
| Intrinsic value of stock options exercised | 436 | 56 | 813 | 186 |

Phantom Stock Plan: The Company maintains a non-qualified phantom stock plan as a supplement to its profit sharing plan for officers who have achieved the level of Senior Vice President and above and completed one year of service. However, officers who had achieved at least the level of Vice President and completed one year of service prior to January 1, 2009 remain eligible to participate in the phantom stock plan. Awards are made under this plan on certain compensation not eligible for awards made under the profit sharing plan, due to the terms of the profit sharing plan and the Internal Revenue Code. Employees receive awards under this plan proportionate to the amount they would have received under the profit sharing plan, but for limits imposed by the profit sharing plan and the Internal Revenue Code. The awards are made as cash awards, and then converted to common stock equivalents (phantom shares) at the then current market value of the Company's common stock. Dividends are credited to each employee's account in the form of additional phantom shares each time the Company pays a dividend on its common stock. In the event of a change of control (as defined in this plan), an employee's interest is converted to a fixed dollar amount and deemed to be invested in the same manner as his or her interest in the Bank's non-qualified deferred compensation plan. Employees vest under this plan 20% per year for 5 years. Employees also become 100% vested upon a change of control. Employees receive their vested interest in this plan in the form of a cash lump sum payment or installments, as elected by the employee, after termination of employment. The Company adjusts its liability under this plan to the fair value of the shares at the end of each period.

The following table summarizes the Phantom Stock Plan at or for the nine months ended September 30, 2013:

| Phantom Stock Plan | Shares | Fair Value |
|---|---|---|
| Outstanding at December 31, 2012 | 50,067 | $ 15.34 |
| Granted | 9,467 | 15.74 |
| Forfeited | - | - |
| Distributions | (500) | 16.26 |
| Outstanding at September 30, 2013 | 59,034 | $ 18.45 |
| Vested at September 30, 2013 | 58,742 | $ 18.45 |

The Company recorded stock-based compensation expense for the Phantom Stock Plan of $0.1 million for the three months ended September 30, 2013 and 2012. There were no distributions made from the Phantom Stock Plan during the three months ended September 30, 2013. The total fair value of the distributions from the Phantom Stock Plan was

$1,000 for the three months ended September 30, 2012.

For the nine months ended September 30, 2013 and 2012, the Company recorded stock-based compensation expense for the Phantom Stock Plan of $0.2 million. The total fair value of the distributions from the Phantom Stock Plan during the nine months ended September 30, 2013 and 2012 were $8,000 and $6,000, respectively.

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9. Pension and Other Postretirement Benefit Plans

The following table sets forth information regarding the components of net expense for the pension and other postretirement benefit plans.

| (In thousands) | Three months ended September 30, 2013 | Three months ended September 30, 2012 | Nine months ended September 30, 2013 | Nine months ended September 30, 2012 |
|---|---|---|---|---|
| Employee Pension Plan: | | | | |
| Interest cost | $ 207 | $ 220 | $ 621 | $ 660 |
| Amortization of unrecognized loss | 306 | 263 | 918 | 789 |
| Expected return on plan assets | (315) | (310) | (945) | (930) |
| Net employee pension expense | $ 198 | $ 173 | $ 594 | $ 519 |
| | | | | |
| Outside Director Pension Plan: | | | | |
| Service cost | $ 21 | $ 20 | $ 63 | $ 60 |
| Interest cost | 24 | 28 | 72 | 84 |
| Amortization of unrecognized gain | (9) | (7) | (27) | (21) |
| Amortization of past service liability | 9 | 9 | 27 | 27 |
| Net outside director pension expense | $ 45 | $ 50 | $ 135 | $ 150 |
| | | | | |
| Other Postretirement Benefit Plans: | | | | |
| Service cost | $ 112 | $ 100 | $ 336 | $ 300 |
| Interest cost | 55 | 54 | 165 | 162 |
| Amortization of unrecognized loss | 12 | 10 | 36 | 30 |
| Amortization of past service credit | (20) | (21) | (60) | (63) |
| Net other postretirement expense | $ 159 | $ 143 | $ 477 | $ 429 |

The Company previously disclosed in its Consolidated Financial Statements for the year ended December 31, 2012 that it expects to contribute $0.8 million to the Company’s Employee Pension Plan (the “Employee Pension Plan”) and $0.2 million to each of the Outside Director Pension Plan (the “Outside Director Pension Plan”) and the other postretirement benefit plans (the “Other Postretirement Benefit Plans”) during the year ending December 31, 2013. As of September 30, 2013, the Company has contributed $0.7 million to the Employee Pension Plan, $73,000 to the Outside Director Pension Plan and $50,000 to the Other Postretirement Benefit Plans. As of September 30, 2013, the Company has not revised its expected contributions for the year ending December 31, 2013.

10. Fair Value of Financial Instruments

The Company carries certain financial assets and financial liabilities at fair value in accordance with ASC Topic 825, “Financial Instruments” (“ASC Topic 825”) and values those financial assets and financial liabilities in accordance with ASC Topic 820, “Fair Value Measurements and Disclosures” (“ASC Topic 820”). ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, establishes a framework for measuring fair value and expands disclosures about fair value measurements. ASC Topic 825 permits entities to choose to measure many financial instruments and certain other items at fair value. At September 30, 2013, the Company carried financial assets and financial liabilities

under the fair value option with fair values of $41.5 million and $26.5 million, respectively. At December 31, 2012, the Company carried financial assets and financial liabilities under the fair value option with fair values of $54.5 million and $23.9 million, respectively. During the nine months ended September 30, 2013, the Company did not elect to carry any additional financial assets or financial liabilities under the fair value option. The Company elected to measure at fair value securities with a cost of $10.0 million that were purchased during the nine months ended September 30, 2012.

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The following table presents the financial assets and financial liabilities reported at fair value under the fair value option, and the changes in fair value included in the Consolidated Statement of Income – Net gain (loss) from fair value adjustments, at or for the periods indicated:

| | Fair Value Measurements at September 30, | Fair Value Measurements at December 31, | Changes in Fair Values For Items Measured at Fair Value Pursuant to Election of the Fair Value Option | | | |
|---|---|---|---|---|---|---|
| | | | Three Months Ended | | Nine Months Ended | |
| (In thousands) | 2013 | 2012 | September 30, 2013 | September 30, 2012 | September 30, 2013 | September 30, 2012 |
| Mortgage-backed securities | $ 12,004 | $ 24,911 | $ (95) | $ (14) | $ (626) | $ (175) |
| Other securities | 29,491 | 29,577 | (381) | 325 | (328) | 571 |
| Borrowed funds | 26,465 | 23,922 | (272) | 374 | (2,547) | 2,279 |
| Net (loss) gain from fair value adjustments (1) (2) | | | $ (748) | $ 685 | $ (3,501) | $ 2,675 |

(1) The net gain (loss) from fair value adjustments presented in the above table does not include net gains of $0.6 million and $0.1 million for the three months ended September 30, 2013 and 2012, respectively, from the change in the fair value of interest rate caps/swaps.

(2) The net gain (loss) from fair value adjustments presented in the above table does not include net gains of $2.9 million and net losses of ($2.9) million for the nine months ended September 30, 2013 and 2012, respectively, from the change in the fair value of interest rate caps/swaps.

Included in the fair value of the financial assets and financial liabilities selected for the fair value option is the accrued interest receivable or payable for the related instrument. One pooled trust preferred security is over 90 days past due and the Company has stopped accruing interest. The Company continues to accrue on the remaining financial instruments and reports, as interest income or interest expense in the Consolidated Statement of Income, the interest receivable or payable on the financial instruments selected for the fair value option at their respective contractual rates.

The borrowed funds had a contractual principal amount of $61.9 million at September 30, 2013 and December 31, 2012. The fair value of borrowed funds includes accrued interest payable of $0.1 million and $0.4 million at September 30, 2013 and December 31, 2012, respectively.

The Company generally holds its earning assets, other than securities available for sale, to maturity and settles its liabilities at maturity. However, fair value estimates are made at a specific point in time and are based on relevant market information. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular instrument. Accordingly, as assumptions change, such as interest rates and prepayments, fair value estimates change and these amounts may not necessarily be realized in an immediate sale.

Disclosure of fair value does not require fair value information for items that do not meet the definition of a financial instrument or certain other financial instruments specifically excluded from its requirements. These items include core deposit intangibles and other customer relationships, premises and equipment, leases, income taxes, foreclosed properties and equity.

Further, fair value disclosure does not attempt to value future income or business. These items may be material and accordingly, the fair value information presented does not purport to represent, nor should it be construed to represent, the underlying "market" or franchise value of the Company.

Financial assets and financial liabilities reported at fair value are required to be measured based on either: (1) quoted prices in active markets for identical financial instruments (Level 1); (2) significant other observable inputs (Level 2); or (3) significant unobservable inputs (Level 3).

A description of the methods and significant assumptions utilized in estimating the fair value of the Company's assets and liabilities that are carried at fair value on a recurring basis are as follows:

Level 1 – where quoted market prices are available in an active market. The Company did not value any of its assets or liabilities that are carried at fair value on a recurring basis as Level 1 at September 30, 2013 and December 31, 2012.

Level 2 – when quoted market prices are not available, fair value is estimated using quoted market prices for similar financial instruments and adjusted for differences between the quoted instrument and the instrument being valued. Fair value can also be estimated by using pricing models, or discounted cash flows. Pricing models primarily use market-based or independently sourced market parameters as inputs, including, but not limited to, yield curves, interest rates, equity or debt prices and credit spreads. In addition to observable market information, models also incorporate maturity and cash flow assumptions. At September 30, 2013 and December 31, 2012, Level 2 included mortgage related securities, corporate debt and interest rate caps/swaps.

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Level 3 – when there is limited activity or less transparency around inputs to the valuation, financial instruments are classified as Level 3. At September 30, 2013 and December 31, 2012, Level 3 included REMIC and CMO securities, municipal securities and trust preferred securities owned by and junior subordinated debentures issued by the Company.

The methods described above may produce fair values that may not be indicative of net realizable value or reflective of future fair values. While the Company believes its valuation methods are appropriate and consistent with those of other market participants, the use of different methodologies, assumptions and models to determine fair value of certain financial instruments could produce different estimates of fair value at the reporting date.

The following table sets forth the assets and liabilities that are carried at fair value on a recurring basis and the method that was used to determine their fair value, at September 30, 2013 and December 31, 2012:

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | | Significant Other Observable Inputs (Level 2) | | Significant Other Unobservable Inputs (Level 3) | | Total carried at fair value on a recurring basis | |
|---|---|---|---|---|---|---|---|---|
| | September 30, 2013 | December 31, 2012 | September 30, 2013 | December 31, 2012 | September 30, 2013 | December 31, 2012 | September 30, 2013 | December 31, 2012 |
| | | | | | (in thousands) | | | |
| Assets: | | | | | | | | |
| Mortgage-backed Securities | $ - | $ - | $ 765,016 | $ 696,638 | $ 20,194 | $ 23,475 | $ 785,210 | $ 720,113 |
| Other securities | - | - | 256,563 | 213,374 | 16,781 | 16,079 | 273,344 | 229,453 |
| Interest rate caps | - | - | - | 19 | - | - | - | 19 |
| Interest rate swaps | - | - | 1,212 | 3 | - | - | 1,212 | 3 |
| Total assets | $ - | $ - | $ 1,022,791 | $ 910,034 | $ 36,975 | $ 39,554 | $ 1,059,766 | $ 949,588 |
| Liabilities: | | | | | | | | |
| Borrowings | $ - | $ - | $ - | $ - | $ 26,465 | $ 23,922 | $ 26,465 | $ 23,922 |
| Interest rate swaps | - | - | - | 1,922 | - | - | - | 1,922 |
| Total liabilities | $ - | $ - | $ - | $ 1,922 | $ 26,465 | $ 23,922 | $ 26,465 | $ 25,844 |

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The following table sets forth the Company's assets and liabilities that are carried at fair value on a recurring basis, classified within Level 3 of the valuation hierarchy for the period indicated:

| | For the three months ended September 30, 2013 | | | |
|---|---|---|---|---|
| | REMIC and CMO | Municipals | Trust preferred securities (In thousands) | Junior subordinated debentures |
| Beginning balance | $ 22,930 | $ 9,327 | $ 8,367 | $ 26,192 |
| Transfer into Level 3 | - | - | - | - |
| Net loss from fair value adjustment of financial assets | - | - | (361) | - |
| Net loss from fair value adjustment of financial liabilities | - | - | - | 272 |
| Increase in accrued interest payable | - | - | - | 1 |
| Other-than-temporary impairment charge | (916) | - | - | - |
| Change in net unrealized losses included in other comprehensive income | (1,820) | (52) | (500) | - |
| Ending balance | $ 20,194 | $ 9,275 | $ 7,506 | $ 26,465 |
| | | | | |
| Changes in unrealized held at period end | $ (1,820) | $ (52) | $ (500) | $ - |

The following table sets forth the Company's assets and liabilities that are carried at fair value on a recurring basis, classified within Level 3 of the valuation hierarchy for the period indicated:

| | For the three months ended September 30, 2012 | |
|---|---|---|
| | Trust preferred securities (In thousands) | Junior subordinated debentures |
| Beginning balance | $ 5,653 | $ 24,356 |
| Transfer into Level 3 | - | - |
| Net loss from fair value adjustment of financial assets | 137 | - |
| Net gain from fair value adjustment of financial liabilities | - | (374) |
| Decrease in accrued interest payable | (9) | (273) |
| Other-than-temporary impairment charge | - | - |
| Change in net unrealized gains included in other comprehensive income | 315 | - |
| Ending balance | $ 6,096 | $ 23,709 |
| | | |
| Changes in unrealized held at period end | $ 315 | $ - |

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The following table sets forth the Company's assets and liabilities that are carried at fair value on a recurring basis, classified within Level 3 of the valuation hierarchy for the period indicated:

| | For the nine months ended September 30, 2013 | | | |
|---|---|---|---|---|
| | REMIC and CMO | Municipals | Trust preferred securities | Junior subordinated debentures |
| | (In thousands) | | | |
| Beginning balance | $ 23,475 | $ 9,429 | $ 6,650 | $ 23,922 |
| Transfer into Level 3 | - | - | - | - |
| Net gain from fair value adjustment of financial assets | - | - | 150 | - |
| Net loss from fair value adjustment of financial liabilities | - | - | - | 2,547 |
| Decrease in accrued interest payable | - | - | - | (4 ) |
| Other-than-temporary impairment charge | (1,419 ) | - | - | - |
| Change in net unrealized gains (losses) included in other comprehensive income | (1,862 ) | (154 ) | 706 | - |
| Ending balance | $ 20,194 | $ 9,275 | $ 7,506 | $ 26,465 |
| | | | | |
| Changes in unrealized held at period end | $ (1,862 ) | $ (154 ) | $ 706 | $ - |

The following table sets forth the Company's assets and liabilities that are carried at fair value on a recurring basis, classified within Level 3 of the valuation hierarchy for the period indicated:

| | For the nine months ended September 30, 2012 | |
|---|---|---|
| | Trust preferred securities | Junior subordinated debentures |
| | (In thousands) | |
| Beginning balance | $ 5,632 | $ 26,311 |
| Transfer into Level 3 | - | - |
| Net gain from fair value adjustment of financial assets | 104 | - |
| Net gain from fair value adjustment of financial liabilities | - | (2,279 ) |
| Decrease in accrued interest payable | (10 ) | (323 ) |
| Other-than-temporary impairment charge | - | - |
| Change in net unrealized gains included in other comprehensive income | 370 | - |
| Ending balance | $ 6,096 | $ 23,709 |
| | | |
| Changes in unrealized held at period end | $ 370 | $ - |

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FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
Notes to Consolidated Financial Statements
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The following table presents the quantitative information about recurring Level 3 fair value of financial instruments and the fair value measurements as of September 30, 2013:

| September 30, 2013 | Fair Value | Valuation Technique | Unobservable Input | Range | | | (Weighted Average) |
|---|---|---|---|---|---|---|---|
| | | (Dollars in thousands) | | | | | |
| Assets: | | | | | | | |
| | | | Spread to index | 2.1% | - | 3.9% | (3.4%) |
| | | | Loss Severity | 40.0% | - | 70.0% | (53.1%) |
| | | | Prepayment speeds | 1.0% | - | 9.6% | (6.4%) |
| | | | Defaults | 3.0% | - | 16.0% | (9.0%) |
| REMIC and CMO | $ 20,194 | Discounted cash flows | Average Life (years) | 3.7 | - | 15.1 | (6.2) |
| Municipals | $ 9,275 | Discounted cash flows | Discount rate | 0.4% | - | 4.0% | (3.6%) |
| | | | Discount rate | 8.0% | - | 18.1% | (12.2%) |
| | | | Prepayment assumptions | 0% | - | 44.3% | (32.2%) |
| Trust Preferred Securities | $ 7,506 | Discounted cash flows | Defaults | 0% | - | 15.6% | (12.1%) |
| Liabilities: | | | | | | | |
| Junior subordinated debentures | $ 26,465 | Discounted cash flows | Discount rate | | | 8.0% | (8.0%) |

The significant unobservable inputs used in the fair value measurement of the Company's REMIC and CMO securities valued under Level 3 are the spread to an index, loss severity, default rate, prepayment speeds and the average life of the security. Significant increases or decreases in either of those inputs in isolation would result in a significantly lower or higher fair value measurement.

The significant unobservable inputs used in the fair value measurement of the Company's municipal securities valued under Level 3 are the securities' effective yield. Significant increases or decreases in the effective yield in isolation would result in a significantly lower or higher fair value measurement.

The significant unobservable inputs used in the fair value measurement of the Company's trust preferred securities valued under Level 3 are the securities' prepayment assumptions and default rate. Significant increases or decreases in any of the inputs in isolation would result in a significantly lower or higher fair value measurement.

The significant unobservable inputs used in the fair value measurement of the Company's junior subordinated Debentures are effective yield. Significant increases or decreases in the effective yield in isolation would result in a significantly lower or higher fair value measurement.

The following table sets forth the Company's assets that are carried at fair value on a non-recurring basis and the method that was used to determine their fair value, at September 30, 2013 and December 31, 2012:

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | | Significant Other Observable Inputs (Level 2) | | Significant Other Unobservable Inputs (Level 3) | | Total carried at fair value on a non-recurring basis | |
|---|---|---|---|---|---|---|---|---|
| | September 30, 2013 | December 31, 2012 | September 30, 2013 | December 31, 2012 | September 30, 2013 | December 31, 2012 | September 30, 2013 | December 31, 2012 |
| | (in thousands) | | | | | | | |
| Assets: | | | | | | | | |
| Loans held for sale | $- | $ - | $ - | $ - | $ 5,485 | $ 5,313 | $ 5,485 | $ 5,313 |
| Impaired loans | - | - | - | - | 27,813 | 49,703 | 27,813 | 49,703 |
| Other Real Estate Owned | - | - | - | - | 3,503 | 5,278 | 3,503 | 5,278 |
| Total assets | $- | $ - | $ - | $ - | $ 36,801 | $ 60,294 | $ 36,801 | $ 60,294 |

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The following table presents the quantitative information about non-recurring Level 3 fair value of financial instruments and the fair value measurements as of September 30, 2013:

| September 30, 2013 | Fair Value | Valuation Technique | Unobservable Input | Range | | (Weighted Average) |
|---|---|---|---|---|---|---|
| | | (Dollars in thousands) | | | | |
| Assets: | | | | | | |
| Loans held for sale | $ 5,485 | Fair value of collateral | Loss severity discount | 24.5% - | 57.9% | (56.2%) |
| Impaired loans | $ 27,813 | Fair value of collateral | Loss severity discount | 0.5% | - 90.4% | (33.5%) |
| Other real estate owned | $ 3,503 | Fair value of collateral | Loss severity discount | 0.0% | - 42.1% | (8.1%) |

The Company carries its Loans held for sale and OREO at the expected sales price less selling costs.

The Company carries its impaired collateral dependent loans at 85% of the appraised or internally estimated value of the underlying property.

The Company did not have any liabilities that were carried at fair value on a non-recurring basis at September 30, 2013 and December 31, 2012.

The estimated fair value of each material class of financial instruments at September 30, 2013 and December 31, 2012 and the related methods and assumptions used to estimate fair value are as follows:

Cash and Due from Banks, Overnight Interest-Earning Deposits and Federal Funds Sold:

The fair values of financial instruments that are short-term or reprice frequently and have little or no risk are considered to have a fair value that approximates carrying value (Level 1).

FHLB-NY stock:

The fair value is based upon the par value of the stock which equals its carrying value (Level 2).

Securities Available for Sale:

The estimated fair values of securities available for sale are contained in Note 6 of the Notes to Consolidated Financial Statements. Fair value is based upon quoted market prices (Level 1 input), where available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities and adjusted for differences between the quoted instrument and the instrument being valued (Level 2 input). When there is limited activity or less transparency around inputs to the valuation, securities are classified as (Level 3 input).

Loans held for sale:

The fair value of non-performing loans held for sale is estimated through bids received on the loans and, as such, are classified as a Level 3 input.

Loans:

The estimated fair value of loans is estimated by discounting the expected future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and remaining maturities (Level 3 input).

For non-accruing loans, fair value is generally estimated by discounting management's estimate of future cash flows with a discount rate commensurate with the risk associated with such assets or for collateral dependent loans 85% of the appraised or internally estimated value of the property (Level 3 input).

Due to Depositors:

The fair values of demand, passbook savings, NOW, money market deposits and escrow deposits are, by definition, equal to the amount payable on demand at the reporting dates (i.e. their carrying value) (Level 1). The fair value of fixed-maturity certificates of deposits are estimated by discounting the expected future cash flows using the rates currently offered for deposits of similar remaining maturities (Level 2 input).

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Borrowings:

The estimated fair value of borrowings are estimated by discounting the contractual cash flows using interest rates in effect for borrowings with similar maturities and collateral requirements (Level 2 input) or using a market-standard model (Level 3 input).

Interest Rate Caps:

The estimated fair value of interest rate caps is based upon broker quotes (Level 2 input).

Interest Rate Swaps:

The estimated fair value of interest rate swaps is based upon broker quotes (Level 2 input).

Other Real Estate Owned:

OREO are carried at fair value less selling costs. The fair value is based on appraised value through a current appraisal, or sometimes through an internal review, additionally adjusted by the estimated costs to sell the property (Level 3 input).

Other Financial Instruments:

The fair values of commitments to sell, lend or borrow are estimated using the fees currently charged or paid to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties or on the estimated cost to terminate them or otherwise settle with the counterparties at the reporting date. For fixed-rate loan commitments to sell, lend or borrow, fair values also consider the difference between current levels of interest rates and committed rates (where applicable).

At September 30, 2013 and December 31, 2012, the fair values of the above financial instruments approximate the recorded amounts of the related fees and were not considered to be material.

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The following table sets forth the carrying amounts and estimated fair values of selected financial instruments based on the assumptions described above used by the Company in estimating fair value at September 30, 2013:

| | September 30, 2013 | | | | |
|---|---|---|---|---|---|
| | Carrying Amount | Fair Value | Level 1 | Level 2 | Level 3 |
| | | | (in thousands) | | |
| Assets: | | | | | |
| Cash and due from banks | $40,328 | $40,328 | $40,328 | $- | $- |
| Mortgage-backed Securities | 785,210 | 785,210 | - | 765,016 | 20,194 |
| Other securities | 273,344 | 273,344 | - | 256,563 | 16,781 |
| Loans held for sale | 5,485 | 5,485 | - | - | 5,485 |
| Loans | 3,396,138 | 3,465,973 | - | - | 3,465,973 |
| FHLB-NY stock | 46,003 | 46,003 | - | 46,003 | - |
| Interest rate caps | - | - | - | - | - |
| Interest rate swaps | 1,212 | 1,212 | - | 1,212 | - |
| OREO | 3,503 | 3,503 | - | - | 3,503 |
| Total assets | $4,551,223 | $4,621,058 | $40,328 | $1,068,794 | $3,511,936 |
| Liabilities: | | | | | |
| Deposits | $3,239,370 | 3,262,780 | $1,997,053 | $1,265,727 | $- |
| Borrowings | 1,018,231 | 1,043,413 | - | 1,016,948 | 26,465 |
| Total liabilities | $4,257,601 | $4,306,193 | $1,997,053 | $2,282,675 | $26,465 |

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FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
Notes to Consolidated Financial Statements
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The following table sets forth the carrying amounts and estimated fair values of selected financial instruments based on the assumptions described above used by the Company in estimating fair value at December 31, 2012:

| | December 31, 2012 | | | | |
|---|---|---|---|---|---|
| | Carrying Amount | Fair Value | Level 1 | Level 2 | Level 3 |
| | (in thousands) | | | | |
| Assets: | | | | | |
| Cash and due from banks | $40,425 | $40,425 | $40,425 | $- | $- |
| Mortgage-backed Securities | 720,113 | 720,113 | - | 696,638 | 23,475 |
| Other securities | 229,453 | 229,453 | - | 213,374 | 16,079 |
| Loans held for sale | 5,313 | 5,313 | - | - | 5,313 |
| Loans | 3,234,121 | 3,416,313 | - | - | 3,416,313 |
| FHLB-NY stock | 42,337 | 42,337 | - | 42,337 | - |
| Interest rate caps | 19 | 19 | - | 19 | - |
| Interest rate swaps | 3 | 3 | - | 3 | - |
| OREO | 5,278 | 5,278 | - | - | 5,278 |
| Total assets | $4,277,062 | $4,459,254 | $40,425 | $952,371 | $3,466,458 |
| Liabilities: | | | | | |
| Deposits | $3,015,193 | 3,057,152 | $1,761,964 | $1,295,188 | $- |
| Borrowings | 948,405 | 992,069 | - | 968,147 | 23,922 |
| Interest rate swaps | 1,922 | 1,922 | - | 1,922 | - |
| Total liabilities | $3,965,520 | $4,051,143 | $1,761,964 | $2,265,257 | $23,922 |

11. Derivative Financial Instruments

At September 30, 2013 and December 31, 2012, the Company's derivative financial instruments consist of purchased options and swaps. The purchased options are used to mitigate the Company's exposure to rising interest rates on its financial liabilities without stated maturities. The Company's swaps are used to mitigate the Company's exposure to rising interest rates on a portion ($18.0 million) of its floating rate junior subordinated debentures that have a contractual value of $61.9 million. Additionally, the Company at times may use swaps to mitigate the Company's exposure to rising interest rates on its fixed rate loans.

At September 30, 2013, derivatives with a combined notional amount of $118.0 million are not designated as hedges and a derivative with a notional amount of $4.2 million is designated as a fair value hedge. Changes in the fair value of the derivatives not designated as hedges are reflected in "Net gain/loss from fair value adjustments" in the Consolidated Statements of Income. The portions of the changes in the fair value of the derivative designated as a fair value hedge which is considered ineffective are reflected in "Net gain/loss from fair value adjustments" in the Consolidated Statements of Income.

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The following table sets forth information regarding the Company’s derivative financial instruments at September 30, 2013:

| | Notional Amount | Purchase Price | Net Carrying Value |
|---|---|---|---|
| | | (In thousands) | |
| Interest rate caps (non-hedge) | $100,000 | $ 9,035 | $ - |
| Interest rate swaps (non-hedge) | 18,000 | - | 960 |
| Interest rate swaps (hedge) | 4,238 | - | 252 |
| Total derivatives | $122,238 | $ 9,035 | $ 1,212 |

The following table sets forth information regarding the Company’s derivative financial instruments at December 31, 2012:

| | Notional Amount | Purchase Price | Net Carrying (1) Value |
|---|---|---|---|
| | | (In thousands) | |
| Interest rate caps (non-hedge) | $100,000 | $ 9,035 | $ 19 |
| Interest rate swaps (non-hedge) | 18,000 | - | (1,922) |
| Interest rate swaps (hedge) | 4,300 | - | 3 |
| Total derivatives | $122,300 | $ 9,035 | $ (1,900) |

(1) Derivatives in a net positive position are recorded as “Other assets” and derivatives in a net negative position are recorded as “Other liabilities” in the Consolidated Statements of Financial Condition.

The following table sets forth the effect of derivative instruments on the Consolidated Statements of Income for the periods indicated:

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| (In thousands) | 2013 | 2012 | 2013 | 2012 |
| Financial Derivatives: | | | | |
| Interest rate caps | $ (7) | $ (52) | $ (18) | $ (314) |
| Interest rate swaps | 565 | 192 | 2,898 | (2,546) |
| Net gain (loss) (1) | $ 558 | $ 140 | $ 2,880 | $ (2,860) |

(1) Net gains and (losses) are recorded as part of “Net gain/loss from fair value adjustments” in the Consolidated Statements of Income.

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12. Income Taxes

Flushing Financial Corporation files consolidated Federal and combined New York State and New York City income tax returns with its subsidiaries, with the exception of Flushing Financial Capital Trust II, Flushing Financial Capital Trust III, and Flushing Financial Capital Trust IV, which file separate Federal income tax returns as trusts, and Flushing Preferred Funding Corporation, which files a separate Federal and New York State income tax return as a real estate investment trust.

Income tax provisions are summarized as follows:

| (In thousands) | For the three months ended September 30, 2013 | For the three months ended September 30, 2012 | For the nine months ended September 30, 2013 | For the nine months ended September 30, 2012 |
|---|---|---|---|---|
| Federal: | | | | |
| Current | $ 4,678 | $ 4,578 | $ 12,699 | $ 12,807 |
| Deferred | (85) | (35) | 18 | (404) |
| Total federal tax provision | 4,593 | 4,543 | 12,717 | 12,403 |
| State and Local: | | | | |
| Current | 1,468 | 1,460 | 3,773 | 3,793 |
| Deferred | (37) | (15) | 8 | (131) |
| Total state and local tax provision | 1,431 | 1,445 | 3,781 | 3,662 |
| | | | | |
| Total income tax provision | $ 6,024 | $ 5,988 | $ 16,498 | $ 16,065 |

The income tax provision in the Consolidated Statements of Income has been provided at an effective rate of 39.0% for all periods presented in the table above.

The effective rates differ from the statutory federal income tax rate as follows:

| (dollars in thousands) | For the three months ended September 30, 2013 | | For the three months ended September 30, 2012 | | For the nine months ended September 30, 2013 | | For the nine months ended September 30, 2012 | |
|---|---|---|---|---|---|---|---|---|
| Taxes at federal statutory rate | $ 5,406 | 35.0 % | $ 5,374 | 35.0 % | $ 14,806 | 35.0 % | 14,419 | 35.0 % |
| Increase (reduction) in taxes resulting from: | | | | | | | | |
| State and local income tax, net of Federal income tax benefit | 930 | 6.0 | 938 | 6.1 | 2,458 | 5.8 | 2,380 | 5.8 |
| Other | (312) | (2.0) | (324) | (2.1) | (766) | (1.8) | (734) | (1.8) |
| | $ 6,024 | 39.0 % | $ 5,988 | 39.0 % | $ 16,498 | 39.0 % | $ 16,065 | 39.0 % |

| Taxes at effective rate |
|---|

The Company has recorded a deferred tax asset of $35.4 million at September 30, 2013, which is included in "Other assets" in the Consolidated Statements of Financial Condition. This represents the anticipated net federal, state and local tax benefits expected to be realized in future years upon the utilization of the underlying tax attributes comprising this balance. The Company has reported taxable income for federal, state, and local tax purposes in each of the past three fiscal years. In management's opinion, in view of the Company's previous, current and projected future earnings trend, the probability that some of the Company's $20.5 million deferred tax liability can be used to offset a portion of the deferred tax asset, as well as certain tax planning strategies, it is more likely than not that the deferred tax asset will be fully realized. Accordingly, no valuation allowance was deemed necessary for the deferred tax asset at September 30, 2013.

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FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
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13. Accumulated Other Comprehensive Income:

The following table sets forth the changes in accumulated other comprehensive income by component for the nine months ended September 30, 2013:

| | Unrealized Gains and (Losses) on Available for Sale Securities | Defined Benefit Pension Items (In thousands) | Total |
|---|---|---|---|
| Beginning balance, net of tax | $ 18,921 | $ (6,784 ) | $ 12,137 |
| Other comprehensive income (loss) before reclassifications, net of tax | (19,947 ) | - | $ (19,947 ) |
| Amounts reclassified from accumulated other comprehensive income (loss), net of tax | (874 ) | 503 | (371 ) |
| Net current period other comprehensive income (loss), net of tax | (20,821 ) | 503 | (20,318 ) |
| Ending balance, net of tax | $ (1,900 ) | $ (6,281 ) | $ (8,181 ) |

The following table sets forth significant amounts reclassified out of accumulated other comprehensive income by component for the three months ended September 30, 2013:

| Details about Accumulated Other Comprehensive Income Components | Amounts Reclassified from Accumulated Other Comprehensive Income (Dollars in thousands) | Affected Line Item in the Statement Where Net Income is Presented |
|---|---|---|
| Unrealized gains (losses) on available for sale securities: | $ 96 | Net gain on sale of securities |
| | (42 ) | Tax expense |
| | $ 54 | Net of tax |
| OTTI charges | $ (916 ) | OTTI charge |
| | 400 | Tax benefit |
| | $ (516 ) | Net of tax |

| | | | | | |
|---|---|---|---|---|---|
| Amortization of defined benefit pension items: | | | | | |
| Actuarial losses | $ | (309 | ) | (1) | Other expense |
| Prior service credits | | 11 | | (1) | Other expense |
| | | (298 | ) | | Total before tax |
| | | 130 | | | Tax benefit |
| | $ | (168 | ) | | Net of tax |

(1) These accumulated other comprehensive income components are included in the computation of net periodic pension cost (see Note 9 of the Notes to Consolidated Financial Statements “Pension and Other Postretirement Benefit Plans”).

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The following table sets forth significant amounts reclassified out of accumulated other comprehensive income by component for the nine months ended September 30, 2013:

| Details about Accumulated Other Comprehensive Income Components | | Amounts Reclassified from Accumulated Other Comprehensive Income (Dollars in thousands) | | | Affected Line Item in the Statement Where Net Income is Presented |
|---|---|---|---|---|---|
| Unrealized gains losses on available for sale securities: | $ | 2,972 | | | Net gain on sale of securities |
| | | (1,299 | ) | | Tax expense |
| | $ | 1,673 | | | Net of tax |
| | | | | | |
| | | | | | |
| OTTI charges | $ | (1,419 | ) | | OTTI charge |
| | | 620 | | | Tax benefit |
| | $ | (799 | ) | | Net of tax |
| | | | | | |
| | | | | | |
| Amortization of defined benefit pension items: | | | | | |
| Actuarial losses | $ | (927 | ) | (1) | Other expense |
| Prior service credits | | 33 | | (1) | Other expense |
| | | (894 | ) | | Total before tax |
| | | 391 | | | Tax benefit |
| | $ | (503 | ) | | Net of tax |

(1) These accumulated other comprehensive income components are included in the computation of net periodic pension cost (see Note 9 of the Notes to Consolidated Financial Statements “Pension and Other Postretirement Benefit Plans”).

14. Regulatory

The Federal Deposit Insurance Corporation Improvement Act of 1991 (“FDICIA”) imposes a number of mandatory supervisory measures on banks and thrift institutions. Among other matters, FDICIA established five capital zones or classifications (well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized). Such classifications are used by bank regulatory agencies to determine matters ranging from each institution’s quarterly FDIC deposit insurance premium assessments, to approvals of applications authorizing institutions to grow their asset size or otherwise expand business activities. Under current capital regulations, the Bank is required to comply with each of three separate capital adequacy standards.

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At September 30, 2013, the Bank exceeded each of the three capital requirements and is categorized as "well-capitalized" under the prompt corrective action regulations. Set forth below is a summary of the Bank's compliance:

| (Dollars in thousands) | | Amount | Percent of Assets | |
|---|---|---|---|---|
| Core Capital: | | | | |
| Capital level | $ | 438,423 | 9.48 | % |
| Well capitalized | | 231,234 | 5.00 | |
| Excess | | 207,189 | 4.48 | |
| | | | | |
| Tier 1 Risk-Based Capital: | | | | |
| Capital level | $ | 438,423 | 14.22 | % |
| Well capitalized | | 185,022 | 6.00 | |
| Excess | | 253,401 | 8.22 | |
| | | | | |
| Risk-Based Capital: | | | | |
| Capital level | $ | 469,239 | 15.22 | % |
| Well capitalized | | 308,370 | 10.00 | |
| Excess | | 160,869 | 5.22 | |

As a result of its conversion to a bank holding company on February 28, 2013, the Holding Company became subject to the same regulatory capital requirements as the Bank. At September 30, 2013, the Holding Company's Tier I (leverage) capital, Tier I risk-based capital and Total risk-based capital was 9.64%, 14.47%, and 15.47%, respectively.

15. New Authoritative Accounting Pronouncements

In February 2013, the FASB issued ASU No. 2013-02, which amends the authoritative accounting guidance under ASC Topic 220 "Comprehensive Income." The amendments do not change the current requirements for reporting net income or other comprehensive income in financial statements. However, the amendments require an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under GAAP that provide additional detail about those amounts. The amendments in this update are effective prospectively for reporting periods beginning after December 15, 2012. Adoption of this update did not have a material effect on the Company's consolidated results of operations or financial condition. See Note 13 of the Notes to Consolidated Financial Statements "Accumulated Other Comprehensive Income."

PART I – FINANCIAL INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
Management's Discussion and Analysis of
Financial Condition and Results of Operations

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Quarterly Report should be read in conjunction with the more detailed and comprehensive disclosures included in our Annual Report on Form 10-K for the year ended December 31, 2012. In addition, please read this section in conjunction with our Consolidated Financial Statements and Notes to Consolidated Financial Statements contained herein.

As used in this Quarterly Report, the words "we," "us," "our" and the "Company" are used to refer to Flushing Financia Corporation and our consolidated subsidiaries, including the surviving entity of the merger (the "Merger") on February 28, 2013 of our wholly owned subsidiary, Flushing Savings Bank, FSB (the "Savings Bank") with and into Flushing Commercial Bank (the "Commercial Bank"). The surviving entity of the Merger was the Commercial Bank, whose name has been changed to "Flushing Bank." References herein to the "Bank" mean the Savings Bank (including its wholly owned subsidiary, the Commercial Bank) prior to the Merger and the surviving entity after the Merger.

Statements contained in this Quarterly Report relating to plans, strategies, objectives, economic performance and trends, projections of results of specific activities or investments and other statements that are not descriptions of historical facts may be forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking information is inherently subject to risks and uncertainties and actual results could differ materially from those currently anticipated due to a number of factors, which include, but are not limited to, factors discussed elsewhere in this Quarterly Report and in other documents filed by us with the Securities and Exchange Commission from time to time, including, without limitation, our Annual Report on Form 10-K for the year ended December 31, 2012. Forward-looking statements may be identified by terms such as "may," "will," "should," "could," "expects," "plans," "intends," "anticipates," "believes," "estimates," "predicts," "fo or "continue" or similar terms or the negative of these terms. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We have no obligation to update these forward-looking statements.

Executive Summary

We are a Delaware corporation organized in May 1994. The Savings Bank was organized in 1929 as a New York State-chartered mutual savings bank. In 1994, the Savings Bank converted to a federally chartered mutual savings bank and changed its name from Flushing Savings Bank to Flushing Savings Bank, FSB. The Savings Bank converted from a federally chartered mutual savings bank to a federally chartered stock savings bank on November 21, 1995, at which time Flushing Financial Corporation acquired all of the stock of the Savings Bank. On February 28, 2013, in the Merger, the Savings Bank merged with and into the Commercial Bank, with the Commercial Bank as the surviving entity. Pursuant to the Merger, the Commercial Bank's charter was changed to a full-service New York State chartered commercial bank, and its name was changed to Flushing Bank.

On July 21, 2011, as a result of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the Savings Bank's primary regulator became the Office of the Comptroller of the Currency and Flushing Financial Corporation's primary regulator became the Federal Reserve Board of Governors. Upon completion of the Merger, on February 28, 2013, the Bank's primary regulator became the New York State Department of Financial Services (formerly, the New York State Banking Department), and its primary federal regulator became the Federal Deposit Insurance Corporation ("FDIC"). Deposits are insured to the maximum allowable amount by the FDIC. Additionally, the Bank is a member of the

Federal Home Loan Bank system. Also in connection with the Merger, Flushing Financial Corporation became a bank holding company. We do not anticipate any significant changes to our operations or services as a result of the Merger. The primary business of Flushing Financial Corporation has been the operation of the Bank. The Bank owns three subsidiaries: Flushing Preferred Funding Corporation, Flushing Service Corporation, and FSB Properties Inc. In November 2006, the Bank launched an internet branch, iGObanking.com®. The activities of Flushing Financial Corporation are primarily funded by dividends, if any, received from the Bank, issuances of junior subordinated debt, and issuances of equity securities. Flushing Financial Corporation's common stock is traded on the NASDAQ Global Select Market under the symbol "FFIC."

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Our principal business is attracting retail deposits from the general public and investing those deposits together with funds generated from ongoing operations and borrowings, primarily in (1) originations and purchases of multi-family residential properties and, to a lesser extent, one-to-four family (focusing on mixed-use properties, which are properties that contain both residential dwelling units and commercial units) and commercial real estate mortgage loans; (2) construction loans, primarily for residential properties; (3) Small Business Administration ("SBA") loans and other small business loans; (4) mortgage loan surrogates such as mortgage-backed securities; and (5) U.S. government securities, corporate fixed-income securities and other marketable securities. We also originate certain other consumer loans including overdraft lines of credit. Our results of operations depend primarily on net interest income, which is the difference between the income earned on its interest-earning assets and the cost of our interest-bearing liabilities. Net interest income is the result of our interest rate margin, which is the difference between the average yield earned on interest-earning assets and the average cost of interest-bearing liabilities, adjusted for the difference in the average balance of interest-earning assets as compared to the average balance of interest-bearing liabilities. We also generate non-interest income from loan fees, service charges on deposit accounts, mortgage servicing fees, and other fees, income earned on Bank Owned Life Insurance ("BOLI"), dividends on Federal Home Bank of New York ("FHLB-NY") stock and net gains and losses on sales of securities and loans. Our operating expenses consist principally of employee compensation and benefits, occupancy and equipment costs, other general and administrative expenses and income tax expense. Our results of operations also can be significantly affected by our periodic provision for loan losses and specific provision for losses on real estate owned.

Our strategy is to continue our focus on being an institution serving consumers, businesses, and governmental units in our local markets. In furtherance of this objective, we intend to:

- continue our emphasis on the origination of multi-family residential mortgage loans;
- continue our transition to a commercial banking institution;
- increase our commitment to the multi-cultural marketplace, with a particular focus on the Asian community in Queens;
- maintain asset quality;
- manage deposit growth and maintain a low cost of funds through
  - § business banking deposits,
  - § municipal deposits through government banking, and
  - § new customer relationships via iGObanking.com®;
- cross sell to lending and deposit customers;
- take advantage of market disruptions to attract talent and customers from competitors;
- manage interest rate risk and capital; and
- manage enterprise-wide risk.

There can be no assurance that we will be able to effectively implement this strategy. Our strategy is subject to change by the Board of Directors.

Our investment policy, which is approved by the Board of Directors, is designed primarily to manage the interest rate sensitivity of our overall assets and liabilities, to generate a favorable return without incurring undue interest rate risk and credit risk, to complement our lending activities and to provide and maintain liquidity. In establishing our investment strategies, we consider our business and growth strategies, the economic environment, our interest rate risk exposure, our interest rate sensitivity "gap" position, the types of securities to be held and other factors. We classify our investment securities as available for sale.

We carry a portion of our financial assets and financial liabilities at fair value and record changes in their fair value through earnings in non-interest income on our Consolidated Statements of Income and Comprehensive Income. A description of the financial assets and financial liabilities that are carried at fair value through earnings can be found in Note 10 of the Notes to the Consolidated Financial Statements.

We saw continued improvement in non-performing assets, as they decreased by $12.3 million during the three months ended September 30, 2013. Charge-offs for the third quarter of 2013 were primarily due to sales of delinquent loans and our continued practice of obtaining updated appraisals, and recording charge-offs based on these up-to-date values as opposed to adding to the allowance for loan losses. Net charge-offs in the third quarter were $5.0 million. We do not carry non-performing loans at more than 85% of their current appraised value. This process has ensured that we have kept pace with changing values in the real estate market. The average loan-to-value ratio for our non-performing loans, based upon current appraisals, was 45.4% at the end of the quarter.

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Net loans increased $109.6 million during the third quarter of 2013, as loan originations for the quarter totaled a record $262.2 million. Our loan pipeline at September 30, 2013 grew to $262.2 million from $211.4 million at December 31, 2012. Our lending departments continue to emphasize full relationship banking with our borrowers. Originations were focused on multi-family and commercial business loans, which represented 49% and 38%, respectively, of loan originations during the third quarter of 2013. We generally obtain full banking relationships with these borrowers.

Our net interest margin for the third quarter of 2013 was 3.38%, a decrease of 11 basis points from the second quarter of 2013. While we saw a decrease in our funding costs of five basis points for the quarter, the yield on interest-earning assets decreased 14 basis points. In the current interest rate environment, new loans and securities are added at rates well below our portfolio average yield, and higher yielding loans and securities are prepaid. We also continued to experience higher than average activity in loans refinancing during the third quarter of 2013, which further reduced the yield on our loan portfolio.

Net income for the nine months ended September 30, 2013 was $25.8 million, an increase of $0.7 million, or 2.7%, compared to $25.1 million for the nine months ended September 30, 2012. Diluted earnings per common share were $0.86 for the nine months ended September 30, 2013, an increase of $0.04, or 4.9%, from $0.82 for the nine months ended September 30, 2012.

We recorded a provision for loan losses of $12.9 million for the nine months ended September 30, 2013, which was a decrease of $3.1 million from $16.0 million recorded in the nine months ended September 30, 2012. During the nine months ended September 30, 2013, non-performing loans decreased $28.7 million to $61.2 million from $89.8 million at December 31, 2012. Net charge-offs for the nine months ended September 30, 2013 totaled $13.2 million, or 55 basis points of average loans. The current loan-to-value ratio for our non-performing loans collateralized by real estate was 45.4% at September 30, 2013. When we have obtained properties through foreclosure, we have been able to quickly sell the properties at amounts that approximate book value. We anticipate that we will continue to see low loss content in our loan portfolio. The Bank continues to maintain conservative underwriting standards. As a result of the quarterly analysis of the allowance for loans losses, it was deemed necessary to record a $12.9 million provision for possible loan losses for the nine months ended September 30, 2013. See "-ALLOWANCE FOR LOAN LOSSES."

At September 30, 2013, the Bank continues to be well-capitalized under regulatory requirements, with Core, Tier 1 risk-based and Total risk-based capital ratios of 9.48%, 14.21% and 15.21%, respectively. The Company is also subject to the same regulatory requirements. At September 30, 2013, the Company's capital ratios for Core, Tier 1 risk-based and Total risk-based capital ratios were 9.64%, 14.46% and 15.46%, respectively.

COMPARISON OF OPERATING RESULTS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2013 AND 2012

General. Net income for the three months ended September 30, 2013 was $9.4 million, an increase of $0.1 million, or 0.6%, from the comparable prior year period. Diluted earnings per common share were $0.32 for the three months ended September 30, 2013, an increase of $0.01, or 3.2%, from $0.31 for the three months ended September 30, 2012.

Return on average equity was 8.9% for the three months ended September 30, 2013 compared to 8.7% for the three months ended September 30, 2012. Return on average assets was 0.8% for the three months ended September 30, 2013 compared to 0.9% for the three months ended September 30, 2012.

Interest Income. Total interest and dividend income decreased $3.3 million, or 6.3%, to $49.9 million for the three months ended September 30, 2013 from $53.2 million for the three months ended September 30, 2012. The decrease in interest income was attributable to a 56 basis point decline in the yield of interest-earning assets to 4.56% for the three months ended September 30, 2013 from 5.12% in the comparable prior year period, partially offset by the effect of an increase of $213.5 million in the average balance of interest-earning assets to $4,371.3 million for the three months ended September 30, 2013 from $4,157.8 million for the comparable prior year period. The 56 basis point decline in the yield of interest-earning assets was primarily due to a 47 basis point reduction in the yield of the loan portfolio to 5.18% for the three months ended September 30, 2013 from 5.65% for the three months ended September 30, 2012, combined with an 82 basis point decline in the yield on total securities to 2.77% for the three months ended September 30, 2013 from 3.59% for the comparable prior year period. In addition, the yield of interest-earning assets was negatively impacted by a $127.7 million increase in the average balance of the lower yielding securities portfolio for the three months ended September 30, 2013. $48.0 million of the increase in the average balance of the securities portfolio was due to the purchase of floating rate corporate debt that was purchased to assist in the management of interest rate risk. The 47 basis point decrease in the yield of the loan portfolio was primarily due to a decline in the rates earned on new loan originations and existing loans modified to lower rates, partially offset by an increase in prepayment penalty income during the three months ended September 30, 2013 compared to the three months ended September 30, 2012. The 82 basis point decrease in the yield of the securities portfolio was primarily due to the purchase of new securities at lower yields than the existing portfolio. The yield on the mortgage loan portfolio, excluding prepayment penalty income, decreased 44 basis points to 5.16% for the three months ended September 30, 2013 from 5.60% for the three months ended September 30, 2012.

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Interest Expense. Interest expense decreased $2.7 million, or 17.6%, to $12.9 million for the three months ended September 30, 2013 from $15.6 million for the three months ended September 30, 2012. The decrease in interest expense was due to the reduction in the cost of interest-bearing liabilities, which decreased 36 basis points to 1.29% for the three months ended September 30, 2013 from 1.65% for the comparable prior year period, partially offset by a $190.1 million increase in the average balance of interest-bearing liabilities to $3,981.4 million for the three months ended September 30, 2013 from $3,791.3 million for the comparable prior year period. The 36 basis point decrease in the cost of interest-bearing liabilities was primarily attributable to the Bank reducing the rates it pays on its deposit products and a shifting of deposit concentrations, as higher costing certificates of deposits average balance decreased $313.2 million to $1,191.6 million, while lower costing core deposits average balance increased $291.2 million to $1,759.5 million for the three months ended September 30, 2013. Additionally, the cost of borrowed funds decreased 76 basis points to 2.06% for the three months ended September 30, 2013 from 2.82% for the comparable prior year period. The decrease in the cost of borrowed funds was primarily due to maturing and new borrowings being replaced and obtained at lower rates. The cost of certificates of deposit, money market accounts, savings accounts and NOW accounts decreased 26 basis points, two basis points, one basis point and six basis points, respectively, for the three months ended September 30, 2013 from the comparable prior year period. This resulted in a decrease in the cost of due to depositors of 31 basis points to 1.05% for the three months ended September 30, 2013 from 1.36% for the three months ended September 30, 2012.

Net Interest Income. For the three months ended September 30, 2013, net interest income was $37.0 million, a decrease of $0.6 million, or 1.6%, from $37.6 million for the three months ended September 30, 2012. The decrease in net interest income was attributable to a 20 basis point decrease in the net-interest spread to 3.27% for the three months ended September 30, 2013 from 3.47% for the three months ended September 30, 2012, partially offset by the effect of an increase of $213.5 million in the average balance of interest-earning assets to $4,371.3 million for the three months ended September 30, 2013 from $4,157.8 million for the comparable prior year period. The yield on interest-earning assets decreased 56 basis points to 4.56% for the three months ended September 30, 2013 from 5.12% for the three months ended September 30, 2012, while the cost of funds decreased 36 basis points to 1.29% for the three months ended September 30, 2013 from 1.65% for the comparable prior year period. The net interest margin decreased 24 basis points to 3.38% for the three months ended September 30, 2013 from 3.62% for the three months ended September 30, 2012. Excluding prepayment penalty income, the net interest margin would have decreased 22 basis points to 3.26% for the three months ended September 30, 2013 from 3.48% for the three months ended September 30, 2012.

Provision for Loan Losses. A provision for loan losses of $3.4 million was recorded for the three months ended September 30, 2013, which was a decrease of $1.6 million, or 31.3%, from that recorded for the three months ended September 30, 2012. During the three months ended September 30, 2013, non-performing loans decreased $12.7 million to $61.2 million from $73.9 million at June 30, 2013. Net charge-offs for the three months ended September 30, 2013 totaled $5.0 million, or 61 basis points of average loans. The current loan-to-value ratio for our non-performing loans collateralized by real estate was 45.4% at September 30, 2013. When we have obtained properties through foreclosure, we have been able to quickly sell the properties at amounts that approximate book value. We anticipate that we will continue to see low loss content in our loan portfolio. The Bank continues to maintain conservative underwriting standards. As a result of the quarterly analysis of the allowance for loans losses, it was deemed necessary to record a $3.4 million provision for possible loan losses for the three months ended September 30, 2013. See "-ALLOWANCE FOR LOAN LOSSES."

Non-Interest Income. Non-interest income for the three months ended September 30, 2013 was $0.9 million, a decrease of $2.6 million from $3.5 million for the three months ended September 30, 2012. The decrease in non-interest income was primarily due to a $0.9 million OTTI charge recorded for the three months ended September 30, 2013 on three private issue CMOs and a decrease of $1.0 million in income from fair value adjustments for the three months ended September 30, 2013 compared to the comparable prior year period. Loan fees decreased $0.8 million during the three months ended September 30, 2013, primarily due to the deferral of $0.5 million of loan fees previously recognized in income during 2013 which were deferred in the current quarter to be amortized as a yield adjustment. A corresponding amount of additional compensation expense for loan origination costs was also deferred during the current quarter. These decreases were partially offset by a $0.2 million increase in income from bank owned life insurance ("BOLI") compared to the three months ended September 30, 2012.

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Non-Interest Expense. Non-interest expense was $19.1 million for the three months ended September 30, 2013, a decrease of $1.7 million from $20.7 million for the three months ended September 30, 2012. The decrease was primarily due to decreases of $0.4 million in FDIC insurance expense primarily due to a reduction in the assessment rate, $0.5 million in OREO/foreclosure expense primarily due to a reduction in non-accrual loans, $0.2 million in net losses on sales of OREO and $0.3 million in professional services.

Income before Income Taxes. Income before the provision for income taxes increased $0.1 million, or 0.6%, to $15.4 million for the three months ended September 30, 2013 from $15.3 million for the three months ended September 30, 2012 for the reasons discussed above.

Provision for Income Taxes. Income tax expense was $6.0 million for the three months ended September 30, 2013 and 2012. The effective tax rate was 39.0% for the three months ended September 30, 2013 and 2012.

COMPARISON OF OPERATING RESULTS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2013 AND 2012

General. Net income for the nine months ended September 30, 2013 was $25.8 million, an increase of $0.7 million, or 2.7%, compared to $25.1 million for the nine months ended September 30, 2012. Diluted earnings per common share were $0.86 for the nine months ended September 30, 2013, an increase of $0.04, or 4.9%, from $0.82 for the nine months ended September 30, 2012.

Return on average equity was 7.9% for both of the nine months ended September 30, 2013 and 2012. Return on average assets was 0.8% for both of the nine months ended September 30, 2013 and 2012.

Interest Income. Total interest and dividend income decreased $11.8 million, or 7.3%, to $150.2 million for the nine months ended September 30, 2013 from $162.0 million for the nine months ended September 30, 2012. The decrease in interest income was attributable to a 55 basis point decline in the yield of interest-earning assets to 4.69% for the nine months ended September 30, 2013 from 5.24% in the comparable prior year period. The decrease in the yield was partially offset by a $143.0 million increase in the average balance of interest-earning assets to $4,268.5 million for the nine months ended September 30, 2013 from $4,125.5 million for the comparable prior year period. The 55 basis point decline in the yield of interest-earning assets was primarily due to a 44 basis point reduction in the yield of the loan portfolio to 5.31% for the nine months ended September 30, 2013 from 5.75% for the nine months ended September 30, 2012, combined with a 76 basis point decline in the yield on total securities to 2.89% for the nine months ended September 30, 2013 from 3.65% for the comparable prior year period. In addition, the yield of interest-earning assets was negatively impacted by a $116.9 million increase in the average balance of the lower yielding securities portfolio for the nine months ended September 30, 2013. The 44 basis point decrease in the yield of the loan portfolio was primarily due to a decline in the rates earned on new loan originations and existing loans modified to lower rates. The 76 basis point decrease in the yield of the securities portfolio was primarily due to the purchase of new securities at lower yields than the existing portfolio. The yield on the mortgage loan portfolio decreased 38 basis points to 5.46% for the nine months ended September 30, 2013 from 5.84% for the nine months ended September 30, 2012. The yield on the mortgage loan portfolio, excluding prepayment penalty income, decreased 42 basis points to 5.29% for the nine months ended September 30, 2013 from 5.71% for the nine months ended September 30, 2012.

Interest Expense. Interest expense decreased $7.0 million, or 14.3%, to $41.8 million for the nine months ended September 30, 2013 from $48.8 million for the nine months ended September 30, 2012. The decrease in interest expense was due to the reduction in the cost of interest-bearing liabilities, which decreased 29 basis points to 1.43% for the nine months ended September 30, 2013 from 1.72% for the comparable prior year period and a shifting of deposit concentrations, as higher costing certificates of deposits average balance decreased $287.7 million to $1,187.4 million, while lower costing core deposits average balance increased $214.1 million to $1,724.2 million for the nine months ended September 30, 2013. The 29 basis point decrease in the cost of interest-bearing liabilities was primarily attributable to the Bank reducing the rates it pays on its deposit products and a reduction in the cost of borrowed funds. The cost of certificates of deposit, money market accounts, savings accounts and NOW accounts decreased 24 basis points, 10 basis points, three basis points and nine basis points, respectively, for the nine months ended September 30, 2013 from the comparable prior year period. This resulted in a decrease in the cost of due to depositors of 28 basis points to 1.11% for the nine months ended September 30, 2013 from 1.39% for the nine months ended September 30, 2012. The cost of borrowed funds decreased 60 basis points to 2.52% for the nine months ended September 30, 2013 from 3.12% for the nine months ended September 30, 2012 with the average balance increasing $183.4 million to $933.3 million for the nine months ended September 30, 2013 from $749.9 million for the nine months ended September 30, 2012. The decline in the cost of borrowed funds was primarily due to the prepayment of $68.5 million in FHLB-NY advances during the first quarter of 2013 at an average cost of 3.21% which was scheduled to mature in 2014 and replacing those borrowings with new long-term advances costing 0.75%, partially offset by a $2.6 million prepayment penalty incurred on the transaction.

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Net Interest Income. For the nine months ended September 30, 2013, net interest income was $108.4 million, a decrease of $4.8 million, or 4.2%, from $113.2 million for the nine months ended September 30, 2012. The decrease in net interest income was attributable to a 26 basis point decrease in the net-interest spread to 3.26% for the nine months ended September 30, 2013 from 3.52% for the nine months ended September 30, 2012, partially offset by the effect of an increase of $143.0 million in the average balance of interest-earning assets to $4,268.5 million for the nine months ended September 30, 2013 from $4,125.5 million for the comparable prior year period. The yield on interest-earning assets decreased 55 basis points to 4.69% for the nine months ended September 30, 2013 from 5.24% for the nine months ended September 30, 2012, while the cost of funds decreased 29 basis points to 1.43% for the nine months ended September 30, 2013 from 1.72% for the comparable prior year period. The net interest margin decreased 27 basis points to 3.39% for the nine months ended September 30, 2013 from 3.66% for the nine months ended September 30, 2012. Excluding prepayment penalty income on loans and securities, as well as prepayment penalties on borrowings, the net interest margin would have decreased 19 basis points to 3.35% for the nine months ended September 30, 2013 from 3.54% for the nine months ended September 30, 2012.

Provision for Loan Losses. A provision for loan losses of $12.9 million was recorded for the nine months ended September 30, 2013, which was a decrease of $3.1 million from $16.0 million recorded in the nine months ended September 30, 2012. During the nine months ended September 30, 2013, non-performing loans decreased $28.7 million to $61.2 million from $89.8 million at December 31, 2012. Net charge-offs for the nine months ended September 30, 2013 totaled $13.2 million, or 55 basis points of average loans. The current loan-to-value ratio for our non-performing loans collateralized by real estate was 45.4% at September 30, 2013. When we have obtained properties through foreclosure, we have been able to quickly sell the properties at amounts that approximate book value. We anticipate that we will continue to see low loss content in our loan portfolio. The Bank continues to maintain conservative underwriting standards. As a result of the quarterly analysis of the allowance for loans losses, it was deemed necessary to record a $12.9 million provision for possible loan losses for the nine months ended September 30, 2013. See "-ALLOWANCE FOR LOAN LOSSES."

Non-Interest Income. Non-interest income for the nine months ended September 30, 2013 was $8.5 million, an increase of $2.0 million from $6.5 million for the nine months ended September 30, 2012. The increase in non-interest income was primarily due to the $2.9 million gain from the sale of mortgage-backed securities during the nine months ended September 30, 2013 as part of a balance sheet restructuring as discussed above under "Balance Sheet Restructuring". Non-interest income also improved due to a $0.4 million increase in BOLI income. These increases were partially offset by a $0.4 million increase in net losses from fair value adjustments and a $0.6 million increase in OTTI charges recorded on private issue CMOs during the nine months ended September 30, 2013 compared to the nine months ended September 30, 2012. Additionally, loan fees decreased $0.5 million during the nine months ended September 30, 2013, primarily due to the deferral of loan fees to be amortized as yield adjustments. A corresponding amount of additional compensation expense for loan origination costs was also deferred during the current quarter.

Non-Interest Expense. Non-interest expense was $61.7 million for the nine months ended September 30, 2013, a decrease of $0.8 million, or 1.3%, from $62.5 million for the nine months ended September 30, 2012. The decrease was primarily due to decreases of $0.7 million in FDIC insurance expense primarily due to a reduction in the assessment rate, $0.7 million in OREO/foreclosure expense primarily due to a reduction in non-accrual loans, $0.5 million in net losses on sales of OREO and $0.4 million in professional services. These decreases were partially offset by a $1.7 million increase in salaries and employee benefits expense primarily due to annual salary increases and increased incentives for loan and deposit growth.

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Income before Income Taxes. Income before the provision for income taxes increased $1.1 million, or 2.7%, to $42.3 million for the nine months ended September 30, 2013 from $41.2 million for the nine months ended September 30, 2012 for the reasons discussed above.

Provision for Income Taxes. Income tax expense increased $0.4 million to $16.5 million for the nine months ended September 30, 2013 from $16.1 million for the nine months ended September 30, 2012. The effective tax rate was 39.0% for the nine months ended September 30, 2013 and 2012.

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Assets. Total assets at September 30, 2013 were $4,732.3 million, an increase of $280.8 million, or 6.3%, from $4,451.4 million at December 31, 2012. Total loans, net increased $162.3 million during the nine months ended September 30, 2013 to $3,365.3 million from $3,203.0 million at December 31, 2012. Loan originations and purchases were $635.2 million for the nine months ended September 30, 2013, an increase of $202.0 million from $433.2 million for the nine months ended September 30, 2012. During the nine months ended September 30, 2013, we continued to focus on the origination of multi-family properties and business loans with a full relationship. Loan applications in process have continued to remain strong, totaling $262.2 million at September 30, 2013 compared to $211.4 million at December 31, 2012 and $198.0 million at September 30, 2012.

The following table shows loan originations and purchases for the periods indicated:

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|---|---|---|---|
| (In thousands) | 2013 | 2012 | 2013 | 2012 |
| Multi-family residential | $ 127,310 | $ 69,299 | $ 302,527 | $ 211,052 |
| Commercial real estate (1) | 14,180 | 1,943 | 52,778 | 21,756 |
| One-to-four family – mixed-use property | 10,719 | 3,474 | 22,453 | 13,955 |
| One-to-four family – residential | 7,986 | 7,382 | 20,876 | 18,076 |
| Co-operative apartments | 1,037 | 100 | 4,799 | 1,726 |
| Construction | 163 | 83 | 1,951 | 653 |
| Small Business Administration | 92 | 180 | 470 | 513 |
| Taxi Medallion (2) | - | - | - | 3,464 |
| Commercial business and other | 100,664 | 68,452 | 229,365 | 162,053 |
| Total | $ 262,151 | $ 150,913 | $ 635,219 | $ 433,248 |

(1) Includes purchases of $0.5 million for the nine months ended September 30, 2013.
(2) Includes purchases of $3.5 million for the nine months ended September 30, 2012.

The Bank continues to maintain conservative underwriting standards that include, among other things, a loan-to-value ratio of 75% or less and a debt coverage ratio of at least 125%. Multi-family residential, commercial real estate and one-to-four family mixed-use property mortgage loans originated during the three months ended September 30, 2013 had an average loan-to-value ratio of 44.1% and an average debt coverage ratio of 249%.

The Bank's non-performing assets totaled $68.5 million at September 30, 2013, a decrease of $30.0 million from $98.5 million at December 31, 2012. Total non-performing assets as a percentage of total assets were 1.45% at September

30, 2013 and 2.21% at December 31, 2012. The ratio of allowance for loan losses to total non-performing loans was 50.4% at September 30, 2013 and 34.6% at December 31, 2012. See – "TROUBLED DEBT RESTRUCUTURED AND NON-PERFORMING ASSETS."

During the nine months ended September 30, 2013, mortgage-backed securities increased $65.1 million, or 9.0%, to $785.2 million from $720.1 million at December 31, 2012. The increase in mortgage-backed securities during the nine months ended September 30, 2013 was primarily due to purchases of $292.3 million, partially offset by sales and repayments of $68.5 million and $122.4 million, respectively. During the nine months ended September 30, 2013, other securities increased $43.9 million, or 19.1%, to $273.3 million from $229.5 million at December 31, 2012. The increase in other securities during the nine months ended September 30, 2013 was primarily due to purchases of $88.0 million, partially offset by $30.5 million in calls and sales of $5.9 million. Other securities primarily consist of securities issued by government agencies, mutual or bond funds that invest in government and government agency securities and corporate bonds.

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Liabilities. Total liabilities were $4,305.3 million at September 30, 2013, an increase of $296.2 million, or 7.4%, from $4,009.1 million at December 31, 2012. During the nine months ended September 30, 2013, due to depositors increased $215.7 million, or 7.2%, to $3,198.3 million as a result of a $226.6 million increase in core deposits partially offset by a $10.9 million decrease in certificates of deposit. Borrowed funds increased $69.8 million during the nine months ended September 30, 2013. The increase in borrowed funds was primarily due to a net increase of $109.4 million in long-term borrowings partially offset by a $43.0 million net decrease in short-term borrowings.

Equity. Total stockholders' equity decreased $15.4 million, or 3.5%, to $427.0 million at September 30, 2013 from $442.4 million at December 31, 2012. Stockholders' equity decreased primarily due to a decrease in comprehensive income of $20.3 million primarily due to a decline in the market value of the securities portfolio, the purchase of 836,092 shares of treasury stock at a cost of $13.2 million and the declaration and payment of a dividend of $0.39 per common share totaling $11.8 million, partially offset by net income of $25.8 million and $1.4 million due to the issuance of shares from the annual funding of certain employee retirement plans through the release of common shares from the Employee Benefit Trust. In addition, the exercise of stock options increased stockholders' equity by $0.2 million, including the income tax benefit realized. Book value per common share was $14.19 at September 30, 2013 compared to $14.39 at December 31, 2012. Tangible book value per common share was $13.67 at September 30, 2013 compared to $13.87 at December 31, 2012.

During the nine months ended September 30, 2013, the Company completed the common stock repurchase program that was approved by the Company's Board of Directors on September 20, 2011. On May 22, 2013, the Company announced the authorization by the Board of Directors of a new common stock repurchase program which authorizes the purchase of up to 1,000,000 shares of its common stock. During the nine months ended September 30, 2013, the Company repurchased 836,092 shares of the Company's common stock at an average cost of $15.73 per share. At September 30, 2013, 549,870 shares remain to be repurchased under the current stock repurchase program. The repurchase program does not have an expiration date or a maximum dollar amount that may be paid to repurchase the common shares. Stock repurchases under this program will be made from time to time, on the open market or in privately negotiated transactions, at the discretion of the management of the Company.

Cash flow. During the nine months ended September 30, 2013, funds provided by the Company's operating activities amounted to $56.6 million. These funds combined with $264.6 million provided by financing activities and were utilized to fund net investing activities of $321.3 million. The Company's primary business objective is the origination and purchase of one-to-four family (including mixed-use properties), multi-family residential and commercial real estate mortgage loans and commercial, business and SBA loans. During the nine months ended September 30, 2013, the net total of loan originations and purchases less loan repayments and sales was $176.9 million. During the nine months ended September 30, 2013, the Company also funded $380.3 million in purchases of securities available for sale. During the nine months ended September 30, 2013, funds were provided by a $223.3 million net increase in deposits and $109.4 million net increase in long-term borrowed funds. Additionally, funds were provided by $236.6 million in proceeds from maturities, sales, calls and prepayments of securities available for sale. The Company also used funds of $43.0 million, $14.1 million and $11.7 million for net repayments of short-term borrowed funds, purchases of treasury stock and dividend payments, respectively, during the nine months ended September 30, 2013.

INTEREST RATE RISK

The Consolidated Statements of Financial Position have been prepared in accordance with generally accepted accounting principles in the United States of America, which require the measurement of financial position and

operating results in terms of historical dollars without considering the changes in fair value of certain investments due to changes in interest rates. Generally, the fair value of financial investments such as loans and securities fluctuates inversely with changes in interest rates. As a result, increases in interest rates could result in decreases in the fair value of the Company's interest-earning assets which could adversely affect the Company's results of operation if such assets were sold, or, in the case of securities classified as available-for-sale, decreases in the Company's stockholders' equity, if such securities were retained.

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The Company manages the mix of interest-earning assets and interest-bearing liabilities on a continuous basis to maximize return and adjust its exposure to interest rate risk. On a quarterly basis, management prepares the "Earnings and Economic Exposure to Changes in Interest Rate" report for review by the Board of Directors, as summarized below. This report quantifies the potential changes in net interest income and net portfolio value should interest rates go up or down 200 basis points (shocked), assuming the yield curves of the rate shocks will be parallel to each other. Net portfolio value is defined as the market value of assets net of the market value of liabilities. The market value of assets and liabilities is determined using a discounted cash flow calculation. The net portfolio value ratio is the ratio of the net portfolio value to the market value of assets. All changes in income and value are measured as percentage changes from the projected net interest income and net portfolio value at the base interest rate scenario. The base interest rate scenario assumes interest rates at September 30, 2013. Various estimates regarding prepayment assumptions are made at each level of rate shock. Actual results could differ significantly from these estimates. At September 30, 2013, the Company was within the guidelines set forth by the Board of Directors for each interest rate level.

The following table presents the Company's interest rate shock as of September 30, 2013:

| | Projected Percentage Change In | | | | | |
|---|---|---|---|---|---|---|
| Change in Interest Rate | Net Interest Income | | Net Portfolio Value | | Net Portfolio Value Ratio | |
| -200 Basis points | -2.36 | % | 12.14 | % | 13.56 | % |
| -100 Basis points | 0.31 | | 8.64 | | 13.34 | |
| Base interest rate | 0.00 | | 0.00 | | 12.62 | |
| +100 Basis points | -5.49 | | -12.97 | | 11.34 | |
| +200 Basis points | -11.17 | | -26.06 | | 9.95 | |

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AVERAGE BALANCES

Net interest income represents the difference between income on interest-earning assets and expense on interest-bearing liabilities. Net interest income depends upon the relative amount of interest-earning assets and interest-bearing liabilities and the interest rate earned or paid on them. The following table sets forth certain information relating to the Company's Consolidated Statements of Financial Condition and Consolidated Statements of Income for the three months ended September 30, 2013 and 2012, and reflects the average yield on assets and average cost of liabilities for the periods indicated. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods shown. Average balances are derived from average daily balances. The yields include amortization of fees which are considered adjustments to yields.

| | For the three months ended September 30, | | | | | |
|---|---|---|---|---|---|---|
| | 2013 | | | 2012 | | |
| | Average Balance | Interest | Yield/ Cost | Average Balance | Interest | Cost |
| Assets | | | | | | |
| Interest-earning assets: | | | | | | |
| Mortgage loans, net (1) | $ 2,948,640 | 39,358 | 5.34 % | $ 2,889,894 | 41,373 | 5.73 % |
| Other loans, net (1) | 338,315 | 3,182 | 3.76 | 285,360 | 3,484 | 4.88 |
| Total loans, net | 3,286,955 | 42,540 | 5.18 | 3,175,254 | 44,857 | 5.65 |
| Mortgage-backed securities | 787,680 | 5,732 | 2.91 | 693,001 | 6,765 | 3.90 |
| Other securities | 265,751 | 1,566 | 2.36 | 232,684 | 1,546 | 2.66 |
| Total securities | 1,053,431 | 7,298 | 2.77 | 925,685 | 8,311 | 3.59 |
| Interest-earning deposits and federal funds sold | 30,905 | 13 | 0.17 | 56,813 | 25 | 0.18 |
| Total interest-earning assets | 4,371,291 | 49,851 | 4.56 | 4,157,752 | 53,193 | 5.12 |
| Other assets | 250,745 | | | 244,556 | | |
| Total assets | $ 4,622,036 | | | $ 4,402,308 | | |
| | | | | | | |
| Liabilities and Equity | | | | | | |
| Interest-bearing liabilities: | | | | | | |
| Deposits: | | | | | | |
| Savings accounts | $ 270,956 | 126 | 0.19 | $ 306,573 | 150 | 0.20 |
| NOW accounts | 1,298,242 | 1,673 | 0.52 | 989,644 | 1,446 | 0.58 |
| Money market accounts | 190,262 | 70 | 0.15 | 172,013 | 75 | 0.17 |
| Certificate of deposit accounts | 1,191,574 | 5,898 | 1.98 | 1,504,736 | 8,417 | 2.24 |
| Total due to depositors | 2,951,034 | 7,767 | 1.05 | 2,972,966 | 10,088 | 1.36 |
| Mortgagors' escrow accounts | 40,596 | 9 | 0.09 | 35,729 | 9 | 0.10 |
| Total deposits | 2,991,630 | 7,776 | 1.04 | 3,008,695 | 10,097 | 1.34 |
| Borrowed funds | 989,791 | 5,090 | 2.06 | 782,614 | 5,513 | 2.82 |
| Total interest-bearing liabilities | 3,981,421 | 12,866 | 1.29 | 3,791,309 | 15,610 | 1.65 |
| Non interest-bearing deposits | 175,217 | | | 139,562 | | |
| Other liabilities | 44,272 | | | 38,279 | | |
| Total liabilities | 4,200,910 | | | 3,969,150 | | |
| Equity | 421,126 | | | 433,158 | | |

| | | | | | | |
|---|---|---|---|---|---|---|
| Total liabilities and equity | $ 4,622,036 | | | $ 4,402,308 | | |
| Net interest income / net interest rate spread | | $ 36,985 | 3.27 % | | $ 37,583 | 3.47 % |
| Net interest-earning assets / net interest margin | $ 389,870 | | 3.38 % | $ 366,443 | | 3.62 % |
| Ratio of interest-earning assets to interest-bearing liabilities | | | 1.10 X | | | 1.10 X |

(1) Loan interest income includes net amortization of deferred fees and costs, late charges, and prepayment penalties of approximately $0.9 million and $0.8 million for the three months ended September 30, 2013 and 2012, respectively.

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The following table sets forth certain information relating to the Company's Consolidated Statements of Financial Condition and Consolidated Statements of Income for the nine months ended September 30, 2013 and 2012, and reflects the average yield on assets and average cost of liabilities for the periods indicated. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods shown. Average balances are derived from average daily balances. The yields include amortization of fees which are considered adjustments to yields.

| | For the nine months ended September 30, | | | | | |
|---|---|---|---|---|---|---|
| | 2013 | | | 2012 | | |
| | Average Balance | Interest | Yield/ Cost | Average Balance | Interest | Yield/ Cost |
| Assets | | | | | | |
| Interest-earning assets: | | | | | | |
| Mortgage loans, net (1) | $2,904,864 | 118,921 | 5.46 % | $2,902,201 | 127,111 | 5.84 % |
| Other loans, net (1) | 316,530 | 9,420 | 3.97 | 288,834 | 10,429 | 4.81 |
| Total loans, net | 3,221,394 | 128,341 | 5.31 | 3,191,035 | 137,540 | 5.75 |
| Mortgage-backed securities | 763,918 | 17,321 | 3.02 | 704,347 | 20,652 | 3.91 |
| Other securities | 243,472 | 4,516 | 2.47 | 186,165 | 3,747 | 2.68 |
| Total securities | 1,007,390 | 21,837 | 2.89 | 890,512 | 24,399 | 3.65 |
| Interest-earning deposits and federal funds sold | 39,669 | 54 | 0.18 | 43,913 | 53 | 0.16 |
| Total interest-earning assets | 4,268,453 | 150,232 | 4.69 | 4,125,460 | 161,992 | 5.24 |
| Other assets | 260,912 | | | 240,724 | | |
| Total assets | $4,529,365 | | | $4,366,184 | | |
| | | | | | | |
| Liabilities and Equity | | | | | | |
| Interest-bearing liabilities: | | | | | | |
| Deposits: | | | | | | |
| Savings accounts | $277,451 | 389 | 0.19 | $325,333 | 546 | 0.22 |
| NOW accounts | 1,273,909 | 5,044 | 0.53 | 1,001,843 | 4,685 | 0.62 |
| Money market accounts | 172,868 | 197 | 0.15 | 182,978 | 340 | 0.25 |
| Certificate of deposit accounts | 1,187,403 | 18,504 | 2.08 | 1,475,118 | 25,634 | 2.32 |
| Total due to depositors | 2,911,631 | 24,134 | 1.11 | 2,985,272 | 31,205 | 1.39 |
| Mortgagors' escrow accounts | 46,171 | 26 | 0.08 | 41,179 | 27 | 0.09 |
| Total deposits | 2,957,802 | 24,160 | 1.09 | 3,026,451 | 31,232 | 1.38 |
| Borrowed funds | 933,318 | 17,645 | 2.52 | 749,878 | 17,545 | 3.12 |
| Total interest-bearing liabilities | 3,891,120 | 41,805 | 1.43 | 3,776,329 | 48,777 | 1.72 |
| Non interest-bearing deposits | 162,732 | | | 128,912 | | |
| Other liabilities | 42,026 | | | 35,076 | | |
| Total liabilities | 4,095,878 | | | 3,940,317 | | |
| Equity | 433,487 | | | 425,867 | | |
| Total liabilities and equity | $4,529,365 | | | $4,366,184 | | |
| | | | | | | |
| Net interest income / net interest rate spread | | $108,427 | 3.26 % | | $113,215 | 3.52 % |

| | | | | | | |
|---|---|---|---|---|---|---|
| Net interest-earning assets / net interest margin | $377,333 | 3.39 | % | $349,131 | 3.66 | % |
| Ratio of interest-earning assets to interest-bearing liabilities | | 1.10 | X | | 1.09 | X |

(1) Loan interest income includes net amortization of deferred fees and costs, late charges, and prepayment penalties of approximately $2.7 million and $2.2 million for the nine months ended September 30, 2013 and 2012, respectively.

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LOANS

The following table sets forth the Company's loan originations (including the net effect of refinancing) and the changes in the Company's portfolio of loans, including purchases, sales and principal reductions for the periods indicated.

| (In thousands) | For the nine months ended September 30, 2013 | 2012 |
|---|---|---|
| Mortgage Loans | | |
| At beginning of period | $ 2,906,881 | $ 2,939,012 |
| Mortgage loans originated: | | |
| Multi-family residential | 302,527 | 211,052 |
| Commercial real estate | 52,326 | 21,756 |
| One-to-four family – mixed-use property | 22,453 | 13,955 |
| One-to-four family – residential | 20,876 | 18,076 |
| Co-operative apartments | 4,799 | 1,726 |
| Construction | 1,951 | 653 |
| Total mortgage loans originated | 404,932 | 267,218 |
| Mortgage loans purchased: | | |
| Commercial Loans Purchased | 452 | - |
| Total mortgage loans Purchased | 452 | - |
| Less: | | |
| Principal and other reductions | 281,786 | 284,687 |
| Sales | 22,984 | 33,048 |
| At end of period | $ 3,007,495 | $ 2,888,495 |
| Commercial Business and Other Loans | | |
| At beginning of period | $ 314,494 | $ 274,981 |
| Other loans originated: | | |
| Small business administration | 470 | 513 |
| Taxi Medallion | - | 8 |
| Commercial business | 225,337 | 158,730 |
| Other | 4,028 | 3,323 |
| Total other loans originated | 229,835 | 162,574 |
| Other loans purchased: | | |
| Taxi Medallion | - | 3,456 |

| | | |
|---|---|---|
| Total other loans purchased | - | 3,456 |
| | | |
| Less: | | |
| Principal and other reductions | 164,787 | 148,967 |
| Sales and loans transferred to available for sale | 2,382 | 7,179 |
| | | |
| At end of period | $ 377,160 | $ 284,865 |

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TROUBLED DEBT RESTRUCUTURED AND NON-PERFORMING ASSETS

Management continues to adhere to the Bank's conservative underwriting standards. The majority of the Bank's non-performing loans are collateralized by residential income producing properties that are occupied, thereby retaining more of their value and reducing the potential loss. The Bank takes a proactive approach to managing delinquent loans, including conducting site examinations and encouraging borrowers to meet with a Bank representative. The Bank has been developing short-term payment plans that enable certain borrowers to bring their loans current. The Bank reviews its delinquencies on a loan by loan basis and continually explores ways to help borrowers meet their obligations and return them back to current status. At times, the Bank may restructure a loan to enable a borrower to continue making payments when it is deemed to be in the best long-term interest of the Bank. This restructure may include making concessions to the borrower that the Bank would not make in the normal course of business, such as reducing the interest rate until the next reset date, extending the amortization period thereby lowering the monthly payments, or changing the loan to interest only payments for a limited time period. At times, certain problem loans have been restructured by combining more than one of these options. The Bank believes that restructuring these loans in this manner will allow certain borrowers to become and remain current on their loans. The Bank classifies these loans as TDR. Loans which have been current for six consecutive months at the time they are restructured as TDR remain on accrual status. Loans which were delinquent at the time they are restructured as a TDR are placed on non-accrual status until they have made timely payments for six consecutive months. Loans that are restructured as TDR but are not performing in accordance with the restructured terms are excluded from the TDR table below, as they are placed on non-accrual status and reported as non-performing loans.

The following table shows loans classified as TDR that are performing according to their restructured terms at the periods indicated:

| (In thousands) | September 30, 2013 | June 30, 2013 | December 31, 2012 |
|---|---|---|---|
| Accrual Status: | | | |
| Multi-family residential | $ 2,812 | $ 2,822 | $ 2,348 |
| Commercial real estate | 3,786 | 3,797 | 3,263 |
| One-to-four family - mixed-use property | 2,307 | 2,317 | 2,338 |
| One-to-four family - residential | 367 | 369 | 374 |
| Construction | 1,612 | 1,612 | 3,500 |
| Commercial business and other | 4,368 | 4,403 | 3,849 |
| Total | 15,252 | 15,320 | 15,672 |
| Non-accrual status: | | | |
| Commercial real estate | 3,552 | 4,045 | 3,872 |
| One-to-four family - mixed-use property | 385 | 386 | - |
| Total | 3,937 | 4,431 | 3,872 |
| Total performing troubled debt restructured | $ 19,189 | $ 19,751 | $ 19,544 |

During the nine months ended September 30, 2013, five loans totaling $2.2 million were restructured and classified as TDR, while $2.0 million in repayments were received.

Interest income on loans is recognized on the accrual basis. The accrual of income on loans is discontinued when certain factors, such as contractual delinquency of 90 days or more, indicate reasonable doubt as to the timely collectability of such income. Additionally, uncollected interest previously recognized on non-accrual loans is reversed from interest income at the time the loan is placed on non-accrual status. Loans in default 90 days or more as to their maturity date but not their payments continue to accrue interest as long as the borrower continues to remit monthly payments.

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The following table shows non-performing assets at the periods indicated:

| (In thousands) | September 30, 2013 | June 30, 2013 | December 31, 2012 |
|---|---|---|---|
| Loans 90 days or more past due and still accruing: | | | |
| Multi-family residential | $ 479 | $ - | $ - |
| Commercial real estate | 298 | - | - |
| One-to-four family - residential | 15 | 15 | - |
| Commercial business and other | 502 | 558 | 644 |
| Total | 1,294 | 573 | 644 |
| | | | |
| Non-accrual loans: | | | |
| Multi-family residential | 18,445 | 19,273 | 16,486 |
| Commercial real estate | 10,653 | 12,676 | 15,640 |
| One-to-four family - mixed-use property | 9,854 | 11,272 | 18,280 |
| One-to-four family - residential | 13,229 | 12,158 | 13,726 |
| Co-operative apartments | 160 | 160 | 234 |
| Construction | 4,962 | 7,326 | 7,695 |
| Small business administration | - | 445 | 283 |
| Commercial business and other | 2,564 | 9,999 | 16,860 |
| Total | 59,867 | 73,309 | 89,204 |
| | | | |
| Total non-performing loans | 61,161 | 73,882 | 89,848 |
| | | | |
| Other non-performing assets: | | | |
| Real estate acquired through foreclosure | 3,503 | 2,591 | 5,278 |
| Investment securities | 3,831 | 4,301 | 3,332 |
| Total | 7,334 | 6,892 | 8,610 |
| | | | |
| Total non-performing assets | $ 68,495 | $ 80,774 | $ 98,458 |

Included in non-accrual loans were three loans totaling $7.3 million, four loans totaling $10.1 million and seven loans totaling $11.1 million which were restructured as TDR which were not performing in accordance with their restructured terms at September 30, 2013, June 30, 2013 and December 31, 2012, respectively.

The Bank's non-performing assets totaled $68.5 million at September 30, 2013, a decrease of $12.3 million from $80.8 million at June 30, 2013 and a decrease of $30.0 million from $98.5 million at December 31, 2012. Total non-performing assets as a percentage of total assets were 1.45% at September 30, 2013, 1.76% at June 30, 2013 and 2.21% at December 31, 2012. The ratio of allowance for loan losses to total non-performing loans was 50.4% at September 30, 2013, 43.8% at June 30, 2013 and 34.6% at December 31, 2012.

The Bank's non-performing loans totaled $61.2 million at September 30, 2013, a decrease of $12.7 million from $73.9 million at June 30, 2013 and a decrease of $28.7 million from $89.8 million at December 31, 2012. During the three months ended September 30, 2013, 29 loans totaling $11.1 million were added to non-accrual loans, 12 loans totaling $3.6 million were returned to performing status, nine loans totaling $7.9 million were paid in full, seven loans totaling

$4.3 million were sold, seven loans totaling $1.6 million were transferred to other real estate owned and charge-offs of $4.7 million were recorded on non-performing loans that were non-performing at the beginning of the third quarter of 2013.

Non-performing investment securities include two pooled trust preferred securities for which we are not receiving payments. At September 30, 2013, these investment securities had a combined amortized cost and market value of $8.3 million and $3.8 million, respectively.

The following table shows our delinquent loans that are less than 90 days past due still accruing interest and considered performing at the periods indicated:

| | September 30, 2013 | | December 31, 2012 | |
|---|---|---|---|---|
| | 60 - 89 days | 30 - 59 days | 60 - 89 days | 30 - 59 days |
| | (In thousands) | | | |
| Multi-family residential | $2,864 | $ 15,471 | $4,827 | $ 24,059 |
| Commercial real estate | 5,015 | 9,378 | 3,622 | 9,764 |
| One-to-four family - mixed-use property | 685 | 19,497 | 3,368 | 21,012 |
| One-to-four family - residential | 1,200 | 2,276 | 1,886 | 3,407 |
| Co-operative apartments | - | - | - | - |
| Construction loans | - | - | - | 2,462 |
| Small Business Administration | - | 148 | - | 404 |
| Taxi medallion | - | - | - | - |
| Commercial business and other | - | - | 6 | 2 |
| Total delinquent loans | $9,764 | $ 46,770 | $13,709 | $ 61,110 |

CRITICIZED AND CLASSIFIED ASSETS

Our policy is to review our assets, focusing primarily on the loan portfolio, other real estate owned and the investment portfolios, to ensure that the credit quality is maintained at the highest levels. When weaknesses are identified, immediate action is taken to correct the problem through direct contact with the borrower or issuer. We then monitor these assets and, in accordance with our policy and current regulatory guidelines, we designate them as “Special Mention,” which is considered a “Criticized Asset,” and “Substandard,” “Doubtful,” or “Loss,” which are considered “Classif Assets,” as deemed necessary. We designate an asset as Substandard when a well-defined weakness is identified that jeopardizes the orderly liquidation of the debt. We designate an asset as Doubtful when it displays the inherent weakness of a Substandard asset with the added provision that collection of the debt in full, on the basis of existing facts, is highly improbable. We designate an asset as Loss if it is deemed the debtor is incapable of repayment. Loans that are designated as Loss are charged to the Allowance for Loan Losses. Assets that are non-accrual are designated as Substandard, Doubtful or Loss. We designate an asset as Special Mention if the asset does not warrant designation within one of the other categories, but does contain a potential weakness that deserves closer attention. Our total Criticized and Classified assets were $167.1 million at September 30, 2013, a decrease of $57.2 million from $224.2 million at December 31, 2012.

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The following table sets forth the Banks' assets designated as Criticized and Classified at September 30, 2013:

| (In thousands) | Special Mention | Substandard | Doubtful | Loss | Total |
|---|---|---|---|---|---|
| Loans: | | | | | |
| Multi-family residential | $ 10,848 | $ 23,735 | $ - | $ - | $ 34,583 |
| Commercial real estate | 12,885 | 21,300 | - | - | 34,185 |
| One-to-four family - mixed-use property | 9,656 | 14,931 | - | - | 24,587 |
| One-to-four family - residential | 1,714 | 14,753 | - | - | 16,467 |
| Co-operative apartments | - | 164 | - | - | 164 |
| Construction loans | 1,916 | 5,425 | - | - | 7,341 |
| Small Business Administration | 336 | - | - | - | 336 |
| Commercial business and other | 2,000 | 5,939 | 50 | - | 7,989 |
| Total loans | 39,355 | 86,247 | 50 | - | 125,652 |
| | | | | | |
| Investment Securities: (1) | | | | | |
| Pooled trust preferred securities | - | 10,493 | - | - | 10,493 |
| Private issue trust preferred securities | - | 5,745 | - | - | 5,745 |
| Private issue CMO | - | 21,665 | - | - | 21,665 |
| Total investment securities | - | 37,903 | - | - | 37,903 |
| | | | | | |
| Other Real Estate Owned | - | 3,503 | - | - | 3,503 |
| Total | $ 39,355 | $ 127,653 | $ 50 | $ - | $ 167,058 |

The following table sets forth the Banks' assets designated as Criticized and Classified at December 31, 2012:

| (In thousands) | Special Mention | Substandard | Doubtful | Loss | Total |
|---|---|---|---|---|---|
| Loans: | | | | | |
| Multi-family residential | $ 16,345 | $ 22,769 | $ - | $ - | $ 39,114 |
| Commercial real estate | 11,097 | 27,877 | - | - | 38,974 |
| One-to-four family - mixed-use property | 13,104 | 26,506 | - | - | 39,610 |
| One-to-four family - residential | 5,223 | 15,328 | - | - | 20,551 |
| Co-operative apartments | 103 | 237 | - | - | 340 |
| Construction loans | 3,805 | 10,598 | - | - | 14,403 |
| Small Business Administration | 323 | 212 | 244 | - | 779 |
| Commercial business and other | 3,044 | 18,419 | 1,080 | - | 22,543 |
| Total loans | 53,044 | 121,946 | 1,324 | - | 176,314 |
| | | | | | |
| Investment Securities: (1) | | | | | |
| Pooled trust preferred securities | - | 10,419 | - | - | 10,419 |
| Private issue trust preferred securities | - | 5,770 | - | - | 5,770 |
| Private issue CMO | - | 26,429 | - | - | 26,429 |

| | | | | | |
|---|---|---|---|---|---|
| Total investment securities | - | 42,618 | - | - | 42,618 |
| | | | | | |
| Other Real Estate Owned | - | 5,278 | - | - | 5,278 |
| Total | $ 53,044 | $ 169,842 | $ 1,324 | $- | $224,210 |

(1) Our investment securities are classified as securities available for sale and as such are carried at their fair value in our Consolidated Financial Statements. The securities above had a fair value of $32.7 million and $35.2 million at September 30, 2013 and December 31, 2012, respectively. Under current applicable regulatory guidelines, we are required to disclose the classified investment securities, as shown in the tables above, at their book values (amortized cost, or fair value for securities that are under the fair value option). Additionally, the requirement is only for the Banks' securities. Flushing Financial Corporation had one private issue trust preferred security classified as Substandard with a market value of $0.3 million at September 30, 2013 and two private issue trust preferred securities classified as Substandard with a market value of $0.8 million at December 31, 2012.

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On a quarterly basis, all collateral dependent loans that are designated as Special Mention, Substandard or Doubtful are internally reviewed for impairment, based on updated cash flows for income producing properties or updated independent appraisals. The loan balances of collateral dependent impaired loans are then compared to the loans updated fair value. The balance which exceeds fair value is generally charged-off to the allowance for loan losses.

We designate investment securities as Substandard when the investment grade rating by one or more of the rating agencies is below investment grade. We have designated a total of nine investment securities that are held at the Bank as Substandard at September 30, 2013. Our classified investment securities at September 30, 2013 held by the Bank include five private issue CMOs rated below investment grade by one or more of the rating agencies, three issues of pooled trust preferred securities and one private issue trust preferred security. The Investment Securities which are classified as Substandard at September 30, 2013 are securities that were rated investment grade when we purchased them. These securities have each been subsequently downgraded by at least one rating agency to below investment grade. Through September 30, 2013, two of the pooled trust preferred securities and four private issue CMOs are not paying principal and interest as scheduled. We test each of these securities quarterly for impairment, through an independent third party.

ALLOWANCE FOR LOAN LOSSES

We have established and maintained on our books an allowance for loan losses that is designed to provide a reserve against estimated losses inherent in our overall loan portfolio. The allowance is established through a provision for loan losses based on management's evaluation of the risk inherent in the various components of the loan portfolio and other factors, including historical loan loss experience (which is updated quarterly), changes in the composition and volume of the portfolio, collection policies and experience, trends in the volume of non-accrual loans and local and national economic conditions. The determination of the amount of the allowance for loan losses includes estimates that are susceptible to significant changes due to changes in appraisal values of collateral, national and local economic conditions and other factors. We review our loan portfolio by separate categories with similar risk and collateral characteristics. Impaired loans are segregated and reviewed separately. All non-accrual loans and TDRs are considered impaired. Impaired loans secured by collateral are reviewed based on the fair value of their collateral. For non-collateralized impaired loans, management estimates any recoveries that are anticipated for each loan. In connection with the determination of the allowance, the market value of collateral ordinarily is evaluated by our staff appraiser. On a quarterly basis, the estimated values of impaired mortgage loans are internally reviewed, based on updated cash flows for income producing properties, and at times an updated independent appraisal is obtained. The loan balances of collateral dependent impaired loans are then compared to the property's updated fair value. We consider fair value of collateral dependent loans to be 85% of the appraised or internally estimated value of the property. The balance which exceeds fair value is generally charged-off. When evaluating a loan for impairment, we do not rely on guarantees, and the amount of impairment, if any, is based on the fair value of the collateral. We do not carry loans at a value in excess of the fair value due to a guarantee from the borrower. Impaired mortgage loans that were written down resulted from quarterly reviews or updated appraisals that indicated the properties' estimated value had declined from when the loan was originated. Current year charge-offs, charge-off trends, new loan production, current balance by particular loan categories, and delinquent loans by particular loan categories are also taken into account in determining the appropriate amount of allowance. The Board of Directors reviews and approves the adequacy of the allowance for loan losses on a quarterly basis.

In assessing the adequacy of the allowance, we review our loan portfolio by separate categories with similar risk and collateral characteristics, e.g., multi-family residential, commercial real estate, one-to-four family mixed-use property,

one-to-four family residential, co-operative apartment, construction, SBA, commercial business, taxi medallion and consumer loans. Impaired loans are segregated and reviewed separately. We do not carry loans at a value in excess of the fair value due to a guarantee from the borrower. Impaired mortgage loans that were written down resulted from quarterly reviews or updated appraisals that indicated the properties' estimated value had declined from when the loan was originated. Loans classified as TDR which are performing in accordance with their modified terms are evaluated based on the projected discounted cash flow of the restructured loan at the loans effective interest rate prior to restructuring. A portion of the allowance for loan losses is allocated in the amount by which the recorded investment in the TDR exceeds the discounted cash flow. For non-collateralized impaired loans, management estimates any recoveries that are anticipated for each loan. A portion of the allowance is allocated to non-collateralized loans based on these estimates. Based on the review of impaired loans, which includes loans classified as TDR, a portion of the allowance was allocated to impaired loans in the amount of $1.4 million and $1.5 million at September 30, 2013 and December 31, 2012, respectively.

General provisions are established against performing loans in our portfolio in amounts deemed prudent by management. A portion of the allowance is allocated to the remaining portfolio based on historical loss experience. The historical loss period used for this allocation was three years. Management also prepared an additional analysis to ensure that the remaining portion of the allowance for possible loan losses is sufficient to cover losses inherent in the loan portfolio. This analysis considered: (1) the current economic environment, (2) delinquency and non-accrual trends, (3) classified loan trends, (4) the risk inherent in our loan portfolio and volume and trends of loan types, (5) recent trends in charge-offs, (6) changes in underwriting standards, (7) the experience, ability and depth of our lenders, and (8) collection policies and experience. Based on these reviews, management concluded the general portion of the allowance should be $29.4 million and $29.6 million at September 30, 2013 and December 31, 2012, respectively, resulting in a total allowance of $30.8 million and $31.1 million at September 30, 2013 and December 31, 2012, respectively. The Board of Directors reviews and approves the adequacy of the allowance for loan losses on a quarterly basis. Management has concluded and the Board of Directors has concurred, that at September 30, 2013, the allowance was sufficient to absorb losses inherent in our loan portfolio.

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The following table sets forth the activity in the Company's allowance for loan losses for the periods indicated:

| (Dollars in thousands) | For the nine months ended September 30, 2013 | 2012 |
|---|---|---|
| Balance at beginning of period | $ 31,104 | $ 30,344 |
| Provision for loan losses | 12,935 | 16,000 |
| Loans charged-off: | | |
| Multi-family residential | (3,459) | (5,252) |
| Commercial real estate | (905) | (2,401) |
| One-to-four family – mixed-use property | (3,780) | (3,401) |
| One-to-four family – residential | (695) | (1,096) |
| Co-operative apartments | (74) | (62) |
| Construction | (2,678) | (2,500) |
| Small Business Administration | (426) | (324) |
| Commercial business and other | (2,057) | (1,488) |
| Total charge-offs | (14,074) | (16,524) |
| Recoveries: | | |
| Multi-family residential | 155 | 89 |
| Commercial real estate | 293 | 249 |
| One-to-four family – mixed-use property | 169 | 337 |
| One-to-four family – residential | 117 | 29 |
| Co-operative apartments | 4 | - |
| Small Business Administration | 77 | 59 |
| Commercial business and other | 36 | 104 |
| Total recoveries | 851 | 867 |
| Net charge-offs | (13,223) | (15,657) |
| Balance at end of period | $ 30,816 | $ 30,687 |
| Ratio of net charge-offs during the period to average loans outstanding during the period | 0.55 % | 0.65 % |
| Ratio of allowance for loan losses to gross loans at end of period | 0.91 % | 0.97 % |
| Ratio of allowance for loan losses to non-performing assets at end of period | 44.99 % | 28.56 % |
| Ratio of allowance for loan losses to non-performing loans at end of period | 50.39 % | 30.44 % |

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RECENT PROPOSED CHANGES TO REGULATORY CAPITAL RULES

During July 2013, the federal bank regulatory agencies issued revised notices of proposed rulemaking ("NPRs") that would revise and replace the agencies' current capital rules. The NPRs include numerous revisions to the existing capital regulations, including, but not limited to, the following:

- Revises the definition of regulatory capital components and related calculations.
- Adds a new common equity tier 1 capital ratio.
- Increases the minimum tier 1 capital ratio requirement from four percent to six percent.
- Incorporates the revised regulatory capital requirements into the Prompt Corrective Action framework.
- Implements a new capital conservation buffer that would limit payment of capital distributions and certain discretionary bonus payments to executive officers and key risk takers if the banking organization does not hold certain amounts of common equity tier 1 capital in addition to those needed to meet its minimum risk-based capital requirements.
- Provides a transition period for several aspects of the proposed rule: the new minimum capital ratio requirements, the capital conservation buffer, and the regulatory capital adjustments and deductions.
- Increases capital requirements for past-due loans, high volatility commercial real estate exposures, and certain short-term loan commitments.
- Removes references to credit ratings consistent with Section 939A of the Dodd-Frank Act.
- Establishes due diligence requirements for securitization exposures.

The capital regulations would be effective January 1, 2015 for bank holding companies and banks with less than $15 billion in total assets, such as our Company and Bank. Based on our preliminary assessment of the NPRs, we believe we will see an increase in our total risk-weighted assets. However, the Company and the Banks, based on our preliminary assessment, would meet the requirements of the NPRs and will continue to be considered well-capitalized.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

For a discussion of the qualitative and quantitative disclosures about market risk, see the information under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations - Interest Rate Risk."

## ITEM 4. CONTROLS AND PROCEDURES

The Company carried out, under the supervision and with the participation of the Company's management, including its Chief Executive Officer and Chief Financial Officer, an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this Quarterly Report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of September 30, 2013, the design and operation of these disclosure controls and procedures were effective. During the period covered by this Quarterly Report, there have been no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II – OTHER INFORMATION
FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

ITEM 1. LEGAL PROCEEDINGS

The Company is a defendant in various lawsuits. Management of the Company, after consultation with outside legal counsel, believes that the resolution of these various matters will not result in any material adverse effect on the Company's consolidated financial condition, results of operations and cash flows.

ITEM 1A. RISK FACTORS

There have been no material changes from the risk factors disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2012.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table sets forth information regarding the shares of common stock repurchased by the Company during the three months ended September 30, 2013:

| Period | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Number of Shares That May Yet Be Purchased Under the Plans or Programs |
|---|---|---|---|---|
| July 1 to July 31, 2013 | - | $ - | - | 579,870 |
| August 1 to August 31, 2013 | 10,000 | 18.01 | 10,000 | 569,870 |
| September 1 to September 30, 2013 | 20,000 | 18.17 | 20,000 | 549,870 |
| Total | 30,000 | $ 18.12 | 30,000 | |

During the three months ended June 30, 2013, the Company completed the common stock repurchase program that was approved by the Company's Board of Directors on September 20, 2011. On May 22, 2013, the Company announced the authorization by the Board of Directors of a new common stock repurchase program which authorizes the purchase of up to 1,000,000 shares of its common stock. The repurchase program does not have an expiration date or a maximum dollar amount that may be paid to repurchase the common shares. Stock repurchases under this program will be made from time to time, on the open market or in privately negotiated transactions, at the discretion of the management of the Company.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

PART II – OTHER INFORMATION

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

ITEM 6. EXHIBITS

| Exhibit No. | Description |
|---|---|
| 2.1 | Agreement and Plan of Merger dated as of December 20, 2005 by and between Flushing Financial Corporation and Atlantic Liberty Financial Corp. (7) |
| 3.1 | Certificate of Incorporation of Flushing Financial Corporation (1) |
| 3.2 | Certificate of Amendment to Certificate of Incorporation of Flushing Financial Corporation (3) |
| 3.3 | Certificate of Amendment to Certificate of Incorporation of Flushing Financial Corporation (6) |
| 3.4 | Certificate of Designations of Series A Junior Participating Preferred Stock of Flushing Financial Corporation (4) |
| 3.5 | Certificate of Increase of Shares Designated as Series A Junior Participating Preferred Stock of Flushing Financial Corporation (2) |
| 3.6 | By-Laws of Flushing Financial Corporation (1) |
| 4.1 | Rights Agreement, dated as of September 8, 2006, between Flushing Financial Corporation and Computershare Trust Company N.A., as Rights Agent, which includes the form of Certificate of Increase of Shares Designated as Series A Junior Participating Preferred Stock as Exhibit A, form of Right Certificate as Exhibit B and the Summary of Rights to Purchase Preferred Stock as Exhibit C (5) |
| 4.2 | Flushing Financial Corporation has outstanding certain long-term debt. None of such debt exceeds ten percent of Flushing Financial Corporation's total assets; therefore, copies of constituent instruments defining the rights of the holders of such debt are not included as exhibits. Copies of instruments with respect to such long-term debt will be furnished to the Securities and Exchange Commission upon request. |
| 31.1 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Chief Executive Officer (filed herewith) |
| 31.2 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Chief Financial Officer (filed herewith) |
| 32.1 | Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002 by the Chief Executive Officer (furnished herewith) |
| 32.2 | Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002 by the Chief Financial Officer (furnished herewith) |
| 101.INS | XBRL Instance Document (filed herewith) |
| 101.SCH | XBRL Taxonomy Extension Schema Document (filed herewith) |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document (filed herewith) |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document (filed herewith) |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document (filed herewith) |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document (filed herewith) |

(1) Incorporated by reference to Exhibits filed with the Registration Statement on Form S-1 filed September 1, 1995, Registration No. 33-96488.
(2) Incorporated by reference to Exhibits filed with Form 8-K filed September 26, 2006.
(3) Incorporated by reference to Exhibits filed with Form S-8 filed May 31, 2002.
(4) Incorporated by reference to Exhibits filed with Form 10-Q for the quarter ended September 30, 2002.
(5) Incorporated by reference to Exhibit filed with Form 8-K filed September 11, 2006.
(6) Incorporated by reference to Exhibit filed with Form 10-K filed March 15, 2012.
(7) Incorporated by reference to Exhibit filed with Form 8-K filed December 23, 2005.

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FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Flushing Financial Corporation,

Dated: November 12, 2013

By: /s/John R. Buran
John R. Buran
President and Chief Executive Officer

Dated: November 12, 2013

By: /s/David W. Fry
David W. Fry
Executive Vice President, Treasurer and
Chief Financial Officer

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
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