

FULTON FINANCIAL CORP

Form 10-Q

November 10, 2008

Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20459
FORM 10-Q**

(Mark One)

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

For the quarterly period ended **September 30, 2008**, or

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

For the transition period from _____ to _____

Commission File No. **0-10587**

FULTON FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

PENNSYLVANIA

23-2195389

(State or other jurisdiction of incorporation or organization)

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

One Penn Square, P.O. Box 4887 Lancaster,
Pennsylvania

17604

(Address of principal executive offices)

(Zip Code)

(717) 291-2411

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant 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 Accelerated filer Non-accelerated filer Smaller reporting company

(Do not check if a smaller reporting company)

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

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

Common Stock, \$2.50 Par Value 174,981,000 shares outstanding as of October 31, 2008.

FULTON FINANCIAL CORPORATION
FORM 10-Q FOR THE QUARTER ENDED SEPTEMBER 30, 2008
INDEX

Description	Page
PART I. FINANCIAL INFORMATION	
<u>Item 1. Financial Statements (Unaudited):</u>	
<u>(a) Consolidated Balance Sheets September 30, 2008 and December 31, 2007</u>	3
<u>(b) Consolidated Statements of Income Three and nine months ended September 30, 2008 and 2007</u>	4
<u>(c) Consolidated Statements of Shareholders Equity and Comprehensive Income Nine months ended September 30, 2008 and 2007</u>	5
<u>(d) Consolidated Statements of Cash Flows Nine months ended September 30, 2008 and 2007</u>	6
<u>(e) Notes to Consolidated Financial Statements</u>	7
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	23
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	48
<u>Item 4. Controls and Procedures</u>	54
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	55
<u>Item 1A. Risk Factors</u>	55
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	56
<u>Item 3. Defaults Upon Senior Securities</u>	56
<u>Item 4. Submission of Matters to a Vote of Security Holders</u>	57
<u>Item 5. Other Information</u>	57
<u>Item 6. Exhibits</u>	57
<u>Signatures</u>	58
<u>Exhibit Index</u>	59
<u>Certifications</u>	60
<u>EXHIBIT 31.1</u>	

EXHIBIT 31.2

EXHIBIT 32.1

EXHIBIT 32.2

Table of Contents**Item 1. Financial Statements****FULTON FINANCIAL CORPORATION
CONSOLIDATED BALANCE SHEETS**

(in thousands, except per-share data)

	September 30 2008 (unaudited)	December 31 2007
ASSETS		
Cash and due from banks	\$ 315,841	\$ 381,283
Interest-bearing deposits with other banks	11,819	11,330
Federal funds sold	38,370	9,823
Loans held for sale	71,090	103,984
Investment securities:		
Held to maturity (estimated fair value of \$9,926 in 2008 and \$10,399 in 2007)	9,823	10,285
Available for sale	2,796,712	3,143,267
Loans, net of unearned income	11,823,529	11,204,424
Less: Allowance for loan losses	(136,988)	(107,547)
<i>Net Loans</i>	11,686,541	11,096,877
Premises and equipment	199,464	193,296
Accrued interest receivable	62,018	73,435
Goodwill	624,410	624,072
Intangible assets	25,225	30,836
Other assets	294,832	244,610
<i>Total Assets</i>	\$ 16,136,145	\$ 15,923,098
LIABILITIES		
Deposits:		
Noninterest-bearing	\$ 1,690,499	\$ 1,722,211
Interest-bearing	8,226,056	8,383,234
<i>Total Deposits</i>	9,916,555	10,105,445
Short-term borrowings:		
Federal funds purchased	1,326,873	1,057,335
Other short-term borrowings	1,263,093	1,326,609
<i>Total Short-Term Borrowings</i>	2,589,966	2,383,944
Accrued interest payable	47,950	69,238

Other liabilities	157,875	147,418
Federal Home Loan Bank advances and long-term debt	1,819,889	1,642,133
<i>Total Liabilities</i>	14,532,235	14,348,178
 SHAREHOLDERS EQUITY		
Common stock, \$2.50 par value, 600 million shares authorized, 192.3 million shares issued in 2008 and 191.8 million shares issued in 2007	480,810	479,559
Additional paid-in capital	1,253,851	1,254,369
Retained earnings	159,320	141,993
Accumulated other comprehensive loss	(21,262)	(21,773)
Treasury stock, 17.6 million shares in 2008 and 18.3 million shares in 2007, at cost	(268,809)	(279,228)
<i>Total Shareholders Equity</i>	1,603,910	1,574,920
<i>Total Liabilities and Shareholders Equity</i>	\$ 16,136,145	\$ 15,923,098

See Notes to Consolidated Financial Statements

Table of Contents

FULTON FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)
(in thousands, except per-share data)

	Three Months Ended September 30		Nine Months Ended September 30	
	2008	2007	2008	2007
INTEREST INCOME				
Loans, including fees	\$ 180,170	\$ 204,580	\$ 550,477	\$ 598,130
Investment securities:				
Taxable	26,025	24,583	84,114	71,201
Tax-exempt	4,513	4,388	13,540	13,069
Dividends	1,421	2,063	5,103	5,998
Loans held for sale	1,539	2,694	4,727	9,771
Other interest income	141	432	460	1,339
<i>Total Interest Income</i>	213,809	238,740	658,421	699,508
INTEREST EXPENSE				
Deposits	47,192	76,403	161,807	221,410
Short-term borrowings	12,877	17,786	44,093	51,734
Long-term debt	19,722	22,141	60,714	61,271
<i>Total Interest Expense</i>	79,791	116,330	266,614	334,415
<i>Net Interest Income</i>	134,018	122,410	391,807	365,093
Provision for loan losses	26,700	4,606	54,626	8,263
<i>Net Interest Income After Provision for Loan Losses</i>	107,318	117,804	337,181	356,830
OTHER INCOME				
Service charges on deposit accounts	16,177	11,293	45,463	33,145
Other service charges and fees	9,598	8,530	27,320	23,746
Investment management and trust services	8,045	9,291	25,193	29,374
Gains on sales of mortgage loans	2,266	2,532	7,247	12,113
Gain on sale of credit card portfolio			13,910	
Investment securities (losses) gains	(9,501)	(134)	(29,902)	2,277
Other	4,030	5,231	11,214	12,158
<i>Total Other Income</i>	30,615	36,743	100,445	112,813
OTHER EXPENSES				
Salaries and employee benefits	55,310	52,505	164,786	164,353
Net occupancy expense	10,237	9,813	30,999	29,963
Operating risk loss	3,480	16,345	19,108	26,462

Edgar Filing: FULTON FINANCIAL CORP - Form 10-Q

Data processing	3,242	3,131	9,604	9,550
Advertising	3,097	2,470	9,521	7,869
Equipment expense	3,061	3,438	9,907	10,589
Intangible amortization	1,730	1,995	5,386	6,176
Other	18,998	18,299	56,240	52,046
<i>Total Other Expenses</i>	99,155	107,996	305,551	307,008
<i>Income Before Income Taxes</i>	38,778	46,551	132,075	162,635
Income taxes	9,702	12,985	35,825	48,096
<i>Net Income</i>	\$ 29,076	\$ 33,566	\$ 96,250	\$ 114,539
PER-SHARE DATA:				
Net income (basic)	\$ 0.17	\$ 0.19	\$ 0.55	\$ 0.66
Net income (diluted)	0.17	0.19	0.55	0.66
Cash dividends	0.150	0.150	0.450	0.448

See Notes to Consolidated Financial Statements

Table of Contents

FULTON FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME
(UNAUDITED)
NINE MONTHS ENDED SEPTEMBER 30, 2008 AND 2007
(in thousands)

	Number of Shares Outstanding	Common Stock	Additional Paid-in Capital	Accumulated			Total
				Retained Earnings	Other Comprehensive Income (Loss)	Treasury Stock	
Balance at December 31, 2007	173,503	\$ 479,559	\$ 1,254,369	\$ 141,993	\$ (21,773)	\$ (279,228)	\$ 1,574,920
Comprehensive income:							
Net income				96,250			96,250
Other comprehensive income					511		511
<i>Total comprehensive income</i>							96,761
Stock issued, including related tax benefits	1,184	1,251	(2,189)			10,419	9,481
Stock-based compensation awards			1,671				1,671
Impact of pension plan measurement date change (net of \$23,000 tax effect)				43			43
Cumulative effect of EITF 06-4 adoption				(677)			(677)
Cash dividends \$0.450 per share				(78,289)			(78,289)
Balance at September 30, 2008	174,687	\$ 480,810	\$ 1,253,851	\$ 159,320	\$ (21,262)	\$ (268,809)	\$ 1,603,910
Balance at December 31, 2006	173,648	\$ 476,987	\$ 1,246,823	\$ 92,592	\$ (39,091)	\$ (261,001)	\$ 1,516,310

Comprehensive income:								
Net income				114,539				114,539
Other comprehensive income					10,046			10,046
<i>Total comprehensive income</i>								124,585
Stock issued, including related tax benefits	920	2,298	4,383					6,681
Stock-based compensation awards			2,069					2,069
Cumulative effect of FIN 48 adoption				220				220
Acquisition of treasury stock	(1,174)					(18,227)		(18,227)
Cash dividends \$0.448 per share				(77,518)				(77,518)
Balance at September 30, 2007	173,394	\$ 479,285	\$ 1,253,275	\$ 129,833	\$ (29,045)	\$ (279,228)		\$ 1,554,120

See Notes to Consolidated Financial Statements

Table of Contents

FULTON FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(in thousands)

	Nine Months Ended	
	September 30	
	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	\$ 96,250	\$ 114,539
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	54,626	8,263
Depreciation and amortization of premises and equipment	14,776	14,801
Net amortization of investment security premiums	372	1,726
Gain on sale of credit card portfolio	(13,910)	
Investment securities losses (gains)	29,902	(2,277)
Net decrease in loans held for sale	17,396	92,314
Amortization of intangible assets	5,386	6,176
Stock-based compensation expense	1,671	2,069
Excess tax benefits from stock-based compensation expense	(20)	(111)
Decrease (increase) in accrued interest receivable	11,417	(2,102)
(Increase) decrease in other assets	(12,274)	8,940
(Decrease) increase in accrued interest payable	(21,288)	9,373
Decrease in other liabilities	(17,279)	(10,858)
Total adjustments	70,775	128,314
<i>Net cash provided by operating activities</i>	167,025	242,853
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sales of securities available for sale	662,993	314,979
Proceeds from maturities of securities held to maturity	5,273	2,774
Proceeds from maturities of securities available for sale	546,407	366,308
Proceeds from sale of credit card portfolio	100,516	
Purchase of securities held to maturity	(4,813)	(1,986)
Purchase of securities available for sale	(903,817)	(739,377)
(Increase) decrease in short-term investments	(29,036)	8,515
Net increase in loans	(715,219)	(589,419)
Net purchases of premises and equipment	(20,944)	(13,492)
<i>Net cash used in investing activities</i>	(358,640)	(651,698)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net decrease in demand and savings deposits	(21,071)	(171,584)
Net (decrease) increase in time deposits	(167,819)	230,301
Additions to long-term debt	344,690	723,633
Repayments of long-term debt	(166,934)	(394,801)
Increase in short-term borrowings	206,022	92,243

Dividends paid	(78,196)	(77,113)
Net proceeds from issuance of stock	9,461	6,570
Excess tax benefits from stock-based compensation expense	20	111
Acquisition of treasury stock		(18,227)
<i>Net cash provided by financing activities</i>	126,173	391,133
Net Decrease in Cash and Due From Banks	(65,442)	(17,712)
Cash and Due From Banks at Beginning of Year	381,283	355,018
Cash and Due From Banks at End of Year	\$ 315,841	\$ 337,306
Supplemental Disclosures of Cash Flow Information		
Cash paid during the period for:		
Interest	\$ 287,902	\$ 325,042
Income taxes	67,264	52,355
<i>See Notes to Consolidated Financial Statements</i>		

Table of Contents**FULTON FINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)****NOTE A Basis of Presentation**

The accompanying unaudited consolidated financial statements of Fulton Financial Corporation (the Corporation) have been prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and notes required by U.S. GAAP for complete financial statements. The preparation of financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the amounts of assets and liabilities as of the date of the financial statements as well as revenues and expenses during the period. Actual results could differ from those estimates. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine-month periods ended September 30, 2008 are not necessarily indicative of the results that may be expected for the year ending December 31, 2008.

NOTE B Net Income Per Share and Comprehensive Income

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

A reconciliation of the weighted average shares outstanding used to calculate basic net income per share and diluted net income per share follows:

	Three months ended		Nine months ended	
	September 30		September 30	
	2008	2007	2008	2007
	(in thousands)			
Weighted average shares outstanding (basic)	174,463	173,304	174,017	173,254
Impact of common stock equivalents	449	1,066	534	1,239
Weighted average shares outstanding (diluted)	174,912	174,370	174,551	174,493
Stock options excluded from the earnings per share computation as their effect would have been anti-dilutive	5,560	4,429	5,261	3,988

Table of Contents

The following table presents the components of other comprehensive income (loss):

	Nine months ended September 30	
	2008	2007
	(in thousands)	
Unrealized (loss) gain on securities (net of \$11.9 million and \$1.3 million tax effect in 2008 and 2007, respectively)	\$ (22,118)	\$ 2,416
Unrealized gain (loss) on derivative financial instruments (net of \$55,000 and \$29,000 tax effect in 2008 and 2007, respectively)	102	(53)
Reclassification adjustment for securities losses (gains) included in net income (net of \$12.1 million tax benefit in 2008 and \$797,000 tax expense in 2007)	22,527	(1,480)
Defined benefit pension plan curtailment (net of \$4.9 million tax effect in 2007)		9,122
Amortization of unrecognized pension and postretirement costs (net of \$22,000 tax effect in 2007)		41
Other comprehensive income	\$ 511	\$ 10,046

NOTE C INVESTMENT SECURITIES

The following tables present the amortized cost and estimated fair values of investment securities:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(in thousands)			
Held to Maturity at September 30, 2008				
U.S. Government sponsored agency securities	\$ 6,720	\$ 22	\$	\$ 6,742
State and municipal securities	912	4		916
Corporate debt securities	25			25
Mortgage-backed securities	2,166	77		2,243
	\$ 9,823	\$ 103	\$	\$ 9,926
Available for Sale at September 30, 2008				
Equity securities	\$ 171,944	\$ 4,842	\$ (5,737)	\$ 171,049
U.S. Government securities	14,585	59		14,644
U.S. Government sponsored agency securities	76,952	1,632	(10)	78,574
State and municipal securities	519,718	1,681	(9,520)	511,879
Corporate debt securities	173,057	681	(41,855)	131,883
Collateralized mortgage obligations	521,489	15,358	(107)	536,740
Mortgage-backed securities	1,191,267	10,755	(3,160)	1,198,862
Auction rate securities (1)	157,011		(3,930)	153,081
	\$ 2,826,023	\$ 35,008	\$ (64,319)	\$ 2,796,712

(1) See Note I,
Commitments

and
Contingencies
for additional
details related to
auction rate
securities.

Table of Contents

Held to Maturity at December 31, 2007	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
		(in thousands)		
U.S. Government sponsored agency securities	\$ 6,478	\$ 33	\$	\$ 6,511
State and municipal securities	1,120	7		1,127
Corporate debt securities	25			25
Mortgage-backed securities	2,662	74		2,736
	\$ 10,285	\$ 114	\$	\$ 10,399

Available for Sale at December 31, 2007

Equity securities	\$ 215,177	\$ 282	\$ (23,734)	\$ 191,725
U.S. Government securities	14,489	47		14,536
U.S. Government sponsored agency securities	200,899	1,658	(34)	202,523
State and municipal securities	520,670	2,488	(1,620)	521,538
Corporate debt securities	172,907	1,259	(8,184)	165,982
Collateralized mortgage obligations	588,848	6,604	(677)	594,775
Mortgage-backed securities	1,460,219	6,167	(14,198)	1,452,188
	\$ 3,173,209	\$ 18,505	\$ (48,447)	\$ 3,143,267

The following table presents the gross unrealized losses and estimated fair values of investments, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at September 30, 2008:

	Less Than 12 months		12 Months or Longer		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
			(in thousands)			
U.S. Government sponsored agency securities	\$ 1,344	\$ (1)	\$ 528	\$ (9)	\$ 1,872	\$ (10)
State and municipal securities	198,135	(9,497)	3,587	(23)	201,722	(9,520)
Corporate debt securities	87,817	(29,246)	28,596	(12,609)	116,413	(41,855)
Collateralized mortgage obligations	24,099	(107)	10		24,109	(107)
Mortgage-backed securities	324,071	(2,000)	99,041	(1,160)	423,112	(3,160)
Auction rate securities (1)	152,986	(3,930)			152,986	(3,930)
Total debt securities	788,452	(44,781)	131,762	(13,801)	920,214	(58,582)
Equity securities	23,690	(4,674)	4,010	(1,063)	27,700	(5,737)

\$ 812,142 \$ (49,455) \$ 135,772 \$ (14,864) \$ 947,914 \$ (64,319)

- (1) See Note I,
Commitments
and
Contingencies
for additional
details related to
auction rate
securities.

As of September 30, 2008, the unrealized losses on the Corporation's investments in corporate debt securities were caused by decreases in the estimated fair values of investments in single-issuer and pooled trust preferred securities and subordinated debt issued by financial institutions. The unrealized losses on mortgage-backed securities and collateralized mortgage obligations were the result of increases in U.S. Treasury yields at terms that were consistent with the terms of the investments held by the Corporation. The unrealized losses on equity securities in the above table were due to decreases in the values of stocks of financial institutions.

Table of Contents

The Corporation evaluates whether unrealized losses on investment securities indicate other-than-temporary impairment. Based upon this evaluation, losses of \$10.7 million and \$39.3 million were recognized during the three and nine months ended September 30, 2008, respectively, for the other-than-temporary impairment of investment securities.

The following table presents other-than-temporary impairment charges, included within Investment securities (losses) gains on the consolidated statements of income, by investment security type:

	September 30, 2008	
	Three months ended	Nine months ended
	(in thousands)	
Financial institution stocks	\$ 2,021	\$ 30,250
Government sponsored agency stock	356	356
Mutual funds	460	820
Total Equity securities charges	2,837	31,426
Bank-issued subordinated debt	4,855	4,855
Pooled trust preferred security	2,990	2,990
Total Debt securities charges	7,845	7,845
Total other-than-temporary impairment charges	\$ 10,682	\$ 39,271

During the three and nine months ended September 30, 2007, the Corporation recognized losses of \$117,000 for the other-than-temporary impairment of financial institutions stocks. There were no other-than-temporary impairment charges recorded for debt securities during the three and nine months ended September 30, 2007.

Beginning in 2007 and continuing through the third quarter of 2008, the values of financial institution stocks, including those held by the Corporation, declined significantly. The other-than-temporary impairment charges of \$2.0 million and \$30.3 million for the three and nine months ended September 30, 2008 were due to the increasing severity and duration of the decline in fair values of the stocks written down. These factors, in conjunction with management's evaluation of the near-term prospects of each specific issuer, resulted in the charges recognized during the current year. As of September 30, 2008, after other-than-temporary impairment charges, the financial institution stock portfolio had a cost basis of \$55.2 million and a fair value of \$54.3 million.

In addition to financial institution stocks, the Corporation recorded other-than-temporary impairment charges on other equity securities of \$816,000 and \$1.2 million for the three and nine months ended September 30, 2008. The charges included a write-down for the Corporation's entire investment in the stock of government sponsored agencies.

As noted above, the unrealized losses on the Corporation's investments in debt securities were caused by decreases in the estimated fair values of investments in single-issuer and pooled trust preferred securities and subordinated debt securities issued by financial institutions. As with equity securities issued by financial institutions, the estimated fair value of debt securities issued by financial institutions has also declined significantly during 2008. The \$4.9 million other-than-temporary impairment charge for bank-issued subordinated debt was related to an investment in a financial institution which failed during the third quarter of 2008. The \$3.0 million other-than-temporary impairment charge for a pooled trust preferred security was due to management's assessment that the expected cash flows from this investment would not exceed its amortized cost.

Table of Contents

The following table presents the amortized cost and estimated fair values of corporate debt securities issued by financial institutions:

	September 30, 2008		December 31, 2007	
	Amortized cost	Estimated fair value (in thousands)	Amortized cost	Estimated fair value
Single-issuer trust preferred securities (1)	\$ 97,870	\$ 74,512	\$ 96,781	\$ 92,515
Subordinated debt	40,009	31,666	37,886	36,760
Pooled trust preferred securities	32,220	22,749	35,271	33,743
Total corporate debt securities issued by financial institutions	\$ 170,099	\$ 128,927	\$ 169,938	\$ 163,018

(1) Single-issuer trust preferred securities with estimated fair values totaling \$8.9 million as of September 30, 2008 are classified as Level 3 assets. See Note J, Fair Value Measurements for additional details.

Based on management's other-than-temporary impairment evaluations and the Corporation's ability and intent to hold these investments for a reasonable period of time sufficient for a recovery of fair value, the Corporation does not consider these investments to be other-than-temporarily impaired as of September 30, 2008.

In relation to the Corporation's investments in mortgage-backed securities and collateralized mortgage obligations, the contractual terms of those investments generally do not permit the issuer to settle the securities at a price less than the amortized cost of the investment. Because the decline in market value for mortgage-backed securities and collateralized mortgage obligations held by the Corporation are attributable to changes in interest rates and not credit quality, and because the Corporation has the ability and intent to hold those investments until a recovery of fair value, which may be maturity, the Corporation does not consider those investments to be other-than-temporarily impaired at September 30, 2008.

NOTE D Sale of Credit Card Portfolio

In April 2008, the Corporation sold its approximately \$87.0 million credit card portfolio to U.S. Bank National Association ND, d/b/a Elan Financial Services (Elan). As a result of this sale, the Corporation recorded a \$13.9 million gain.

Under a separate agreement with Elan, the Corporation provides ongoing marketing services on behalf of Elan and receives fee income for each new account originated and a percentage of the revenue earned on both new accounts and accounts sold. During the three and nine months ended September 30, 2008, the Corporation recorded \$1.3 million

and \$2.4 million, respectively, of credit card fee income, included within other income on the consolidated statements of income, in connection with this agreement.

NOTE E Income Taxes

In accordance with Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48), the Corporation maintains a reserve for unrecognized income tax positions as a component of other liabilities. Upon adoption of FIN 48 on January 1, 2007, the Corporation recorded a \$220,000 decrease in existing reserves for unrecognized income tax positions, with a cumulative effect adjustment for the same amount recorded to retained earnings.

As of September 30, 2008 and 2007, the Corporation had total reserves for unrecognized income tax positions of \$2.8 million and \$4.1 million, respectively, all of which, if recognized, would impact the effective tax rate. Also as of September 30, 2008 and 2007, the Corporation had \$807,000 and \$1.4 million,

Table of Contents

respectively, in accrued interest payable related to such unrecognized positions. The Corporation recognizes interest accrued related to unrecognized income tax positions as a component of income tax expense. Penalties, if incurred, would also be recognized in income tax expense.

In March 2008, the Corporation reversed \$2.0 million of its reserves for unrecognized income tax positions, resulting in a reduction of income tax expense. The Corporation had not fully recognized in the consolidated financial statements the positions it had taken on its tax returns for disallowed interest expense on certain tax-exempt municipal securities. In the fourth quarter of 2007, a court ruled in favor of a taxpayer who had taken a similar position on its tax returns. In March 2008, the Internal Revenue Service indicated that it would not pursue an appeal of this ruling. As a result, the criteria for remeasurement of this tax position were reached.

The Corporation, or one of its subsidiaries, files income tax returns in the U.S. Federal jurisdiction, and various states. In many cases, unrecognized income tax positions are related to tax years that remain subject to examination by the relevant taxing authorities. With few exceptions, the Corporation is no longer subject to U.S. Federal, state and local examinations by tax authorities for years before 2005.

NOTE F Stock-Based Compensation

As required by Statement of Financial Accounting Standards No. 123R, *Share-Based Payment*, the fair value of equity awards to employees is recognized as compensation expense over the period during which employees are required to provide service in exchange for such awards. The Corporation's equity awards consist of stock options and restricted stock granted under its Stock Option and Compensation Plans (Option Plans) and shares purchased by employees under its Employee Stock Purchase Plan.

The following table presents compensation expense and the related tax benefits for equity awards recognized in the consolidated statements of income:

	Three months ended		Nine months ended	
	September 30		September 30	
	2008	2007	2008	2007
	(in thousands)			
Stock-based compensation expense	\$ 606	\$ 811	\$ 1,671	\$ 2,069
Tax benefit	(108)	(130)	(234)	(310)
Stock-based compensation expense, net of tax	\$ 498	\$ 681	\$ 1,437	\$ 1,759

Under the Option Plans, stock options and restricted stock are granted to key employees at option prices equal to the fair market value of the Corporation's stock on the date of grant, with stock options having terms of up to ten years. Stock options and restricted stock are typically granted annually on July 1st and become fully vested after a three-year vesting period. Certain events, as specified in the Option Plans and agreements, would result in the acceleration of the vesting period. As of September 30, 2008, there were 13.6 million shares reserved for future grants through 2013. On July 1, 2008, the Corporation granted approximately 358,000 stock options and 45,000 shares of restricted stock under its Option Plans.

NOTE G Employee Benefit Plans

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

Table of Contents

On April 30, 2007, the Corporation amended the Pension Plan to discontinue the accrual of benefits for all existing participants, effective January 1, 2008. As a result of this amendment, the Corporation recorded a \$58,000 curtailment loss, as determined by consulting actuaries, during the second quarter of 2007. The curtailment loss resulted from a \$13.8 million gain from adjusting the funded status of the Pension Plan and an offsetting \$13.9 million write-off of unamortized pension costs and related deferred tax assets.

The Corporation currently provides medical and life insurance benefits under a postretirement benefits plan (Postretirement Plan) to certain retired full-time employees who were employees of the Corporation prior to January 1, 1998. Certain full-time employees may become eligible for these discretionary benefits if they reach retirement age while working for the Corporation. Benefits are based on a graduated scale for years of service after attaining the age of 40.

As required by Statement of Financial Accounting Standards No. 158, Employers Accounting for Defined Benefit Pension and Postretirement Plans (Statement 158), the Corporation recognizes the funded status of its Pension Plan and Postretirement Plan on the consolidated balance sheets and recognizes the changes in that funded status through other comprehensive income.

Effective January 1, 2008, as required by Statement 158, the Corporation changed the actuarial measurement date for its Pension Plan from a fiscal year-end of September 30th to December 31st. The impact of this change in the actuarial measurement date resulted in a \$66,000 increase to the Corporation's prepaid pension asset and a cumulative effect adjustment, net of tax, of \$43,000 recorded as an increase to retained earnings.

The net periodic benefit cost for the Corporation's Pension Plan and Postretirement Plan, as determined by consulting actuaries, consisted of the following components for the three and nine-month periods ended September 30:

	Pension Plan			
	Three months		Nine months ended	
	ended		September 30	
	September 30	2007	2008	2007
	2008		2008	
	(in thousands)			
Service cost (1)	\$ 36	\$ 394	\$ 110	\$ 1,508
Interest cost	816	769	2,448	2,515
Expected return on plan assets	(918)	(901)	(2,754)	(3,018)
Net amortization and deferral				233
Curtailment loss				58
Net periodic benefit (income) cost	\$ (66)	\$ 262	\$ (196)	\$ 1,296

(1) The Pension Plan service cost recorded for the three and nine months ended September 30, 2008 was related to administrative costs associated with the plan and not due to

the accrual of
additional
participant
benefits.

	Postretirement Plan			
	Three months ended		Nine months ended	
	September 30		September 30	
	2008	2007	2008	2007
	(in thousands)			
Service cost	\$ 132	\$ 138	\$ 390	\$ 367
Interest cost	184	182	538	483
Expected return on plan assets	(1)	(2)	(4)	(4)
Net amortization and deferral		(57)		(170)
Net periodic benefit cost	\$ 315	\$ 261	\$ 924	\$ 676

Table of Contents

In September 2006, the FASB ratified Emerging Issues Task Force (EITF) Issue 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements* (EITF 06-4). EITF 06-4 addresses accounting for endorsement split-dollar life insurance arrangements that provide a benefit to an employee that extends to postretirement periods. EITF 06-4 requires that the postretirement benefit aspects of an endorsement-type split-dollar life insurance arrangement be recognized as a liability by the employer if that obligation has not been settled through the related insurance arrangement.

The Corporation adopted the provisions of EITF 06-4 on January 1, 2008 and recorded a \$677,000 liability, with a cumulative effect adjustment for the same amount recorded as a reduction to retained earnings. The amount represents the actuarial cost of maintaining endorsement split-dollar life insurance policies for certain employees which have not been effectively settled through their related insurance arrangements.

NOTE H Derivative Financial Instruments**Interest Rate Swaps**

As of September 30, 2008, interest rate swaps with a notional amount of \$18.0 million were used to hedge certain long-term fixed rate certificates of deposit. The terms of the certificates of deposit and the interest rate swaps are similar and were committed to simultaneously. Under the terms of the swap agreements, the Corporation is the fixed rate receiver and the floating rate payer (generally tied to the three-month London Interbank Offering Rate, or LIBOR, a common index used for setting rates between financial institutions). The interest rate swaps and the certificates of deposit are recorded at fair value, with changes in the fair values during the period recorded to other expense. For the three and nine months ended September 30, 2008, the net impact of the change in fair values of the interest rate swaps and the certificates of deposit was insignificant. For the three and nine months ended September 30, 2007, the net impact of the change in fair values of the interest rate swaps and certificates of deposit, recorded in other expenses, were \$10,000 and \$251,000, respectively.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* (Statement 159). Statement 159 permits entities to choose to measure many financial instruments and certain other items at fair value and amends Statement 115 to, among other things, require certain disclosures for amounts for which the fair value option is applied. Statement 159 became effective on January 1, 2008 and the Corporation adopted the provisions of Statement 159 for the interest rate swaps and the related certificates of deposit.

Prior to the adoption of Statement 159, the Corporation accounted for these interest rate swaps and the related certificates of deposit under Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities* (Statement 133). Under Statement 133, the Corporation performed tests for each swap to prove they were highly effective. The adoption of Statement 159 for these instruments did not result in a change in the reported values of the interest rate swaps or certificates of deposit on the Corporation's consolidated balance sheets. However, the administrative burden of completing these periodic effectiveness tests was removed, as such tests are not required under Statement 159.

The Corporation did not adopt the provisions of Statement 159 for any other financial assets or liabilities on its consolidated balance sheets.

Forward Starting Interest Rate Swaps

In prior years, the Corporation had entered into forward-starting interest rate swaps in anticipation of the issuance of fixed-rate debt. In October 2005, the Corporation entered into a forward-starting interest rate swap with a notional amount of \$150.0 million in anticipation of the issuance of trust preferred securities in January 2006. In February 2007, the Corporation entered into a forward-starting interest rate swap with a notional amount of \$100.0 million in anticipation of the issuance of subordinated debt in May 2007.

Table of Contents

These swaps were accounted for as cash flow hedges as they hedged the variability of interest payments attributable to changes in interest rates on the forecasted issuances of fixed-rate debt. The total amounts recorded in accumulated other comprehensive income upon settlement of these derivatives are being amortized to interest expense over the lives of the related securities using the effective interest method. The amount of net losses in accumulated other comprehensive income that will be reclassified into earnings during the next twelve months is approximately \$135,000.

NOTE I Commitments and Contingencies**Commitments**

The Corporation is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. Those financial instruments include commitments to extend credit and letters of credit, which involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized on the Corporation's consolidated balance sheets. Exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and letters of credit is represented by the outstanding amount of those instruments.

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

	September 30	
	2008	2007
	(in thousands)	
Commitments to extend credit	\$ 3,810,535	\$ 4,430,940
Standby letters of credit	778,811	727,171
Commercial letters of credit	35,605	26,208

As of September 30, 2008, the reserve for unfunded lending commitments, included in other liabilities on the consolidated balance sheets, was \$4.8 million. Prior to December 31, 2007, the reserve for unfunded lending commitments was included as a component of the allowance for loan losses. As of December 31, 2007, the Corporation reclassified the reserve for unfunded lending commitments to other liabilities. Prior periods were not reclassified.

Auction Rate Securities

During 2008, developments in the market for student loan auction rate securities, also known as auction rate certificates (ARCs), resulted in the Corporation recording charges of \$2.7 million and \$15.9 million for the three and nine months ended September 30, 2008, respectively.

The Corporation's trust company subsidiary, Fulton Financial Advisors, N.A. (FFA), holds ARCs for some of its customers' accounts. ARCs are one of several types of securities that were previously utilized by FFA as short-term investment vehicles for its customers. ARCs are long-term securities structured to allow their sale in periodic auctions, giving the securities some of the characteristics of short-term instruments in normal market conditions. However, in mid-February, 2008, market auctions for ARCs began to fail due to an insufficient number of buyers; these market failures were the first widespread and continuing failures in the over 20-year history of the auction rate securities markets. As a result, although the credit quality of ARCs has not been impacted, ARCs are currently not liquid investments for their holders, including FFA's customers. It is unclear when liquidity will return to this market. FFA has agreed to purchase ARCs from customer accounts upon notification from customers that they have liquidity needs or otherwise desire to liquidate their holdings. FFA will generally purchase customer ARCs at par value with an interest adjustment, which would position customers as if they had owned 90-day U.S. Treasury bills instead of ARCs. The guarantee was recorded as a liability in accordance with FASB Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including

Table of Contents

Indirect Guarantees of Indebtedness of Others an interpretation of FASB Statements No. 5, 57, and 107 and rescission of FASB Interpretation No. 34, and carried at estimated fair value with a corresponding pre-tax charge to earnings both upon the initial establishment of the guarantee and upon changes in its estimated fair value. The estimated fair value of the guarantee was determined based on the difference between the fair value of the underlying ARCs, assuming that all ARCs held in customer accounts would be purchased, and their estimated purchase price. The Corporation determined the fair value of the ARCs held by customers based on independent third-party valuations. See Note J, Fair Value Measurements for additional details related to the Corporation's determination of fair value. The following table presents the change in the ARC investment balances held by customers and the related financial guarantee liability, recorded within other liabilities on the Corporation's consolidated balance sheet, since establishment of the Corporation's financial guarantee liability during the second quarter of 2008:

	Nine months ended September 30, 2008	
	ARCs Held by Customers, at Par Value	Financial Guarantee Liability
	(in thousands)	
Upon establishment of financial guarantee	\$ 332,715	\$ (13,200)
Purchases of ARCs	(166,765)	7,138
Redemptions of ARCs	(360)	
Estimated fair value adjustment charged to expense		(2,660)
Balance at September 30, 2008	\$ 165,590	\$ (8,772)

During the three and nine months ended September 30, 2008, the Corporation purchased ARCs with a par value of \$34.2 million and \$166.8 million, respectively, from customers. The cost of the ARCs purchased, net of interest adjustments, during the three and nine months ended September 30, 2008 was approximately \$33.8 million and \$164.4 million, respectively. Upon purchase, the Corporation recorded the ARCs as available for sale investment securities at their estimated fair value. During the three and nine months ended September 30, 2008, the financial guarantee liability was reduced by an amount equal to the difference between the purchase price of the ARCs and their estimated fair value, or \$1.5 million and \$7.1 million, respectively.

Management believes that the financial guarantee liability recorded as of September 30, 2008 is adequate. Future purchases of ARCs, changes in their estimated fair value or changes in the likelihood of their purchase from customers could require the Corporation to make adjustments to the liability.

Residential Lending Contingencies

Residential mortgages are originated and sold by the Corporation through Fulton Mortgage Company (Fulton Mortgage), which is a division of each of the Corporation's subsidiary banks, and The Columbia Bank, which maintains its own mortgage lending operations. The loans originated and sold through these channels are predominately prime loans that conform to published standards of government sponsored agencies. Prior to 2008, the Corporation's Resource Bank affiliate operated a significant national wholesale mortgage lending operation from the time the Corporation acquired Resource Bank in 2004 through 2007. In the first quarter of 2008, the Corporation merged Resource Bank into its Fulton Bank affiliate.

For the year ended December 31, 2007, the Corporation recorded \$25.1 million of charges related to actual and potential repurchases of residential mortgage loans and home equity loans which were originated and sold to secondary market investors by the former Resource Bank's mortgage division, Resource Mortgage. Of the \$25.1 million charge, \$16.0 million and \$24.9 million were recorded during

Table of Contents

the three and nine months ended September 30, 2007, respectively. Resource Mortgage's national wholesale mortgage lending operation originated loans that were sold under various investor programs, including some that allowed for reduced documentation and/or no verification of certain borrower qualifications, such as income or assets.

The Corporation reduced its residential mortgage lending risk by exiting from the national wholesale mortgage business at Resource Mortgage, where the majority of the repurchased loans were originated. During the three and nine months ended September 30, 2008, the Corporation recorded \$500,000 and \$2.0 million, respectively, of additional charges related to actual and potential repurchases of residential mortgage and home equity loans, and continued to evaluate and address the loans repurchased from investors from the prior year. The charges incurred in 2008 were for mortgages originated in prior years that could potentially be repurchased.

The following table presents a summary of the approximate principal balances and related reserves/write-downs recognized on the Corporation's consolidated balance sheet, by general category:

	September 30, 2008	
	Principal	Reserves/ Write-downs
	(in thousands)	
Outstanding repurchase requests (1) (2)	\$ 9,900	\$ (4,290)
No repurchase request received - sold loans with identified potential misrepresentations of borrower information (1) (2)	12,300	(3,710)
Repurchased loans (3)	11,544	(1,850)
Foreclosed real estate (OREO) (4)	17,350	
Total reserves/write-downs at September 30, 2008		\$ (9,850)

(1) Principal balances had not been repurchased and, therefore, are not included on the consolidated balance sheet as of September 30, 2008.

(2) Reserve balance included as a component of other liabilities on the consolidated balance sheet as of September 30, 2008.

(3) Principal balances, net of write-downs, are included as a component of loans, net of unearned income on the consolidated balance sheet as of September 30, 2008.

(4) OREO is written down to its estimated fair value upon transfer from loans receivable.

The following presents the change in the reserve/write-down balances:

	Three months ended September 30		Nine months ended September 30	
	2008	2007	2008	2007
	(in thousands)			
Total reserves/write-downs, beginning of period	\$ 17,460	\$ 7,920	\$ 18,620	\$ 500
Additional charges to expense	500	16,040	2,000	24,940
Charge-offs	(8,110)	(4,190)	(10,770)	(5,670)
Total reserves/write-downs, end of period	\$ 9,850	\$ 19,770	\$ 9,850	\$ 19,770

During the third quarter of 2008, the Corporation entered into settlement agreements with certain secondary market investors. In total, the Corporation agreed to pay these investors \$8.3 million in settlement of outstanding repurchase requests and other potential claims, subject to certain conditions. The result of these settlements was a reduction of the Corporation's exposure to previously sold loans totaling \$16.1 million and a reduction of the reserves for repurchases of \$7.7 million.

Management believes that the reserves recorded as of September 30, 2008 are adequate for the known potential repurchases. However, continued declines in collateral values or the identification of additional loans to be repurchased could necessitate additional reserves in the future.

Table of Contents

NOTE J FAIR VALUE MEASUREMENTS

On January 1, 2008, the Corporation adopted the provisions of Statement of Financial Accounting Standards No. 157,

Fair Value Measurement (Statement 157) for all financial assets and liabilities and all nonfinancial assets and liabilities required to be measured at fair value on a recurring basis. Although the adoption of Statement 157 did not impact the values of assets and liabilities on the Corporation's consolidated balance sheets, the adoption resulted in expanded disclosure requirements for assets and liabilities recorded at fair value.

Statement 157 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into the following three categories (from highest to lowest priority):

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

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

Level 3 Inputs that are largely unobservable, as little or no market data exists for the instrument being valued. Companies are required to categorize all financial assets and liabilities and all nonfinancial assets and liabilities required to be measured at fair value on a recurring basis into the above three levels.

In February 2008, the FASB issued Staff Position No. 157-2, Effective Date of FASB Statement No. 157 (FSP 157-2). FSP 157-2 delayed the effective date of Statement 157 for nonfinancial assets and liabilities measured at fair value on a nonrecurring basis, until fiscal years beginning after November 15, 2008, or January 1, 2009 for the Corporation. In accordance with FSP 157-2, the Corporation did not apply the provisions of Statement 157 for the following nonfinancial assets and liabilities, which are not measured at fair value on a nonrecurring basis: loans, deposits and borrowings acquired in prior years business combinations, other intangible assets initially measured at fair value upon acquisition and reporting units tested annually for goodwill impairment under Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets. The application of FSP 157-2 for these nonfinancial assets and liabilities is not expected to have an impact on their reported values.

In October 2008, the FASB issued Staff Position No. 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active (FSP 157-3). FSP 157-3 clarifies the application of Statement 157 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. FSP 157-3 was effective upon issuance for the Corporation.

Table of Contents**Items Measured at Fair Value on a Recurring Basis**

The Corporation's assets and liabilities measured at fair value on a recurring basis and reported on the consolidated balance sheet as of September 30, 2008 were as follows:

	Level 1	Level 2	Level 3	Total
		(in thousands)		
Available for sale investment securities	\$ 57,965	\$ 2,447,898	\$ 184,735	\$ 2,690,598
Other financial assets	9,711			9,711
Total assets	\$ 67,676	\$ 2,447,898	\$ 184,735	\$ 2,700,309
Certificates of deposit	\$	\$ 13,809	\$	\$ 13,809
Other financial liabilities	9,711	(150)	8,722	18,283
Total liabilities	\$ 9,711	\$ 13,659	\$ 8,722	\$ 32,092

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

Available for sale investment securities Included within this asset category are both equity and debt securities. Equity securities consisting of stocks of financial institutions and mutual funds are listed as Level 1 assets, measured at fair value based on quoted prices for identical securities in active markets. Debt securities, excluding ARCs and certain single-issuer and pooled trust preferred securities, are classified as Level 2 assets and consist of: U.S. government and U.S. government sponsored securities, state and municipal securities, corporate debt securities, collateralized mortgage obligations and mortgage-backed securities. Fair values are determined by a third party pricing service using both quoted prices for similar assets, when available, and model-based valuation techniques that derive fair value based on market-corroborated data, such as instruments with similar prepayment speeds and default interest rates. See Note C, Investment Securities for additional details related to the Corporation's available for sale investment securities.

ARCs, as discussed in Note I, Commitments and Contingencies, are classified as Level 3 assets and measured at fair value based on an independent third-party valuation. All ARCs held by the Corporation were acquired during 2008. Due to their illiquidity, ARCs were valued through the use of an expected cash flows model. The assumptions used in preparing the expected cash flow model include estimates for coupon rates, a time to maturity and market rates of return.

As of September 30, 2008, the Corporation transferred pooled trust-preferred debt securities and certain single-issuer trust preferred securities, for which no current market exists, to Level 3 assets based on guidance provided within FSP 157-3. Prior to September 30, 2008, these securities were presented as Level 2 assets. As of September 30, 2008, the fair values of pooled-trust preferred debt securities were determined through the use of a discounted cash flow model which applied a credit and liquidity adjusted discount rate to expected cash flows for the securities. The fair values of single-issuer trust preferred securities included within Level 3 assets were determined based on quotes provided by third party brokers who determined fair values based predominantly on internal valuation models and were not indicative prices or binding offers.

Restricted equity securities totaling \$106.1 million, issued by the Federal Home Loan Bank and Federal Reserve Bank, have been excluded from the above table.

Table of Contents

Other financial assets Included within this asset category are Level 1 assets, consisting of mutual funds that are held in trust for employee deferred compensation plans and measured at fair value based on quoted prices for identical securities in active markets. The Corporation maintains a separate Level 1 deferred compensation liability of the same amount, included within the **Other financial liabilities** category above, which represents the amounts due to employees under these deferred compensation plans.

Certificates of deposit This category consists of hedged long-term fixed rate certificates of deposit accounted for under Statement 159. The certificates of deposit and their associated interest rate swaps, included within the **Other financial liabilities** category, are measured at fair value through the use of a model-based approach which utilizes market prices for similar instruments in addition to using market-corroborated means, such as interest rates. See Note H, **Derivative Financial Instruments** for additional information.

Other financial liabilities Included within this category are the following liabilities: employee deferred compensation liabilities, described under the heading **Other financial assets** above and included as Level 1 liabilities; interest rate swaps that hedge the aforementioned certificates of deposit, categorized as Level 2 liabilities; and financial guarantees associated with the Corporation's commitment to purchase ARCs held within customer accounts, categorized as Level 3 liabilities.

The fair value of the financial guarantee liability associated with ARCs held by the Corporation's customers was determined using the same methods as the ARCs held by the Corporation and described under the heading **Available for sale investment securities** above. This liability was initially recorded during 2008. See Note I, **Commitments and Contingencies** for additional information.

The following tables present reconciliations of the Corporation's assets and liabilities measured at fair value on a recurring basis using unobservable inputs (Level 3) for the three and nine months ended September 30, 2008:

	Three months ended September 30, 2008			
	Available for Sale Investment Securities			Other Financial
	Pooled Trust	Single-issuer Trust	ARC Investments	Liabilities ARC Financial Guarantee
	Preferred Securities	Preferred Securities	ARC Investments	
	(in thousands)			
Balance, July 1, 2008	\$	\$	\$ 124,992	\$ (7,560)
Transfers to Level 3 (1)	22,749	8,905		
Purchases (2)			32,327	1,498
Adjustment to fair value (3)			(3,839)	(2,660)
Settlements (4)			(833)	
Discount accretion (5)			434	
Balance, September 30, 2008	\$ 22,749	\$ 8,905	\$ 153,081	\$ (8,722)

Table of Contents

	Nine months ended September 30, 2008			
	Available for Sale Investment Securities			Other Financial
	Pooled Trust	Single-issuer Trust	ARC Investments	Liabilities - ARC Financial Guarantee
	Preferred Securities	Preferred Securities	Preferred Securities	
	(in thousands)			
Balance, January 1, 2008	\$	\$	\$	\$
Transfers to Level 3 (1)	22,749	8,905		
Purchases (2)			157,309	7,138
Adjustment to fair value (3)			(3,930)	(15,860)
Settlements (4)			(833)	
Discount accretion (5)			535	
Balance, September 30, 2008	\$ 22,749	\$ 8,905	\$ 153,081	\$ (8,722)

(1) As of September 30, 2008, the Corporation determined that the market for these securities was not active and transferred all amounts from Level 2 to Level 3 based on fair value measurements performed.

(2) For ARC purchases above, amounts represent ARCs acquired from customers at par value with an interest adjustment based on the difference between the interest

customers earned on ARCs during their holding period and the interest that customers would have earned had the amount of the ARCs been invested in 90-day U.S. Treasury bills, less an adjustment to fair value upon purchase.

- (3) Adjustment to fair value was based on a third party valuation of the ARCs held in customer accounts and by the Corporation as of September 30, 2008. For ARCs held within customer accounts, the adjustment to fair value has been included as a component of operating risk loss on the Corporation's consolidated statements of income. For ARCs held by the Corporation as available for sale investment securities, the adjustment to fair value was recorded as an unrealized

holding loss.

- (4) Represent redemptions of ARCs by their issuers.
- (5) Included as a component of net interest income on the Corporation's consolidated statements of income.

Items Measured at Fair Value on a Nonrecurring Basis

Certain financial assets are not measured at fair value on an ongoing basis but are subject to fair value measurement in certain circumstances, such as upon their acquisition or when there is evidence of impairment.

The Corporation's financial assets measured at fair value on a nonrecurring basis and reported on the Corporation's consolidated balance sheet as of September 30, 2008 were as follows:

	Level 1	Level 2	Level 3	Total
		(in thousands)		
Loans held for sale	\$	\$ 71,090	\$	\$ 71,090
Net loans		950	219,441	220,391
Other financial assets		16,526		16,526
Total assets	\$	\$ 88,566	\$ 219,441	\$ 308,007

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

Loans held for sale This category consists of loans held for sale that were measured at the lower of aggregate cost or fair value. Fair value was measured by the price that secondary market investors were offering for loans with similar characteristics.

Net loans This category consists of residential mortgage loans and home equity loans that were previously sold and repurchased from secondary market investors during the first nine months of 2008 and have been classified as Level 2 assets. Upon repurchase, these loans were written down to the appraised value of their underlying collateral. See Note I, Commitments and Contingencies for additional information.

This category also includes commercial loans and commercial mortgage loans which were considered to be impaired under Statement of Financial Accounting Standards No. 114, Accounting

Table of Contents

by Creditors for Impairment of a Loan and have been classified as Level 3 assets. Impaired loans are measured at fair value based on the present value of expected future cash flows discounted at the loan's effective interest rate, or at the loan's observable market price or fair value of its collateral, if the loan is collateral dependent. An allowance for loan losses is allocated to an impaired loan if its carrying value exceeds its estimated fair value. The amount shown is the balance of impaired loans, net of their related allowance for loan loss.

Other financial assets This category includes foreclosed assets that the Corporation obtained during the first nine months of 2008. Fair values for these Level 2 assets were based on estimated selling prices less estimated selling costs for similar assets in active markets.

NOTE K New Accounting Standard

In March 2008, the FASB issued Statement of Financial Accounting Standards No. 161, Disclosures about Derivative Instruments and Hedging Activities (Statement 161). Statement 161 establishes the disclosure requirements for derivative instruments and for hedging activities, including disclosure of information that should enable users of financial information to understand how and why a company uses derivative instruments, how derivative instruments and related hedged items are accounted for, and how derivative instruments and related hedged items affect a company's financial position, financial performance, and cash flows. The standard is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, or the Corporation's March 31, 2009 quarterly report on Form 10-Q. The adoption of Statement 161 is not expected to have a material impact on the Corporation's consolidated financial statements.

NOTE L Reclassifications

Certain amounts in the 2007 consolidated financial statements and notes have been reclassified to conform to the 2008 presentation.

Table of Contents

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

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

FORWARD-LOOKING STATEMENTS

The Corporation has made, and may continue to make, certain forward-looking statements with respect to its acquisition and growth strategies; market risk; changes or adverse developments in economic, political, or regulatory conditions; a continuation or worsening of the current disruption in credit and other markets, including the lack of or reduced access to, and the abnormal functioning of markets for mortgages and other asset-backed securities and for commercial paper and other short-term borrowings; the effect of competition and interest rates on net interest margin and net interest income; investment strategy and income growth; investment securities gains; declines in the value of securities which may result in charges to earnings; changes in rates of deposit and loan growth; asset quality and the impact on assets from adverse changes in the economy and in credit or other markets and resulting effects on credit risk and asset values; balances of risk-sensitive assets to risk-sensitive liabilities; salaries and employee benefits and other expenses; amortization of intangible assets; goodwill impairment; capital and liquidity strategies and other financial and business matters for future periods. The Corporation cautions that these forward-looking statements are subject to various assumptions, risks and uncertainties. Because of the possibility of changes in these assumptions, actual results could differ materially from forward-looking statements. The Corporation undertakes no obligations to update or revise any forward-looking statements.

RESULTS OF OPERATIONS

Overview

Summary Financial Results

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

During the three and nine months ended September 30, 2008, in comparison to the same periods in the prior year, the Corporation experienced strong loan growth in all loan categories, excluding consumer and construction loans. The loan growth was throughout the Corporation's geographical footprint. New loans are underwritten to the Corporation's stringent underwriting standards and are priced to compensate for risk and mitigate pressure on the net interest margin.

Obtaining customer funding for this loan growth has been, and will continue to be, a challenge. During 2008, the Corporation experienced declines in total noninterest and interest-bearing demand and savings balances. As a result, increases in short and long-term borrowings were necessary to fund loan growth. While interest rates on these borrowings have been favorable, future interest rate increases could be detrimental to net interest margin and net interest income.

Table of Contents

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

	As of or for the Three months ended September 30		As of or for the Nine months ended September 30	
	2008	2007	2008	2007
Net income (in thousands)	\$ 29,076	\$ 33,566	\$ 96,250	\$ 114,539
Diluted net income per share	\$ 0.17	\$ 0.19	\$ 0.55	\$ 0.66
Return on average assets	0.73%	0.88%	0.81%	1.03%
Return on average equity	7.25%	8.67%	8.02%	10.07%
Return on average tangible equity (1)	12.72%	15.76%	14.00%	18.42%
Net interest margin (2)	3.74%	3.62%	3.69%	3.69%
Non-performing assets to total assets	1.15%	0.69%	1.15%	0.69%
Net charge-offs to average loans (annualized)	0.38%	0.08%	0.29%	0.07%

(1) Calculated as net income, adjusted for intangible asset amortization (net of tax), divided by average shareholders equity, excluding goodwill and intangible assets.

(2) Presented on a fully taxable-equivalent (FTE) basis, using a 35% Federal tax rate and statutory interest expense disallowances. See also Net Interest Income section of Management's Discussion.

The Corporation's income before taxes for the third quarter of 2008 decreased \$7.8 million, or 16.7%, from the same period in 2007. Income before taxes for the first nine months of 2008 decreased \$30.6 million, or 18.8%, in comparison to the first nine months of 2007. The decrease in income before taxes for the three and nine months ended September 30, 2008 in comparison to the same periods in 2007 were primarily due to the following significant items:

Decreases in income before taxes:

Increases in the provision for loan losses of \$22.1 million and \$46.4 million for the three and nine months ended September 30, 2008, respectively.

Charges associated with the other-than-temporary impairment of investment securities of \$10.7 million and \$39.3 million for the three and nine months ended September 30, 2008, respectively.

Charges related to the Corporation's decision to purchase auction rate securities from customer accounts of \$2.7 million and \$15.9 million for the three and nine months ended September 30, 2008, respectively.

Increases in income before taxes:

Increases in net interest income of \$11.6 million and \$26.7 million for the three and nine months ended September 30, 2008, respectively.

A \$13.9 million gain on the sale of the Corporation's credit card portfolio, recognized in the second quarter of 2008.

A reduction in charges associated with the Corporation's contingent losses related to the potential repurchase of residential mortgage and home equity loans of \$15.5 million and \$22.9 million for the three and nine months ended September 30, 2008, respectively. See Note I, "Commitments and Contingencies" in the Notes to Consolidated Financial Statements for additional details.

Asset Quality Asset quality refers to the underlying credit characteristics of borrowers and the likelihood that defaults on contractual loan payments will result in charge-offs of account balances, which, in turn, result in provisions for loan losses recorded on the consolidated statements of income. By its nature, risk in lending cannot be completely eliminated, but it can be controlled and managed through proper underwriting policies, effective collection procedures and risk management activities. External factors, such as economic conditions, which cannot be controlled by the Corporation, will always have some effect on asset quality, regardless of the strength of an organization's control policies and procedures. During 2008, the banking industry in general, including the Corporation, has been negatively impacted by deteriorating economic conditions. Significant declines in residential real estate values has

Table of Contents

led to an increase in defaults on mortgages and a slowing of the housing markets. This, in turn, has had a detrimental impact on developers and their ability to meet the contractual payments on their loans. Furthermore, weakening economic conditions have impacted other types of credit extended by banks.

The Corporation's non-performing assets increased significantly, from \$107.0 million, or 0.69% of total assets, at September 30, 2007 to \$186.4 million, or 1.15% of total assets, at September 30, 2008. The increase was primarily due to deteriorating general economic conditions, which have negatively impacted consumer confidence and residential real estate values. The Corporation's non-performing assets increased across all loan types, geographic areas, and industries.

The increase in non-performing assets and net charge-offs contributed to the provision for loan losses increasing \$22.1 million, or 479.7%, in comparison to the third quarter of 2007. The provision for loan losses for the first nine months of 2008 increased \$46.4 million, or 561.1%, in comparison to the first nine months of 2007.

Management believes that its policies and procedures for managing asset quality are sound. However, no assurance regarding asset quality in the future can be given. Continuing negative trends in general economic conditions and decreases in the values of underlying collateral could have a detrimental impact on borrowers' ability to repay their loans.

Other-Than-Temporary Impairment of Investment Securities During the three and nine months ended September 30, 2008, the Corporation recorded charges of \$10.7 million and \$39.3 million for the other-than-temporary impairment of investment securities, recorded within Investment securities (losses) gains on the consolidated statements of income.

The Corporation had a portfolio of financial institution stocks at September 30, 2008 with a cost basis of \$55.2 million and a fair value of \$54.3 million. During the three and nine months ended September 30, 2008, the Corporation's other-than-temporary impairment charges related to financial institution stocks were \$2.0 million and \$30.3 million, respectively. Uncertainty surrounding the financial institution sector as a whole negatively impacted the value of these securities. Beginning in 2007 and continuing through the third quarter of 2008, the values of financial institution stocks, including those held by the Corporation, declined significantly. The other-than-temporary impairment charges recorded during the nine months ended September 30, 2008 was due to the increasing severity and duration of the decline in fair values of the stocks written down. These factors, in conjunction with management's evaluation of the near-term prospects of each specific issuer, resulted in the impairment charges.

During the three and nine months ended September 30, 2008, the Corporation also recorded \$816,000 and \$1.2 million in other-than-temporary impairment charges for other equity securities in the form of mutual fund investments and stocks of government sponsored agencies.

During the third quarter of 2008, the Corporation recorded an other-than-temporary charge of \$7.8 million for corporate debt securities. The \$7.8 million charge included a \$4.9 million charge for the write-off of an investment in subordinated debt issued by a failed financial institution and a \$3.0 million charge for a pooled trust preferred security, also issued by financial institutions, for which the carrying value exceeds the future expected cash flows. The fair value of the pooled-trust preferred debt security was determined through the use of a discounted cash flow model which applied a credit and liquidity adjusted discount rate to expected cash flows for the securities. See Note J, Fair Value Measurements in the Notes to Consolidated Financial Statements and the Market Risk section of Management's Discussion for additional details. As of September 30, 2008, the Corporation had debt securities backed by financial institutions, with a cost basis of \$170.1 million and fair value of \$128.9 million, after other-than-temporary write-downs. See Note C, Investment Securities in the Notes to the Consolidated Financial Statements for additional details.

Table of Contents

Further declines in financial institution stock values or in the values of debt securities issued by financial institutions may result in additional other-than-temporary impairment charges, in the future.

Auction Rate Securities Current year developments in the market for student loan auction rate securities, also known as auction rate certificates (ARCs), resulted in the Corporation recording pre-tax charges of \$2.7 million and \$15.9 million, as components of operating risk loss on the consolidated statements of income, during the three and nine months ended September 30, 2008, respectively.

The Corporation's trust company subsidiary, Fulton Financial Advisors, N.A. (FFA), holds ARCs for some of its customers' accounts. ARCs are one of several types of securities that were previously utilized by FFA as short-term investment vehicles for its customers. ARCs are long-term securities structured to allow their sale in periodic auctions, giving the securities some of the characteristics of short-term instruments in normal market conditions. However, in mid-February, 2008, market auctions for ARCs began to fail due to an insufficient number of buyers; these market failures were the first widespread and continuing failures in the over 20-year history of the auction rate securities markets. As a result, although the credit quality of ARCs has not been impacted, ARCs are currently not liquid investments for their holders, including FFA's customers. It is unclear when liquidity will return to this market. Beginning in the second quarter of 2008, FFA agreed to purchase ARCs from customer accounts upon notification from customers that they have liquidity needs or otherwise desire to liquidate their holdings. FFA generally agreed to purchase customer ARCs at par value with an interest adjustment, which would position customers as if they had owned 90-day U.S. Treasury bills instead of ARCs. The estimated fair value of this guarantee was recorded as a liability in accordance with the Financial Accounting Standards Board's Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*—an interpretation of FASB Statements No. 5, 57, and 107 and rescission of FASB Interpretation No. 34, with a corresponding pre-tax charge to earnings. Upon establishment of the guarantee in the second quarter of 2008, \$332.7 million of ARCs, at par value, were held in customer accounts.

As of September 30, 2008, after purchases by the Corporation and redemptions of ARCs by customers, the total balance of ARCs in customer accounts was \$165.6 million. Included within *Available for sale investment securities* on the Corporation's consolidated balance sheet are ARCs with a total cost of \$157.0 million and a fair value of \$153.1 million.

See Note I, *Commitments and Contingencies* in the Notes to Consolidated Financial Statements and the *Market Risk* section of Management's Discussion for additional details.

Net Interest Margin and Net Interest Income The improvement in net interest income in comparison to the three and nine months ended September 30, 2007 was largely due to an increase in average interest-earning assets.

Also contributing to the improvement in net interest income was the fact that interest rates paid on short-term borrowings and many deposit balances declined more quickly than interest rates earned on assets. Decreases in interest rates on short-term borrowings and deposit balances were the result of the Federal Reserve Board (FRB) lowering the Federal Funds rate a total of 275 basis points since September 30, 2007 (from 4.75% to 2.00%). For the three months ended September 30, 2008, interest expense decreased \$36.5 million, or 31.4%, while interest income decreased \$24.9 million, or 10.4%. For the first nine months of 2008, interest expense decreased \$67.8 million, or 20.3%, while interest income decreased \$41.1 million, or 5.9%. The more pronounced decreases in interest expense during the three and nine months ended September 30, 2008 in comparison to the same periods in 2007 contributed to the increase to net interest income for both periods. The continued repricing of assets and the inability to move deposit rates lower in similar increments may mitigate this benefit in the future.

Table of Contents

Finally, the improvement in net interest income was also due to a change in the composition of interest-bearing liabilities in 2008 in comparison to 2007. During the three and nine months ended September 30, 2008, decreases in time deposits and interest-bearing deposits were replaced with lower-cost overnight short-term borrowings.

The Corporation manages its risk associated with changes in interest rates through the techniques described in the Market Risk section of Management's Discussion.

Sale of Credit Card Portfolio In April 2008, the Corporation sold its approximately \$87 million credit card portfolio to U.S. Bank National Association ND, d/b/a Elan Financial Services (Elan). As a result of this sale, the Corporation recorded a \$13.9 million gain in the second quarter of 2008.

Under a separate agreement with Elan, the Corporation provides ongoing marketing services on behalf of Elan and receives fee income for each new account originated and a percentage of the revenue earned on both new accounts and accounts sold. During the three and nine months ended September 30, 2008, the Corporation recognized \$1.3 million and \$2.4 million, respectively, of credit card fee income, included within other income on the consolidated statements of income, in connection with this agreement.

The sale of the credit card portfolio has reduced, and will continue to impact, the Corporation's net interest income for the remainder of 2008. During the year ended December 31, 2007, interest income earned on the credit card portfolio was \$14.8 million, or 1.6% of total interest income, at an average yield of 19.2%. In 2008, prior to the sale of the credit card portfolio, the Corporation recognized interest income on the credit card portfolio of \$5.1 million at an average yield of 20.1%. Assuming the funding for credit cards was provided by Federal funds purchased, the net interest income impact for 2008 and 2007 would be approximately \$4.3 million and \$10.9 million, respectively. Despite the negative impact to the Corporation's net interest margin, the sale of the credit card portfolio has resulted in a reduction of consumer credit risk, while providing a future revenue stream.

Quarter Ended September 30, 2008 compared to the Quarter Ended September 30, 2007

Net Interest Income

Net interest income increased \$11.6 million, or 9.5%, to \$134.0 million in 2008 from \$122.4 million in 2007 due to both an increase in average interest-earning assets and an increase in the net interest margin.

Table of Contents

The following table provides a comparative average balance sheet and net interest income analysis for the third quarter of 2008 as compared to the same period in 2007. Interest income and yields are presented on an FTE basis, using a 35% Federal tax rate and statutory interest expense disallowances. The discussion following this table is based on these FTE amounts. All dollar amounts are in thousands.

	Three months ended September 30					
	2008			2007		
	Average	Yield/	Average	Yield/	Average	Yield/
	Balance	Interest	Rate	Balance	Interest	Rate
	(1)	(1)	(1)	(1)	(1)	(1)
ASSETS						
Interest-earning assets:						
Loans, net of unearned income (2)	\$ 11,696,841	\$ 181,562	6.18%	\$ 10,857,636	\$ 205,747	7.52%
Taxable investment securities (3)	2,117,207	26,025	4.70	2,116,123	24,583	4.65
Tax-exempt investment securities (3)	509,994	6,944	5.45	499,389	6,377	5.11
Equity securities (1) (3)	168,690	1,614	3.82	188,490	2,269	4.80
Total investment securities	2,795,891	34,583	4.78	2,804,002	33,229	4.74
Loans held for sale	101,319	1,539	6.08	159,492	2,694	6.76
Other interest-earning assets	19,013	142	2.94	34,536	432	4.91
Total interest-earning assets	14,613,064	217,826	5.91%	13,855,666	242,102	6.95%
Noninterest-earning assets:						
Cash and due from banks	322,550			338,862		
Premises and equipment	197,895			190,175		
Other assets	933,303			890,901		
Less: Allowance for loan losses	(123,865)			(108,628)		
<i>Total Assets</i>	\$ 15,942,947			\$ 15,166,976		
LIABILITIES AND EQUITY						
Interest-bearing liabilities:						
Demand deposits	\$ 1,734,198	\$ 3,166	0.73%	\$ 1,729,357	\$ 7,630	1.75%
Savings deposits	2,192,747	6,633	1.20	2,259,231	13,680	2.40
Time deposits	4,308,903	37,393	3.45	4,626,160	55,093	4.72
Total interest-bearing deposits	8,235,848	47,192	2.28	8,614,748	76,403	3.52
Short-term borrowings	2,432,109	12,877	2.08	1,477,288	17,786	4.74
FHLB advances and long-term debt	1,819,897	19,722	4.32	1,655,599	22,141	5.32
Total interest-bearing liabilities	12,487,854	79,791	2.54%	11,747,635	116,330	3.93%
Noninterest-bearing liabilities:						
Demand deposits	1,669,908			1,703,137		
Other	190,012			179,391		
<i>Total Liabilities</i>	14,347,774			13,630,163		
Shareholders' equity	1,595,173			1,536,813		

<i>Total Liabilities and Shareholders Equity</i>	\$ 15,942,947			\$ 15,166,976	
Net interest income/net interest margin (FTE)	138,035	3.74%		125,772	3.62%
Tax equivalent adjustment	(4,017)			(3,362)	
Net interest income	\$ 134,018			\$ 122,410	

(1) Includes dividends earned on equity securities.

(2) Includes non-performing loans.

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

Table of Contents

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

	Volume	2008 vs. 2007 Increase (decrease) due to change in Rate (in thousands)		Net
Interest income on:				
Loans, net of unearned income	\$ 14,834	\$	(39,019)	\$ (24,185)
Taxable investment securities	66		1,376	1,442
Tax-exempt investment securities	137		430	567
Equity securities	(223)		(432)	(655)
Loans held for sale	(906)		(249)	(1,155)
Other interest-earning assets	(153)		(137)	(290)
<i>Total interest income</i>	\$ 13,755	\$	(38,031)	\$ (24,276)
Interest expense on:				
Demand deposits	\$ 21	\$	(4,485)	\$ (4,464)
Savings deposits	(392)		(6,655)	(7,047)
Time deposits	(3,593)		(14,107)	(17,700)
Short-term borrowings	7,945		(12,854)	(4,909)
FHLB advances and long-term debt	2,030		(4,449)	(2,419)
<i>Total interest expense</i>	\$ 6,011	\$	(42,550)	\$ (36,539)

Interest income decreased \$24.3 million, or 10.0%, due to a \$38.0 million decrease caused by a 104 basis point reduction in average rates, offset by a \$13.8 million increase in interest income realized from growth in average balances of \$757.4 million, or 5.5%.

The increase in average interest-earning assets was due to loan growth, which is summarized in the following table:

	Three months ended September 30		Increase (decrease)	
	2008	2007	\$	%
			(dollars in thousands)	
Real estate commercial mortgage	\$ 3,820,045	\$ 3,383,487	\$ 436,558	12.9%
Commercial industrial, financial and agricultural	3,557,142	3,281,342	275,800	8.4
Real estate home equity	1,619,935	1,454,947	164,988	11.3
Real estate construction	1,293,096	1,382,951	(89,855)	(6.5)
Real estate residential mortgage	953,420	769,381	184,039	23.9
Consumer	368,804	502,482	(133,678)	(26.6)
Leasing and other	84,399	83,046	1,353	1.6
<i>Total</i>	\$ 11,696,841	\$ 10,857,636	\$ 839,205	7.7%

Loan growth was particularly strong in the commercial mortgage loan and commercial loan categories, which together increased \$712.4 million, or 10.7%. The growth in commercial mortgages and commercial loans was primarily in floating and adjustable rate products. Additional growth came from residential mortgage loans, which increased \$184.0 million, or 23.9%, primarily in traditional adjustable rate products, and an increase in home equity loans of \$165.0 million, or 11.3%, which was primarily due to the introduction of a new blended fixed/floating rate product in late 2007. Generally, the increase was across all loan categories and geographical areas.

Table of Contents

As average deposits decreased, borrowings were used to provide the funding needed to support the growth in average loans. The following table summarizes the changes in average borrowings, by type:

	Three months ended		Increase (decrease)	
	September 30 2008	2007	\$	%
			(dollars in thousands)	
Short-term borrowings:				
Federal funds purchased	\$ 1,399,130	\$ 756,360	\$ 642,770	85.0%
Short-term promissory notes	486,179	446,182	39,997	9.0
FHLB overnight repurchase agreements	290,761	29,413	261,348	888.5
Customer repurchase agreements	213,827	242,375	(28,548)	(11.8)
Other short-term borrowings	42,212	2,958	39,254	N/M
<i>Total short-term borrowings</i>	2,432,109	1,477,288	954,821	64.6
Long-term debt:				
FHLB advances	1,436,741	1,254,251	182,490	14.5
Other long-term debt	383,156	401,348	(18,192)	(4.5)
<i>Total long-term debt</i>	1,819,897	1,655,599	164,298	9.9
<i>Total</i>	\$ 4,252,006	\$ 3,132,887	\$ 1,119,119	35.7%

N/M Not meaningful

The increase in short-term borrowings was mainly due to an increase in Federal funds purchased, which increased \$642.8 million, and Federal Home Loan Bank (FHLB) overnight repurchase agreements, which increased \$261.3 million. The increase in long-term debt was due to an increase in FHLB advances as longer-term rates were locked and durations were extended to manage interest rate risk.

Provision for Loan Losses and Allowance for Credit Losses

The following table presents ending balances of loans outstanding, net of unearned income:

	September	December 31	September 30
	30 2008	2007	2007
		(in thousands)	
Real-estate commercial mortgage	\$ 3,897,703	\$ 3,502,282	\$ 3,407,715
Commercial industrial, agricultural and financial	3,554,615	3,427,085	3,328,963
Real-estate home equity	1,647,245	1,501,231	1,472,376
Real-estate construction	1,277,552	1,342,923	1,389,164
Real-estate residential mortgage	979,486	851,577	809,148
Consumer	387,849	500,708	500,021
Leasing and other	79,079	78,618	80,920
<i>Total</i>	\$ 11,823,529	\$ 11,204,424	\$ 10,988,307

Approximately \$5.2 billion, or 43.8%, of the Corporation's loan portfolio was in commercial mortgage and construction loans at September 30, 2008. While the Corporation does not have a concentration of credit risk with any single borrower, industry or geographical location, the performance of real estate markets and general economic conditions have adversely impacted the performance of these loans.

Poor economic conditions began to have a more noticeable impact on the quality of the Corporation's commercial loans, comprising 30.1% of the total loan portfolio, during the third quarter of 2008, as evidenced by an increasing level of non-performing loans and a continued increase in line of credit usage which

Table of Contents

increased from 38.4% at September 31, 2007 to 42.5% at September 31, 2008. Based on economic forecasts for the remainder of the year, improvements in asset quality for this sector is not expected in the near future.

Approximately \$2.6 billion, or 22.2%, of the Corporation's loan portfolio was in residential mortgage and home equity loans at September 30, 2008. Despite decreases in residential real estate values in some of the Corporation's geographic areas, most notably in portions of Maryland, New Jersey and Virginia, non-performing levels for these loan types have remained steady for the past year.

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

	Three months ended September 30	
	2008	2007
	(dollars in thousands)	
Loans, net of unearned income outstanding at end of period	\$ 11,823,529	\$ 10,988,307
Daily average balance of loans, net of unearned income	\$ 11,696,841	\$ 10,857,636
<i>Balance at beginning of period</i>	\$ 126,223	\$ 106,892
Loans charged off:		
Commercial industrial, agricultural and financial	4,684	1,452
Real estate mortgage	5,857	122
Consumer	991	874
Leasing and other	1,166	357
<i>Total loans charged off</i>	12,698	2,805
Recoveries of loans previously charged off:		
Commercial industrial, agricultural and financial	749	267
Real estate mortgage	238	8
Consumer	304	324
Leasing and other	313	143
<i>Total recoveries</i>	1,604	742
Net loans charged off	11,094	2,063
Provision for loan losses	26,700	4,606
<i>Balance at end of period</i>	\$ 141,829	\$ 109,435
<i>Components of Allowance for Credit Losses:</i>		
Allowance for loan losses	\$ 136,988	\$ 109,435
Reserve for unfunded lending commitments (1)	4,841	
Allowance for credit losses	\$ 141,829	\$ 109,435
<i>Selected Ratios:</i>		
Net charge-offs to average loans (annualized)	0.38%	0.08%

Allowance for credit losses to loans outstanding	1.20%	1.00%
Allowance for loan losses to loans outstanding	1.16%	1.00%

(1) The reserve for unfunded lending commitments was transferred to other liabilities as of December 31, 2007. Prior periods were not reclassified.

Table of Contents

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

	September 30 2008	December 31 2007	September 30 2007
		(dollars in thousands)	
Non-accrual loans	\$ 143,310	\$ 76,150	\$ 71,043
Loans 90 days past due and accruing	21,354	29,782	23,406
<i>Total non-performing loans</i>	164,664	105,932	94,449
Other real estate owned	21,706	14,934	12,536
<i>Total non-performing assets</i>	\$ 186,370	\$ 120,866	\$ 106,985

Non-accrual loans to total loans	1.21%	0.68%	0.65%
Non-performing assets to total assets	1.15%	0.76%	0.69%
Allowance for credit losses to non-performing loans	86%	106%	116%

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

	September 30 2008	December 31 2007	September 30 2007
		(in thousands)	
Real estate construction	\$ 57,436	\$ 30,926	\$ 28,029
Commercial industrial, agricultural and financial	41,489	27,715	24,078
Real estate commercial mortgage	32,642	14,515	14,254
Real estate residential mortgage and home equity	26,274	25,775	24,505
Consumer	6,558	4,741	3,447
Leasing	265	2,260	136
<i>Total non-performing loans</i>	\$ 164,664	\$ 105,932	\$ 94,449

Non-performing assets increased to \$186.4 million, or 1.15% of total assets, at September 30, 2008, from \$107.0 million, or 0.69% of total assets, at September 30, 2007. Total non-performing assets increased \$65.5 million from December 31, 2007. The increase in non-performing assets in comparison to September 30, 2007 was primarily due to increases in non-performing construction loans, commercial mortgages and commercial loans.

In comparison to September 30, 2007, non-performing construction loans increased \$29.4 million, or 104.9%, related to the deteriorating values of residential housing. Non-performing commercial mortgage loans increased \$18.4 million, or 129.0%, and non-performing commercial loans increased \$17.4 million, or 72.3%. The increases in these categories were across most geographical areas and industries and were due to general economic conditions. The \$21.7 million balance of other real estate owned as of September 30, 2008 was primarily due to foreclosures on repurchased residential mortgage loans, which contributed \$17.3 million to the balance of other real estate owned. The provision for loan losses totaled \$26.7 million for the third quarter of 2008, an increase of \$22.1 million, or 479.7%, over the same period in 2007. This significant increase in the provision for loan losses was primarily related to the increase in non-performing loans and net charge-offs, which required additional allocations of the allowance for credit losses.

Table of Contents**Other Expenses**

The following table presents the components of other expenses:

	Three months ended		Increase (decrease)	
	September 30 2008	2007	\$	%
			(dollars in thousands)	
Salaries and employee benefits	\$ 55,310	\$ 52,505	\$ 2,805	5.3%
Net occupancy expense	10,237	9,813	424	4.3
Operating risk loss	3,480	16,345	(12,865)	(78.7)
Data processing	3,242	3,131	111	3.5
Advertising	3,097	2,470	627	25.4
Equipment expense	3,061	3,438	(377)	(11.0)
Telecommunications	2,002	2,016	(14)	(0.7)
Intangible amortization	1,730	1,995	(265)	(13.3)
Professional fees	1,575	1,769	(194)	(11.0)
Supplies	1,419	1,471	(52)	(3.5)
Postage	1,307	1,275	32	2.5
Other	12,695	11,768	927	7.9
<i>Total</i>	\$ 99,155	\$ 107,996	\$ (8,841)	(8.2%)

Salaries and employee benefits increased \$2.8 million, or 5.3%, with salaries increasing \$2.9 million, or 6.8%, and benefits decreasing \$124,000, or 1.3%. The increase in salaries was primarily due to corporate and affiliate management bonus accruals, which increased \$2.1 million, and normal merit increases, offset by decreases related to staff reductions that were made as part of corporate-wide workforce management and centralization initiatives which began in the second quarter of 2007. Average full-time equivalent employees decreased from 3,760 for the third quarter of 2007 to 3,680 for the third quarter of 2008.

The decrease in operating risk loss was due to a \$15.5 million reduction in contingent losses related to the potential repurchase of residential mortgage and home equity loans, offset by a \$2.7 million charge to increase the financial guarantee liability associated with the commitment to purchase ARCs still held in customer accounts, as a result of a decrease in the estimated fair values of the ARCs. See Note I, Commitments and Contingencies in the Notes to Consolidated Financial Statements for additional details.

The \$627,000, or 25.4%, increase in advertising expense was primarily due to core deposit promotional campaigns. The \$377,000 decrease in equipment expense and the \$265,000 decrease in intangible amortization were due to both equipment and intangible assets becoming fully depreciated and amortized during 2008. The \$194,000 decrease in professional fees was due to a decrease in legal fees associated with repurchases of previously sold loans, partially offset by increases in legal fees associated with the disposition of foreclosed real estate. The \$927,000, or 7.9%, increase in other expenses was due to an increase of \$1.2 million associated with the disposition and maintenance of foreclosed real estate and an increase of \$637,000 in insurance premiums assessed by the Federal Deposit Insurance Corporation (FDIC) as a result of one-time credits expiring at certain affiliate banks. These increases were offset by a reduction in non-income based state tax expense of \$1.1 million due to mergers of affiliate banks in prior years. During the three months ended September 30, 2008, FDIC insurance premiums, included in other expenses in the above table, totaled \$1.1 million, consisting of gross premiums of \$1.8 million, reduced by \$662,000 of one-time credits. The FDIC has proposed a change in the insurance assessment rates, which is expected to significantly increase the Corporation's premiums in 2009.

Table of Contents

Income Taxes

Income tax expense for the third quarter of 2008 was \$9.7 million, a \$3.3 million, or 25.3%, decrease from \$13.0 million in 2007. The decrease was primarily due to a decrease in income before taxes.

The Corporation's effective tax rate was 25.0% in 2008, as compared to 27.9% in 2007. The effective rate is generally lower than the Federal statutory rate of 35% due to investments in tax-free municipal securities and Federal tax credits from investments in low and moderate-income housing partnerships. The effective rate for the third quarter of 2008 is lower than the same period in 2007 as non-taxable income and tax credits had a larger impact on the effective rate due to a \$7.8 million decrease in income before taxes.

Nine Months Ended September 30, 2008 Compared to the Nine Months Ended September 30, 2007

Net Interest Income

Net interest income increased \$26.7 million, or 7.3%, to \$391.8 million in 2008 from \$365.1 million in 2007 due to an increase in average interest-earning assets.

Table of Contents

The following table provides a comparative average balance sheet and net interest income analysis for the first nine months of 2008 as compared to the same period in 2007. Interest income and yields are presented on an FTE basis, using a 35% Federal tax rate and statutory interest expense disallowances. The discussion following this table is based on these FTE amounts. All dollar amounts are in thousands.

	Nine months ended September 30					
	2008			2007		
	Average	Yield/	Average	Yield/	Average	Yield/
	Balance	Interest	Rate	Balance	Interest	Rate
	(1)	(1)	(1)	(1)	(1)	(1)
ASSETS						
Interest-earning assets:						
Loans, net of unearned income (2)	\$ 11,472,748	\$ 554,437	6.45%	\$ 10,619,834	\$ 601,390	7.57%
Taxable investment securities (3)	2,275,681	84,114	4.84	2,092,916	71,201	4.54
Tax-exempt investment securities (3)	511,871	20,831	5.43	497,504	19,010	5.09
Equity securities (1) (3)	192,803	5,723	3.96	185,215	6,628	4.78
Total investment securities	2,980,355	110,668	4.89	2,775,635	96,839	4.65
Loans held for sale	102,819	4,726	6.13	188,223	9,771	6.92
Other interest-earning assets	20,701	462	2.96	36,008	1,339	4.93
Total interest-earning assets	14,576,623	670,293	6.13%	13,619,700	709,339	6.96%
Noninterest-earning assets:						
Cash and due from banks	318,844			331,945		
Premises and equipment	196,977			190,711		
Other assets	948,134			896,604		
Less: Allowance for loan losses	(116,598)			(108,425)		
<i>Total Assets</i>	\$ 15,923,980			\$ 14,930,535		
LIABILITIES AND EQUITY						
Interest-bearing liabilities:						
Demand deposits	\$ 1,709,380	\$ 10,538	0.82%	\$ 1,688,129	\$ 21,733	1.72%
Savings deposits	2,179,432	22,396	1.37	2,284,521	41,266	2.41
Time deposits	4,396,409	128,873	3.92	4,537,160	158,411	4.67
Total interest-bearing deposits	8,285,221	161,807	2.61	8,509,810	221,410	3.48
Short-term borrowings	2,365,052	44,093	2.46	1,424,109	51,734	4.82
FHLB advances and long-term debt	1,829,981	60,714	4.43	1,564,333	61,271	5.23
Total interest-bearing liabilities	12,480,254	266,614	2.85%	11,498,252	334,415	3.88%
Noninterest-bearing liabilities:						
Demand deposits	1,649,560			1,726,782		
Other	190,487			184,010		
<i>Total Liabilities</i>	14,320,301			13,409,044		
Shareholders' equity	1,603,679			1,521,491		

<i>Total Liabilities and Shareholders Equity</i>	\$ 15,923,980		\$ 14,930,535	
Net interest income/net interest margin (FTE)	403,679	3.69%	374,924	3.69%
Tax equivalent adjustment	(11,872)		(9,831)	
Net interest income	\$ 391,807		\$ 365,093	

(1) Includes dividends earned on equity securities.

(2) Includes non-performing loans.

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

Table of Contents

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

	2008 vs. 2007		
	Increase (decrease) due to change in		
	Volume	Rate	Net
	(in thousands)		
Interest income on:			
Loans, net of unearned income	\$ 46,318	\$ (93,271)	\$ (46,953)
Taxable investment securities	7,362	5,551	12,913
Tax-exempt investment securities	552	1,269	1,821
Equity securities	264	(1,169)	(905)
Loans held for sale	(4,030)	(1,015)	(5,045)
Other interest-earning assets	(452)	(425)	(877)
<i>Total interest income</i>	\$ 50,014	\$ (89,060)	\$ (39,046)
Interest expense on:			
Demand deposits	\$ 271	\$ (11,466)	\$ (11,195)
Savings deposits	(1,826)	(17,044)	(18,870)
Time deposits	(4,767)	(24,771)	(29,538)
Short-term borrowings	24,482	(32,123)	(7,641)
FHLB advances and long-term debt	9,528	(10,085)	(557)
<i>Total interest expense</i>	\$ 27,688	\$ (95,489)	\$ (67,801)

Interest income decreased \$39.0 million, or 5.5%, due to an \$88.1 million decrease caused by an 83 basis point reduction in average rates, offset by a \$50.0 million increase in interest income realized from a \$956.9 million, or 7.0%, increase in average balances.

The increase in average interest-earning assets was due mainly to loan growth, which is summarized in the following table:

	Nine months ended		Increase (decrease)	
	September 30		\$	%
	2008	2007	(dollars in thousands)	
Real estate commercial mortgage	\$ 3,688,880	\$ 3,303,854	\$ 385,026	11.7%
Commercial industrial, financial and agricultural	3,513,406	3,162,524	350,882	11.1
Real estate home equity	1,571,705	1,444,100	127,605	8.8
Real estate construction	1,304,252	1,386,960	(82,708)	(6.0)
Real estate residential mortgage	903,226	727,491	175,735	24.2
Consumer	406,058	508,544	(102,486)	(20.2)
Leasing and other	85,221	86,361	(1,140)	(1.3)
<i>Total</i>	\$ 11,472,748	\$ 10,619,834	\$ 852,914	8.0%

The growth in loans during the first nine months of 2008 in comparison to the first nine months of 2007 was due to a \$385.0 million, or 11.7%, increase in commercial mortgages and a \$350.9 million, or 11.1%, increase in commercial loans. In both categories, the increases were primarily due to increases in floating and adjustable rate loan products, and partially due to increases in fixed rate products with terms less than five years. Additional growth came from residential mortgage loans, which increased \$175.7 million, or 24.2%, due primarily to increases in traditional adjustable rate products, and an increase in home equity loans of \$127.6 million, or 8.8%, which was primarily due to the introduction of a new blended

Table of Contents

fixed/floating rate product in late 2007. Offsetting these increases were decreases in consumer loans of \$102.5 million, or 20.2%, and a decrease in construction loans of \$82.7 million, or 6.0%. The decrease in consumer loans was due to a decrease in the indirect automobile portfolio and the sale of the credit card portfolio during the second quarter of 2008.

The average yield on loans decreased 112 basis points, or 14.8%, from 7.57% in 2007 to 6.45% in 2008. The decrease in yields reflected a lower interest rate environment, as illustrated by a lower average prime rate during the first nine months of 2008 (5.45%) as compared to the first nine months of 2007 (8.23%).

Average investment securities increased \$204.7 million, or 7.4%. In late 2007, the Corporation pre-purchased investments, based on the expected cash flows to be generated from maturing securities over an approximate six-month period. The result of this pre-purchase was a higher average investment balance for the first nine months of 2008. Also contributing to the increase was the sale of approximately \$250 million of lower-yielding investment securities during the first quarter of 2007, which lowered the balance of average investment securities for the first nine months of 2007.

The average yield on investment securities increased 24 basis points, or 5.2%, from 4.65% in 2007 to 4.89% in 2008. The increase in yield was due to the systematic reinvestment of normal portfolio cash flows, primarily from shorter-duration, lower-yielding mortgage-backed securities, into a combination of higher-yielding mortgage-backed pass-through securities, conservative U.S. government issued collateralized mortgage obligations and longer-term municipal securities.

Average loans held for sale decreased \$85.4 million, or 45.4%, as a result of a \$435.5 million, or 36.6%, decrease in the volume of loans originated for sale in the first nine months 2008 as compared to the first nine months of 2007. The decrease was due to the Corporation's exit from the national wholesale mortgage business, which began during 2007, offset by an increase in volumes across the Corporation's existing retail network.

The \$39.0 million decrease in interest income was more than offset by a decrease in interest expense of \$67.8 million, or 20.3%. Interest expense decreased \$95.5 million as a result of a 103 basis point, or 26.5%, decrease in the average cost of interest-bearing liabilities. The decrease was partially offset by a \$27.7 million increase in interest expense caused by a \$982.0 million, or 8.5%, increase in average interest-bearing liabilities.

The following table summarizes the changes in average deposits, by type:

	Nine months ended		Increase (decrease)	
	September 30		\$	%
	2008	2007		
		(dollars in thousands)		
Noninterest-bearing demand	\$ 1,649,560	\$ 1,726,782	\$ (77,222)	(4.5)%
Interest-bearing demand	1,709,380	1,688,129	21,251	1.3
Savings	2,179,432	2,284,521	(105,089)	(4.6)
<i>Total, excluding time deposits</i>	5,538,372	5,699,432	(161,060)	(2.8)
Time deposits	4,396,409	4,537,160	(140,751)	(3.1)
<i>Total</i>	\$ 9,934,781	\$ 10,236,592	\$ (301,811)	(2.9)%

The Corporation experienced a net decrease in noninterest-bearing and interest-bearing demand and savings accounts of \$161.1 million, or 2.8%. The decrease in non-interest bearing and savings accounts was in both business and personal accounts, while the increase in interest-bearing demand deposits was due to personal accounts. The \$140.8 million decrease in time deposits was due to a \$172.3 million decrease in brokered certificates of deposit, offset by a \$31.5 million increase in customer certificates of deposit.

Table of Contents

As average deposits decreased, borrowings were used to provide the funding needed to support the growth in average loans and investments. The following table summarizes the changes in average borrowings, by type:

	Nine months ended		Increase (decrease)	
	September 30 2008	2007	\$	%
		(dollars in thousands)		
Short-term borrowings:				
Federal funds purchased	\$ 1,296,074	\$ 751,954	\$ 544,120	72.4%
Short-term promissory notes	475,523	379,761	95,762	25.2
FHLB overnight repurchase agreements	346,770	9,912	336,858	N/M
Customer repurchase agreements	221,253	251,520	(30,267)	(12.0)
Other short-term borrowings	25,432	30,962	(5,530)	(17.9)
<i>Total short-term borrowings</i>	2,365,052	1,424,109	940,943	66.1
Long-term debt:				
FHLB advances	1,447,161	1,204,572	242,589	20.1
Other long-term debt	382,820	359,761	23,059	6.4
<i>Total long-term debt</i>	1,829,981	1,564,333	265,648	17.0
<i>Total</i>	\$ 4,195,033	\$ 2,988,442	\$ 1,206,591	40.4%

N/M Not meaningful

The \$940.9 million increase in short-term borrowings was mainly due to an increase in Federal funds purchased, which increased \$544.1 million, and FHLB overnight repurchase agreements, which increased \$336.9 million. The increase in long-term debt was due to an increase in FHLB advances as longer-term rates were locked and durations were extended to manage interest rate risk.

Table of Contents**Provision for Loan Losses and Allowance for Credit Losses**

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

	Nine months ended September 30	
	2008	2007
	(dollars in thousands)	
Loans, net of unearned income outstanding at end of period	\$ 11,823,529	\$ 10,988,307
Daily average balance of loans, net of unearned income	\$ 11,472,748	\$ 10,619,834
<i>Balance at beginning of period</i>	\$ 112,209	\$ 106,884
Loans charged off:		
Commercial industrial, agricultural and financial	12,200	4,596
Real estate mortgage	8,811	527
Consumer	3,738	2,509
Leasing and other	3,771	1,039
<i>Total loans charged off</i>	28,520	8,671
Recoveries of loans previously charged off:		
Commercial industrial, agricultural and financial	1,025	1,467
Real estate mortgage	385	89
Consumer	1,022	903
Leasing and other	1,082	500
<i>Total recoveries</i>	3,514	2,959
Net loans charged off	25,006	5,712
Provision for loan losses	54,626	8,263
<i>Balance at end of period</i>	\$ 141,829	\$ 109,435
Net charge-offs to average loans (annualized)	0.29%	0.07%

The provision for loan losses for the first nine months of 2008 totaled \$54.6 million, an increase of \$46.4 million, or 561.1%, from the same period in 2007. The significant increase in the provision for loan losses was related to the increase in non-performing loans and net charge-offs, which required additional allocations of the allowance for credit losses.

The Corporation experienced increases in charge-offs for commercial loans and mortgage loans of \$7.6 million and \$8.3 million, respectively for the nine months ended September 30, 2008 in comparison to the first nine months of 2007. The ten largest charge-offs for the first nine months of 2008 totaled \$12.7 million, with \$5.8 million of these charge-offs in commercial loans and \$6.9 million in construction and land development loans. Geographically, these charge-offs were spread throughout the Corporation's footprint.

Table of Contents

Investment securities losses of \$29.9 million for the first nine months of 2008 were primarily due to \$30.3 million in charges related to the other-than-temporary impairment of financial institution stocks and \$7.8 million related to the other-than-temporary impairment of debt securities. These impairment charges were offset by \$4.8 million in gains from the redemption of Class B shares in connection with Visa, Inc.'s (Visa) initial public offering and gains on the sale of MasterCard, Incorporated shares, in addition to net gains of \$1.3 million and \$2.2 million on the sale of financial institutions stock and debt securities, respectively.

Other Expenses

The following table presents the components of other expenses:

	Nine months ended		Increase (decrease)	
	September 30			
	2008	2007	\$	%
		(dollars in thousands)		
Salaries and employee benefits	\$ 164,786	\$ 164,353	\$ 433	0.3%
Net occupancy expense	30,999	29,963	1,036	3.5
Operating risk loss	19,108	26,462	(7,354)	(27.8)
Equipment expense	9,907	10,589	(682)	(6.4)
Data processing	9,604	9,550	54	0.6
Advertising	9,521	7,869	1,652	21.0
Telecommunications	5,960	6,189	(229)	(3.7)
Professional fees	5,717	4,353	1,364	31.3
Intangible amortization	5,386	6,176	(790)	(12.8)
Supplies	4,303	4,369	(66)	(1.5)
Postage	4,218	4,047	171	4.2
Other	36,042	33,088	2,954	8.9
<i>Total</i>	\$ 305,551	\$ 307,008	\$ (1,457)	(0.5%)

Salaries and employee benefits increased \$433,000, or 0.3%, with salaries increasing \$3.1 million, or 2.3%, and benefits decreasing \$2.7 million, or 8.6%.

The increase in salaries was primarily due to corporate and affiliate management bonus accruals, which increased \$875,000, and normal merit increases, offset by decreases related to staff reductions that were made as part of corporate-wide workforce management and centralization initiatives which began in the second quarter of 2007.

Average full-time equivalent employees decreased from 3,900 for the first nine months of 2007 to 3,670 for the first nine months of 2008.

The decrease in employee benefits included a \$1.7 million reduction associated with the curtailment of the Corporation's defined benefit pension plan during the second quarter of 2007 and a net decrease in expense for the Corporation's retirement plans as a result of changes in contribution formulas, which were effective January 1, 2008. Also contributing to the decrease was a \$1.1 million decrease in severance expenses as a result of corporate-wide workforce management and centralization initiatives that occurred in 2007.

The \$7.4 million decrease in operating risk loss resulted from \$15.9 million of charges incurred in 2008 due to the Corporation's decision to purchase illiquid ARCs from customer accounts, offset by a \$22.9 million decrease in contingent losses related to the potential repurchase of residential mortgage and home equity loans. See Note I,

Commitments and Contingencies in the Notes to Consolidated Financial Statements for additional details.

The \$1.7 million, or 21.0%, increase in advertising expense was due to core deposit promotional campaigns initiated during 2008. The \$682,000 decrease in equipment expense and the \$790,000 decrease in tangible amortization were due to both equipment and intangible assets becoming depreciated and

Table of Contents

amortized during 2008. The \$1.4 million, or 31.3%, increase in professional fees was primarily due to charges related to a previously disclosed special review conducted at the former Resource Bank relating to potential repurchases of previously sold mortgage loans in the beginning of 2008 and an increase in legal fees as a result of the disposition of foreclosed real estate owned.

The \$3.0 million, or 8.9%, increase in other expenses was primarily due to an increase of \$3.2 million associated with the disposition and maintenance of foreclosed real estate and an increase of \$1.5 million in insurance premiums assessed by the FDIC. These increases were offset by the reversal of \$1.4 million of litigation reserves associated with the Corporation's share of indemnification liabilities with Visa which were no longer necessary as a result of Visa's initial public offering during the first quarter of 2008.

During the nine months ended September 30, 2008, FDIC insurance premiums, included within other expense in the above table, totaled \$2.7 million, consisting of gross premiums of \$5.0 million, reduced by \$2.3 million of one-time credits. The FDIC has proposed a change in the insurance assessment rates, which is expected to significantly increase the Corporation's premiums in 2009.

Income Taxes

Income tax expense for the first nine months of 2008 was \$35.8 million, a \$12.3 million, or 25.5%, decrease from \$48.1 million in 2007, due to a decrease in income before taxes.

The Corporation's effective tax rate was 27.1% in 2008, as compared to 29.6% in 2007. The effective rate is generally lower than the Federal statutory rate of 35% due mainly to investments in tax-free municipal securities and Federal tax credits from investments in low and moderate-income housing partnerships. The effective rate in 2008 is lower than 2007 as non-taxable income and tax credits had a larger impact on the effective tax rate due to a \$30.6 million decrease in income before taxes.

Table of Contents**FINANCIAL CONDITION**

Total assets of the Corporation increased \$213.0 million, or 1.3%, to \$16.1 billion at September 30, 2008, compared to \$15.9 billion at December 31, 2007.

The Corporation experienced a \$619.1 million, or 5.5%, increase in loans, net of unearned income, primarily due to commercial mortgage loans, which increased \$395.4 million, or 11.3%, and commercial loans, which increased \$127.5 million, or 3.7%. The increase in commercial mortgage loans was in adjustable and floating rate products, while the increase in commercial loans was in fixed, floating and adjustable rate products. The Corporation also had additional increases in home equity loans of \$146.0 million, or 9.7%, and residential mortgages of \$127.9 million, or 15.0%. The increase in home equity loans was due to the introduction of a new blended fixed/floating rate product in late 2007. Offsetting these increases were decreases in consumer loans of \$112.9 million, or 22.5%, and construction loans of \$65.4 million, or 4.9%, with the decrease in consumer loans occurring largely as a result of the Corporation's sale of its credit card portfolio in the second quarter of 2008 and the decrease in construction loans due to the slowing in residential housing construction.

Investment securities decreased \$347.0 million, or 11.0%, due to normal pay downs, sales and maturities exceeding purchases. Contributing to the decrease was a late 2007 pre-purchase of approximately \$250 million of investment securities that was based on cash flows expected to be received in the short-term from securities. In addition, during 2008, pay downs and maturities of investment securities were not being fully reinvested. Finally, the Corporation sold approximately \$180 million of securities at the end of the second quarter of 2008 in order to fund balance sheet growth and manage interest rate risk. The impact of the above factors was partially offset by \$166.8 million of ARCs that were purchased from customers during the first nine months of 2008. See Note I, Commitments and Contingencies in the Notes to the Consolidated Financial Statements for additional details.

Deposits decreased \$188.9 million, or 1.9%, due to a decrease in time deposits of \$167.8 million, or 3.7%, and a decrease in noninterest-bearing and interest-bearing demand and savings deposits of \$21.1 million, or 0.4%, due to decreases in personal accounts. The decrease in time deposits was mainly due to a \$247.7 million decrease in brokered certificates of deposit, as interest rates on alternative funding sources were more attractive, offset by an increase of \$79.9 million in customer certificates of deposit.

Short-term borrowings increased \$206.0 million, or 8.6%, due to a \$269.5 million increase in Federal funds purchased and a \$25.0 million increase in borrowings outstanding under the Corporation's line of credit with an unaffiliated bank, offset by a \$100.0 million reduction in FHLB overnight repurchase agreements. Long-term debt increased \$177.8 million, or 10.8%, due to an increase in FHLB term advances.

Capital Resources

Total shareholders' equity increased \$29.0 million, or 1.8%, during the first nine months of 2008. The increase was due to net income of \$96.2 million and \$9.5 million in stock issuances, offset by \$78.3 million in cash dividends paid to shareholders.

The Corporation and its subsidiary banks are subject to various regulatory capital requirements administered by banking regulators. Failure to meet minimum capital requirements can initiate certain actions by regulators that could have a material effect on the Corporation's consolidated financial statements. The regulations require that banks maintain minimum amounts and ratios of total and Tier I capital (as defined in the regulations) to risk weighted assets (as defined), and Tier I capital to average assets (as defined). As of September 30, 2008, the Corporation and each of its bank subsidiaries met the minimum requirements. In addition, each of the Corporation's bank subsidiaries' capital ratios exceeded the amounts required to be considered well capitalized as defined in the regulations.

Table of Contents

The following table summarizes the Corporation's capital ratios in comparison to regulatory requirements:

	September 30 2008	December 31 2007	Regulatory Minimum Capital Adequacy
Total Capital (to Risk Weighted Assets)	11.9%	11.9%	8.0%
Tier I Capital (to Risk Weighted Assets)	9.1%	9.3%	4.0%
Tier I Capital (to Average Assets)	7.5%	7.4%	3.0%

In connection with the Emergency Economic Stabilization Act of 2009 and the Troubled Asset Recovery Program (TARP), the U.S. Department of the Treasury (UST) has initiated a capital purchase program. Through this program, qualifying financial institutions are eligible to participate in the sale of senior preferred stock to the UST in an amount not less than 1% of total risk-weighted assets and not more than 3% of total risk-weighted assets, or between \$125 million and \$375 million for the Corporation as of September 30, 2008. The senior preferred stock will pay cumulative dividends at a rate of 5% per year for the first five years and 9% thereafter. The UST would also receive warrants to purchase a number of shares of common stock of the Corporation having an aggregate market value equal to 15% of the senior preferred stock on the date of the investment, subject to certain reductions.

In November 2008, the Corporation applied to participate in the capital purchase program up to the maximum allowable amount of 3% of risk-weighted assets, or approximately \$375 million.

Liquidity

The Corporation must maintain a sufficient level of liquid assets to meet the cash needs of its customers, who, as depositors, may want to withdraw funds or who, as borrowers, need credit availability. Liquidity is provided on a continuous basis through scheduled and unscheduled principal and interest payments on outstanding loans and investments and through the availability of deposits and borrowings. The Corporation also maintains secondary sources that provide liquidity on a secured and unsecured basis to meet short-term needs.

The Corporation's sources and uses of cash were discussed in general terms in the quarterly and nine months ended net interest income sections of Management's Discussion. The consolidated statements of cash flows provide additional information. The Corporation generated \$167.0 million in cash from operating activities during the first nine months of 2008, mainly due to net income, as adjusted for non-cash expenses such as the provision for loan losses and investment securities gains and losses. Investing activities resulted in a net cash outflow of \$358.6 million, due to purchases of available for sale securities and net increases in loans exceeding the proceeds from the sales and maturities of available for sale securities. Cash flows provided by financing activities were \$126.2 million, due primarily to proceeds from FHLB advances and net increases in short-term borrowings exceeding long-term debt repayments and dividend payments.

Liquidity must also be managed at the Fulton Financial Corporation Parent Company level. For safety and soundness reasons, banking regulations limit the amount of cash that can be transferred from subsidiary banks to the Parent Company in the form of loans and dividends. Generally, these limitations are based on the subsidiary banks' regulatory capital levels and their net income. The Parent Company's cash needs have increased in recent years, requiring additional sources of funds, including the issuance of subordinated debt and trust-preferred securities and the addition of a working capital line of credit with an unaffiliated bank.

These borrowing arrangements supplement the liquidity available from subsidiaries through dividends and borrowings and provide some flexibility in Parent Company cash management. Management

Table of Contents

continues to monitor the liquidity and capital needs of the Parent Company and will implement appropriate strategies, as necessary, to remain adequately capitalized and to meet its cash needs.

As of September 30, 2008, the Corporation had a revolving line of credit agreement with an unaffiliated bank. Under the terms of the agreement, the Parent Company could borrow up to \$100.0 million with interest calculated based on a short-term London Interbank Offering Rate (LIBOR) repriced daily. The credit requires the Corporation to maintain certain financial ratios related to capital strength and earnings. As of September 30, 2008, \$25.0 million was outstanding under this agreement and the Corporation was in compliance with all required covenants. Subsequent to September 30, 2008, the Corporation repaid all outstanding borrowings under this agreement, as the agreement expired on October 31, 2008. These borrowings were replaced by funds from other internal sources.

Table of Contents**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Market risk is the exposure to economic loss that arises from changes in the values of certain financial instruments. The types of market risk exposures generally faced by financial institutions include interest rate risk, equity market price risk, debt security market price risk, foreign currency risk and commodity price risk. Due to the nature of its operations, only equity and debt market price risk and interest rate risk are significant to the Corporation.

Equity Market Price Risk

Equity market price risk is the risk that changes in the values of equity investments could have a material impact on the financial position or results of operations of the Corporation. The Corporation's equity investments consist of \$54.3 million of stocks of publicly traded financial institutions, \$106.1 million of FHLB and FRB stock and \$10.6 million of mutual funds and other. The equity investments most susceptible to equity market price risk are the financial institutions stocks, which had a cost basis of approximately \$55.2 million and fair value of \$54.3 million at September 30, 2008. Gross unrealized gains in this portfolio were \$4.8 million, and gross unrealized losses were \$5.7 million, at September 30, 2008.

Although the carrying value of financial institution stocks accounted for less than 0.4% of the Corporation's total assets at September 30, 2008, the Corporation has a history of realizing gains from this portfolio. However, significant declines in the values of financial institution stocks held in this portfolio have not only impacted the Corporation's ability to realize gains on their sale, but have also resulted in significant other-than-temporary impairment charges. Management continuously monitors the fair value of its equity investments and evaluates current market conditions and operating results of the companies. Periodic sale and purchase decisions are made based on this monitoring process. None of the Corporation's equity securities are classified as trading. Future cash flows from these investments are not provided in the table on page 51 as such investments do not have maturity dates.

The Corporation evaluated, based on existing accounting guidance, whether any unrealized losses on individual equity investments constituted other-than-temporary impairment, which would require a write-down through a charge to earnings. Based on the results of such evaluations, the Corporation recorded write-downs of \$2.0 million and \$30.3 million for specific financial institution stocks that were deemed to exhibit other-than-temporary impairment in value during the three and nine months ended September 30, 2008, respectively. In addition, the Corporation recorded an other-than-temporary impairment charges of \$816,000 and \$1.2 million during the three and nine months ended September 30, 2008, respectively, for a mutual fund investment and stock of government sponsored agencies, also categorized as equity investments. Additional impairment charges may be necessary in the future depending upon the performance of the equity markets in general and the performance of the individual investments held by the Corporation.

In addition to the Corporation's investment portfolio, its investment management and trust services income could be impacted by fluctuations in the securities market. A portion of this revenue is based on the value of the underlying investment portfolios. If the values of those investment portfolios decrease, whether due to factors influencing U.S. securities markets in general, or otherwise, the Corporation's revenue could be negatively impacted. In addition, the Corporation's ability to sell its brokerage services is dependent, in part, upon consumers' level of confidence in the outlook for rising securities prices.

Debt Security Price Risk

Debt security market price risk is the risk that changes in the values of debt security investments could have a material impact on the financial position or results of operations of the Corporation. The

Table of Contents

Corporation's debt security investments consist primarily of mortgage-backed securities and collateralized mortgage obligations whose principal payments are guaranteed by U.S. government sponsored agencies, state and municipal securities, U.S. government sponsored and U.S. government debt securities, auction rate certificates and corporate debt securities. Only the auction rate certificates and corporate debt securities have significant debt security price risk.

Auction rate certificates (ARCs)

Beginning in the second quarter of 2008, the Corporation's debt securities also included ARCs purchased from customers. Due to the current market environment, these ARCs are susceptible to significant market price risk. At September 30, 2008, ARC securities had a cost basis of \$157.0 million and fair value of \$153.1 million, or 0.9% of total assets.

ARCs are long-term securities structured to allow their sale in periodic auctions, resulting in both the treatment of ARCs as short-term instruments in normal market conditions and fair values that could be derived based on periodic auction prices. However, as previously disclosed, beginning in mid-February 2008, market auctions for these securities began to fail due to an insufficient number of buyers, resulting in an illiquid market. This illiquidity has resulted in recent market prices that represent forced liquidations or distressed sales and do not provide an accurate basis for fair value. Therefore, at September 30, 2008, the fair value of the ARC securities held by the Corporation were derived using significant unobservable inputs based on an expected cash flow model which produced fair values which were materially different from those that would be expected from settlement of these investments in the illiquid market that presently exists. The expected cash flow model produced fair values which assumed a return to market liquidity sometime within the next three to five years. If liquidity does not return within a time-frame that is materially consistent with the Corporation's assumptions, the fair value of ARCs could significantly change.

The credit quality of the underlying debt associated with the ARCs is also a factor in the determination of their estimated fair value. As of September 30, 2008, the total estimated fair value of the ARCs held by the Corporation and held within customers' accounts was approximately \$310 million, with \$153.1 million held by the Corporation, as stated above. Approximately 97% of the approximately \$310 million of ARCs are backed by government-backed student loans, while the remaining ARCs are backed by state and municipal securities. Approximately 80% of the student loan ARCs have credit ratings of AAA, with substantially all of the remaining 20% AA-rated. The current illiquid market did not impact the credit risk associated with the assets underlying the ARCs, both those held by the Corporation and those that remain in customer accounts. Therefore, as of September 30, 2008, the risk of changes in the estimated fair values of ARCs due to deterioration in the credit quality of their underlying debt instruments is not significant.

Table of Contents**Corporate Debt Securities**

The Corporation holds corporate debt securities in the form of pooled trust preferred securities, single-issuer trust preferred securities and subordinated debt issued by financial institutions, as presented in the following table:

	September 30, 2008	
	Amortized cost	Estimated fair value
	(in thousands)	
Single-issuer trust preferred securities (1)	\$ 97,870	\$ 74,512
Subordinated debt	40,009	31,666
Pooled trust preferred securities	32,220	22,749
 Total corporate debt securities issued by financial institutions	 \$ 170,099	 \$ 128,927

(1) Single-issuer trust preferred securities with estimated fair values totaling \$8.9 million as of September 30, 2008 are classified as Level 3 assets. See Note J, Fair Value Measurements for additional details.

The single-issuer trust preferred securities and subordinated debt were all issued by banks. Due to the current environment faced by financial institutions, these securities are subject to significant market price risk at this time. Historically, the Corporation determined the fair value of these securities based on prices received from third party brokers and pricing agencies who determined fair values for these securities using both quoted prices for similar assets, when available, and model-based valuation techniques that derived fair value based on market-corroborated data, such as instruments with similar prepayment speeds and default interest rates.

Due to distressed market prices that currently exist for these securities, the Corporation determined that the market for pooled trust preferred securities and certain single-issuer trust preferred securities held by the Corporation was not active. Consistent with the Financial Accounting Standards Board's (FASB) Staff Position No. 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset is not Active* (Staff Position No. 157-3), issued in October 2008, the Corporation determined the fair value of its investments in pooled trust preferred securities using a discounted cash flows model, which applied a credit and liquidity adjusted discount rate to expected cash flows. For certain single-issuer trust preferred securities, the Corporation determined fair values based on quotes provided by third party brokers who determined fair values based predominantly on internal valuation models and were not indicative prices or binding offers.

During the third quarter of 2008, the Corporation recorded a \$3.0 million other-than-temporary impairment charge related to an investment in a pooled trust preferred security based on the fair value calculated using its internal valuation model. In addition, the Corporation recorded a \$4.9 million other-than-temporary charge related to

subordinated debt issued by a failed financial institution. The current distressed market for debt securities issued by financial institutions may continue to impact the fair values of these securities. Additional impairment charges may be necessary in the future depending upon the performance of the individual investments held by the Corporation. See Note J, Fair Value Measurements, in the Notes to Consolidated Financial Statements further discussion related to debt securities fair values.

Interest Rate Risk

Interest rate risk creates exposure in two primary areas. First, changes in rates have an impact on the Corporation's liquidity position and could affect its ability to meet obligations and continue to grow. Second, movements in interest rates can create fluctuations in the Corporation's net income and changes in the economic value of its equity.

Table of Contents

The Corporation employs various management techniques to minimize its exposure to interest rate risk. An Asset/Liability Management Committee (ALCO), consisting of key financial and senior management personnel, meets on a bi-weekly basis. The ALCO is responsible for reviewing the interest rate sensitivity position of the Corporation, approving asset and liability management policies, and overseeing the formulation and implementation of strategies regarding balance sheet positions and earnings.

The following table provides information about the Corporation's interest rate sensitive financial instruments. The table presents expected cash flows and weighted average rates for each significant interest rate sensitive financial instrument, by expected maturity period. None of the Corporation's financial instruments are classified as trading. All dollar amounts are in thousands.

	Expected Maturity Period						Total	Estimated Fair Value
	Year 1	Year 2	Year 3	Year 4	Year 5	Beyond		
Rate loans (1)	\$ 1,122,652	\$ 636,464	\$ 464,427	\$ 338,289	\$ 290,720	\$ 637,201	\$ 3,489,753	\$ 3,500,000
Weighted average rate	5.83%	6.66%	6.62%	6.58%	6.68%	6.37%	6.33%	
Long rate loans (1) (7)	2,614,447	1,179,194	890,475	698,266	1,624,359	1,318,440	8,325,181	8,100,000
Weighted average rate	5.77%	5.99%	5.97%	6.02%	5.25%	6.25%	5.82%	
Rate investments (2)	461,826	379,355	240,044	254,981	274,701	795,372	2,406,279	2,300,000
Weighted average rate	4.65%	4.72%	4.57%	4.61%	5.07%	4.94%	4.79%	
Long rate investments (2)	63		157,511		148	100,830	258,552	230,000
Weighted average rate	4.67%		3.69%		2.86%	5.21%	4.28%	
Interest-earning assets	121,280						121,280	120,000
Weighted average rate	4.78%						4.78%	
	\$ 4,320,268	\$ 2,195,013	\$ 1,752,457	\$ 1,291,536	\$ 2,189,928	\$ 2,851,843	\$ 14,601,045	\$ 14,400,000
Weighted average rate	5.64%	5.96%	5.74%	5.89%	5.42%	5.87%	5.74%	
Rate deposits (3)	\$ 3,207,161	\$ 631,788	\$ 308,281	\$ 86,296	\$ 93,428	\$ 41,774	\$ 4,368,728	\$ 4,300,000
Weighted average rate	3.26%	3.89%	3.60%	4.27%	4.43%	1.82%	3.41%	
Long rate deposits (4)	1,549,506	172,143	172,143	157,202	149,267	1,657,067	3,857,328	3,800,000
Weighted average rate	1.39%	0.93%	0.93%	0.85%	0.81%	0.72%	1.01%	
Rate borrowings (5)	171,877	494,741	179,796	102,743	5,781	508,623	1,463,561	1,300,000
Weighted average rate	4.38%	4.86%	3.74%	4.01%	2.87%	5.58%	4.85%	
Long rate borrowings (6)	2,946,294						2,946,294	2,900,000
Weighted average rate	2.09%						2.09%	
	\$ 7,874,838	\$ 1,298,672	\$ 660,220	\$ 346,241	\$ 248,476	\$ 2,207,464	\$ 12,635,911	\$ 12,500,000
Weighted average rate	2.48%	3.87%	2.94%	2.64%	2.22%	1.86%	2.54%	

(1) Amounts are based on contractual payments and maturities, adjusted for

expected
prepayments.

- (2) Amounts are based on contractual maturities; adjusted for expected prepayments on mortgage-backed securities, collateralized mortgage obligations and expected calls on agency and municipal securities.
- (3) Amounts are based on contractual maturities of time deposits.
- (4) Estimated based on history of deposit flows.
- (5) Amounts are based on contractual maturities of debt instruments, adjusted for possible calls.
- (6) Amounts include Federal Funds purchased, short-term promissory notes, floating FHLB advances and securities sold under agreements to repurchase, which mature in less than 90 days, in addition to

junior
subordinated
deferrable interest
debentures.

- (7) Line of credit amounts are based on historical cash flow assumptions, with an average life of approximately 5 years.

The preceding table and discussion addressed the liquidity implications of interest rate risk and focused on expected contractual cash flows from financial instruments. Expected maturities, however, do not necessarily estimate the net interest income impact of interest rate changes. Certain financial instruments, such as adjustable rate loans, have repricing periods that differ from expected cash flows. Overdraft deposit balances are not included in the preceding table.

Table of Contents

Included within the \$8.2 billion of floating rate loans above are \$3.4 billion of loans, or 40% of the total, that float with the prime interest rate, \$1.1 billion, or 14%, of loans which float with other interest rates, primarily LIBOR, and \$3.7 billion, or 46%, of adjustable rate loans. The \$3.7 billion of adjustable rate loans include loans that are fixed rate instruments for a certain period of time, and then convert to floating rates. The following table presents the percentage of adjustable rate loans, stratified by their initial fixed term:

Fixed Rate Term	Percent of Total Adjustable Rate Loans
One year	33.2%
Two years	21.8
Three years	16.5
Four years	12.4
Five years	12.1
Greater than five years	4.0

The Corporation uses three complementary methods to measure and manage interest rate risk. They are static gap analysis, simulation of earnings, and estimates of economic value of equity. Using these measurements in tandem provides a reasonably comprehensive summary of the magnitude of interest rate risk in the Corporation, level of risk as time evolves, and exposure to changes in interest rate relationships.

Static gap provides a measurement of repricing risk in the Corporation's balance sheet as of a point in time. This measurement is accomplished through stratification of the Corporation's assets and liabilities into repricing periods. The sum of assets and liabilities in each of these periods are compared for mismatches within that maturity segment. Core deposits having no contractual maturities are placed into repricing periods based upon historical balance performance. Repricing for mortgage loans, mortgage-backed securities and collateralized mortgage obligations includes the effect of expected cash flows. Estimated prepayment effects are applied to these balances based upon industry projections for prepayment speeds. The Corporation's policy limits the cumulative six-month ratio of rate sensitive assets to rate sensitive liabilities (RSA/RSL) to a range of 0.85 to 1.15. As of September 30, 2008, the cumulative six-month ratio of RSA/RSL was 1.02.

Simulation of net interest income and net income is performed for the next twelve-month period. A variety of interest rate scenarios are used to measure the effects of sudden and gradual movements upward and downward in the yield curve. These results are compared to the results obtained in a flat or unchanged interest rate scenario. Simulation of earnings is used primarily to measure the Corporation's short-term earnings exposure to rate movements. The Corporation's policy limits the potential exposure of net interest income to 10% of the base case net interest income for a 100 basis point shock in interest rates, 15% for a 200 basis point shock and 20% for a 300 basis point shock. A shock is an immediate upward or downward movement of interest rates across the yield curve based upon changes in the prime rate. The shocks do not take into account changes in customer behavior that could result in changes to mix and/or volumes in the balance sheet nor do they account for competitive pricing over the forward 12-month period.

Table of Contents

The following table summarizes the expected impact of interest rate shocks on net interest income (due to the current level of interest rates, the 300 basis point downward shock scenario is not shown):

Rate Shock	Annual change in net interest income	% Change
+300 bp	+ \$19.0 million	+3.6%
+200 bp	+ \$14.2 million	+2.7%
+100 bp	+ \$8.0 million	+1.5%
-100 bp	- \$11.8 million	- 2.2%

Economic value of equity estimates the discounted present value of asset cash flows and liability cash flows. Discount rates are based upon market prices for like assets and liabilities. Upward and downward shocks of interest rates are used to determine the comparative effect of such interest rate movements relative to the unchanged environment. This measurement tool is used primarily to evaluate the longer-term repricing risks and options in the Corporation's balance sheet. A policy limit of 10% of economic equity may be at risk for every 100 basis point shock movement in interest rates. As of September 30, 2008, the Corporation was within policy limits for every 100 basis point shock movement in interest rates.

Table of Contents

Item 4. Controls and Procedures

The Corporation carried out an evaluation, under the supervision and with the participation of the Corporation's management, including the Corporation's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Corporation's Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this quarterly report, the Corporation's disclosure controls and procedures are effective. Disclosure controls and procedures are controls and procedures that are designed to ensure that information required to be disclosed in Corporation reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. There have been no changes in our internal control over financial reporting during the fiscal quarter covered by this quarterly report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II OTHER INFORMATION

Item 1. Legal Proceedings

Not applicable.

Item 1A. Risk Factors

Information responsive to this item as of September 30, 2008 appears under the heading, Risk Factors within the Corporation's Form 10-K for the year ended December 31, 2007, except for the following risk factors, which has been amended or added since December 31, 2007.

Price fluctuations in equity markets, as well as recent market events, such as a continuation of the disruption in credit and other markets and the abnormal functioning of markets for securities, could have an impact on the Corporation's net income.

At September 30, 2008, the Corporation's equity investments consisted of \$106.1 million of FHLB and FRB stock, \$54.3 million of stocks of other financial institutions and \$10.6 million of mutual funds and other. The value of the securities in the Corporation's equity portfolio may be affected by a number of factors, including factors that impact the performance of the U.S. securities market in general and, due to the concentration in stocks of financial institutions in the Corporation's equity portfolio, specific risks associated with that sector. Historically, gains on sales of stocks of other financial institutions have been a recurring component of the Corporation's earnings. However, general economic conditions and uncertainty surrounding the financial institution sector as a whole has impacted the value of these securities, as shown by the portfolio's \$899,000 net unrealized loss as of September 30, 2008. Further declines in bank stock values may impact the Corporation's ability to realize gains in the future and could result in other-than-temporary impairment charges, as reflected by the \$30.3 million of impairment charges recorded during the first nine months of 2008.

In addition to the Corporation's investment portfolio, the Corporation's investment management and trust services income could be impacted by fluctuations in the securities market. A portion of this revenue is based on the value of the underlying investment portfolios. If the values of those investment portfolios decrease, whether due to factors influencing U.S. securities markets in general, or otherwise, the Corporation's revenue could be negatively impacted. In addition, the Corporation's ability to sell its brokerage services is dependent, in part, upon consumers' level of confidence in the outlook for rising securities prices.

Recent developments in the market for student loan auction rate securities (also known as auction rate certificates or ARCs) resulted in the Corporation recording charges of \$13.2 million, recorded as a component of operating risk loss on the consolidated statements of income, during the second quarter of 2008.

The Corporation's trust company subsidiary, Fulton Financial Advisors, N.A. (FFA), holds ARCs for some of its customers' accounts. ARCs are one of several types of securities that were previously utilized by FFA as short-term investment vehicles for its customers. ARCs are long-term securities structured to allow their sale in periodic auctions, resulting in the treatment of ARCs as short-term instruments in normal market conditions. However, in mid-February, 2008, market auctions for ARCs began to fail due to an insufficient number of buyers; these market failures were the first widespread and continuing failures in the over 20-year history of the auction rate securities markets. As a result, although the credit quality of ARCs has not been impacted, ARCs are currently not liquid investments for their holders, including FFA's customers. It is unclear when liquidity will return to this market.

Table of Contents

FFA has agreed to purchase ARCs from customer accounts upon notification from customers that they have liquidity needs or otherwise desire to liquidate their holdings. Specifically, FFA will generally purchase customer ARCs at par value with an interest adjustment, which would position customers as if they had owned 90-day U.S. Treasury bills instead of ARCs.

Management believes that the financial guarantee liability recorded as of September 30, 2008 is adequate. Future purchases of ARCs, changes in their estimated fair value or changes in the likelihood of their purchase could require the Corporation to make adjustments to the amount of the liability and have a material impact on the Corporation's net income.

Difficult Conditions in the Capital Markets and the Economy Generally May Materially Adversely Affect The Corporation's Business and Results of Operations. The Corporation Does Not Expect These Conditions to Improve in the Near Future.

The Corporation's results of operations are affected by conditions in the capital markets and the economy generally. The capital and credit markets have been experiencing extreme volatility and disruption for more than twelve months. The volatility and disruption in these markets have produced downward pressure on stock prices of, and credit availability to, certain companies without regard to those companies' underlying financial strength.

Recently, concerns over inflation, the availability and cost of credit and a declining U.S. real estate market have contributed to increased volatility and diminished expectations for the economy and the capital and credit markets going forward. These factors, combined with declining business and consumer confidence, have precipitated an economic slowdown and induced fears of a prolonged recession. In addition, the fixed-income markets are experiencing a period of extreme volatility which has negatively impacted market liquidity conditions. Initially, the concerns on the part of market participants were focused on the subprime segment of the mortgage-backed securities market. However, these concerns have since expanded to include a broad range of mortgage- and asset-backed and other fixed income securities, including those rated investment grade, the U.S. and international credit and inter-bank money markets generally, and a wide range of financial institutions and markets, asset classes and sectors. As a result, the market for fixed income instruments has experienced decreased liquidity, increased price volatility, credit downgrade events, and increased risk of default. Equity markets have also been experiencing heightened volatility and turmoil, with issuers that have exposure to the real estate, mortgage and credit markets particularly affected. These events and the continuing market upheavals, may have a continued adverse effect on the Corporation. In addition, in the event of extreme and prolonged market events, such as the global credit crisis, the Corporation could incur significant losses.

Factors such as consumer spending, business investment, government spending, the volatility and strength of the capital markets, and inflation all affect the business and economic environment and, ultimately, the amount and profitability of the Corporation. The current crisis has also raised the possibility of future legislative and regulatory actions in addition to the recent enactment of the Emergency Economic Stabilization Act of 2008 that could further impact the Corporation. The Corporation cannot predict whether or when such actions may occur, or what impact, if any, such actions could have on our business, results of operations and financial condition.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not applicable.

Item 3. Defaults Upon Senior Securities and Use of Proceeds

Not applicable.

Table of Contents

Item 4. Submission of Matters to a Vote of Security Holders

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits

See Exhibit Index for a list of the exhibits required by Item 601 of Regulation S-K and filed as part of this report.

57

Table of Contents

**FULTON 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.

FULTON FINANCIAL CORPORATION

Date: November 10, 2008

/s/ R. Scott Smith, Jr.
R. Scott Smith, Jr.
Chairman, Chief Executive Officer and
President

Date: November 10, 2008

/s/ Charles J. Nugent
Charles J. Nugent
Senior Executive Vice President and
Chief Financial Officer
58

Table of Contents

EXHIBIT INDEX
Exhibits Required Pursuant
to Item 601 of Regulation S-K

- 3.1 Amended and Restated Bylaws of Fulton Financial Corporation, as amended and restated on September 16, 2008 Incorporated by reference to Exhibit 3.1 of the Fulton Financial Corporation Current Report on Form 8-K dated September 18, 2008.
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.