

FLUSHING FINANCIAL CORP
Form 10-Q
November 09, 2012

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

FORM 10-Q

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

For the quarterly period ended September 30, 2012

Commission file number 001-33013

FLUSHING FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

11-3209278
(I.R.S. Employer Identification No.)

1979 Marcus Avenue, Suite E140, Lake Success, New York 11042
(Address of principal executive offices)

(718) 961-5400
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company

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

The number of shares of the registrant's Common Stock outstanding as of October 31, 2012 was 30,896,467.

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PART I – FINANCIAL INFORMATION
 FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
 Consolidated Statements of Financial Condition
 (Unaudited)

Item 1. Financial Statements

| (Dollars in thousands, except per share data) | September 30, 2012 | December 31, 2011 |
|--|-----------------------|----------------------|
| ASSETS | | |
| Cash and due from banks | \$ 36,098 | \$ 55,721 |
| Securities available for sale: | | |
| Mortgage-backed securities (\$28,365 and \$37,787 at fair value pursuant to the fair value option at September 30, 2012 and December 31, 2011, respectively) | 728,537 | 747,288 |
| Other securities (\$29,226 and \$30,942 at fair value pursuant to the fair value option at September 30, 2012 and December 31, 2011 respectively) | 232,959 | 65,242 |
| Loans held for sale | 8,780 | - |
| Loans: | | |
| Multi-family residential | 1,482,765 | 1,391,221 |
| Commercial real estate | 527,337 | 580,783 |
| One-to-four family mixed-use property | 653,151 | 693,932 |
| One-to-four family residential | 202,291 | 220,431 |
| Co-operative apartments | 6,632 | 5,505 |
| Construction | 16,319 | 47,140 |
| Small Business Administration | 10,764 | 14,039 |
| Taxi medallion | 13,103 | 54,328 |
| Commercial business and other | 260,998 | 206,614 |
| Net unamortized premiums and unearned loan fees | 13,288 | 14,888 |
| Allowance for loan losses | (30,687) | (30,344) |
| Net loans | 3,155,961 | 3,198,537 |
| Interest and dividends receivable | 18,235 | 17,965 |
| Bank premises and equipment, net | 22,894 | 24,417 |
| Federal Home Loan Bank of New York stock | 35,002 | 30,245 |
| Bank owned life insurance | 85,541 | 83,454 |
| Goodwill | 16,127 | 16,127 |
| Core deposit intangible | 586 | 937 |
| Other assets | 39,730 | 48,016 |
| Total assets | \$ 4,380,450 | \$ 4,287,949 |
| LIABILITIES | | |
| Due to depositors: | | |
| Non-interest bearing | \$ 148,838 | \$ 118,507 |
| Interest-bearing: | | |
| Certificate of deposit accounts | 1,482,255 | 1,529,110 |
| Savings accounts | 297,224 | 349,630 |
| Money market accounts | 158,857 | 200,183 |
| NOW accounts | 986,996 | 919,029 |
| Total interest-bearing deposits | 2,925,332 | 2,997,952 |
| Mortgagors' escrow deposits | 35,865 | 29,786 |
| Borrowed funds (\$23,709 and \$26,311 at fair value pursuant to the fair value option at September 30, 2012 and December 31, 2011, respectively) | 599,606 | 499,839 |

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| | | |
|---|---------------------|---------------------|
| Securities sold under agreements to repurchase | 185,300 | 185,300 |
| Other liabilities | 44,111 | 39,654 |
| Total liabilities | 3,939,052 | 3,871,038 |
| STOCKHOLDERS' EQUITY | | |
| Preferred stock (\$0.01 par value; 5,000,000 shares authorized; None issued) | - | - |
| Common stock (\$0.01 par value; 100,000,000 shares authorized; 31,530,595 shares issued at September 30, 2012 and December 31, 2011; 30,904,130 shares and 30,904,177 shares outstanding at September 30, 2012 and December 31, 2011, respectively) | 315 | 315 |
| Additional paid-in capital | 198,328 | 195,628 |
| Treasury stock, at average cost (626,465 shares and 626,418 shares at September 30, 2012 and December 31, 2011, respectively) | (7,794) | (7,355) |
| Retained earnings | 236,622 | 223,510 |
| Accumulated other comprehensive income, net of taxes | 13,927 | 4,813 |
| Total stockholders' equity | 441,398 | 416,911 |
| Total liabilities and stockholders' equity | \$ 4,380,450 | \$ 4,287,949 |

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

PART I – FINANCIAL INFORMATION
 FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
 Consolidated Statements of Income
 (Unaudited)

| (Dollars in thousands, except per share data) | For the three months ended September 30, | | For the nine months ended September 30 , | |
|--|---|----------|---|------------|
| | 2012 | 2011 | 2012 | 2011 |
| Interest and dividend income | | | | |
| Interest and fees on loans | \$44,857 | \$47,767 | \$ 137,540 | \$ 144,578 |
| Interest and dividends on securities: | | | | |
| Interest | 8,120 | 8,325 | 23,796 | 24,581 |
| Dividends | 191 | 202 | 603 | 606 |
| Other interest income | 25 | 35 | 53 | 89 |
| Total interest and dividend income | 53,193 | 56,329 | 161,992 | 169,854 |
| Interest expense | | | | |
| Deposits | 10,097 | 12,266 | 31,232 | 36,954 |
| Other interest expense | 5,513 | 6,962 | 17,545 | 21,849 |
| Total interest expense | 15,610 | 19,228 | 48,777 | 58,803 |
| Net interest income | 37,583 | 37,101 | 113,215 | 111,051 |
| Provision for loan losses | 5,000 | 5,000 | 16,000 | 15,000 |
| Net interest income after provision for loan losses | 32,583 | 32,101 | 97,215 | 96,051 |
| Non-interest income | | | | |
| Other-than-temporary impairment ("OTTI") charge | - | (4,816) | (4,102) | (8,999) |
| Less: Non-credit portion of OTTI charge recorded in Other Comprehensive Income, before taxes | - | 4,164 | 3,326 | 7,421 |
| Net OTTI charge recognized in earnings | - | (652) | (776) | (1,578) |
| Loan fee income | 731 | 538 | 1,831 | 1,487 |
| Banking services fee income | 411 | 430 | 1,275 | 1,279 |
| Net gain on sale of loans | 52 | 493 | 91 | 493 |
| Net gain from sale of securities | 96 | - | 96 | - |
| Net gain (loss) from fair value adjustments | 825 | 2,085 | (185) | 1,265 |
| Federal Home Loan Bank of New York stock dividends | 390 | 338 | 1,113 | 1,180 |
| Bank owned life insurance | 703 | 705 | 2,088 | 2,067 |
| Other income | 305 | 358 | 966 | 1,108 |
| Total non-interest income | 3,513 | 4,295 | 6,499 | 7,301 |
| Non-interest expense | | | | |
| Salaries and employee benefits | 10,725 | 9,715 | 32,223 | 29,424 |
| Occupancy and equipment | 2,019 | 1,971 | 5,867 | 5,712 |
| Professional services | 1,546 | 1,697 | 4,821 | 4,933 |
| FDIC deposit insurance | 1,064 | 1,030 | 3,168 | 3,409 |
| Data processing | 1,016 | 1,139 | 3,043 | 3,325 |
| Depreciation and amortization | 810 | 792 | 2,429 | 2,337 |
| Other real estate owned/foreclosure expense | 887 | 770 | 2,194 | 1,638 |
| Other operating expenses | 2,676 | 2,376 | 8,773 | 7,592 |

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| | | | | |
|-----------------------------------|---------|----------|----------|----------|
| Total non-interest expense | 20,743 | 19,490 | 62,518 | 58,370 |
| Income before income taxes | 15,353 | 16,906 | 41,196 | 44,982 |
| Provision for income taxes | | | | |
| Federal | 4,543 | 5,099 | 12,403 | 13,575 |
| State and local | 1,445 | 1,657 | 3,662 | 4,230 |
| Total taxes | 5,988 | 6,756 | 16,065 | 17,805 |
| Net income | \$9,365 | \$10,150 | \$25,131 | \$27,177 |
| Basic earnings per common share | \$0.31 | \$0.33 | \$0.83 | \$0.89 |
| Diluted earnings per common share | \$0.31 | \$0.33 | \$0.82 | \$0.88 |
| Dividends per common share | \$0.13 | \$0.13 | \$0.39 | \$0.39 |

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

PART I – FINANCIAL INFORMATION
 FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
 Consolidated Statements of Comprehensive Income
 (Unaudited)

| (in thousands) | For the three months ended September 30, | | For the nine months ended September 30, | |
|--|--|-----------|---|-----------|
| | 2012 | 2011 | 2012 | 2011 |
| Comprehensive Income | | | | |
| Net income | \$ 9,365 | \$ 10,150 | \$ 25,131 | \$ 27,177 |
| Amortization of actuarial losses | 149 | 77 | 447 | 233 |
| Amortization of prior service credits | (6) | (6) | (19) | (19) |
| OTTI charges included in income | - | 367 | 437 | 885 |
| Reclassification adjustment for gains included in income | (54) | - | (54) | - |
| Unrealized gains (losses) on securities, net | 5,034 | 10,694 | 8,303 | 11,137 |
| Comprehensive income | \$ 14,488 | \$ 21,282 | \$ 34,245 | \$ 39,413 |

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

PART I – FINANCIAL INFORMATION
 FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
 Consolidated Statements of Cash Flows
 (Unaudited)

| (Dollars in thousands) | For the nine months ended September 30, | |
|---|--|------------|
| | 2012 | 2011 |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net income | \$ 25,131 | \$ 27,177 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for loan losses | 16,000 | 15,000 |
| Depreciation and amortization of bank premises and equipment | 2,429 | 2,337 |
| Net gain on sale of loans | (91) | (493) |
| Net gain on sale of securities | (96) | - |
| Amortization of premium, net of accretion of discount | 4,893 | 4,167 |
| Net loss (gain) from fair value adjustments | 185 | (1,265) |
| OTTI charge recognized in earnings | 776 | 1,578 |
| Income from bank owned life insurance | (2,088) | (2,067) |
| Stock-based compensation expense | 2,864 | 2,101 |
| Deferred compensation | (169) | 395 |
| Amortization of core deposit intangibles | 351 | 351 |
| Excess tax benefit from stock-based payment arrangements | (111) | (260) |
| Deferred income tax provision | (600) | (335) |
| Decrease in prepaid FDIC assessment | 2,941 | 3,123 |
| Increase (decrease) in other liabilities | 2,057 | (4,928) |
| Decrease in other assets | 1,964 | 757 |
| Net cash provided by operating activities | 56,444 | 47,638 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchases of bank premises and equipment | (906) | (2,489) |
| Net (purchase) redemption of Federal Home Loan Bank of New York shares | (4,757) | 779 |
| Purchases of securities available for sale | (264,508) | (121,570) |
| Proceeds from sales and call of securities available for sale | 6,856 | 8,000 |
| Proceeds from maturities and prepayments of securities available for sale | 121,215 | 103,495 |
| Net (originations) and repayments of loans | (15,482) | 19,553 |
| Purchases of loans | (3,456) | (14,455) |
| Proceeds from sale of real estate owned | 1,261 | 842 |
| Proceeds from sale of delinquent loans | 30,092 | 16,617 |
| Net cash used in investing activities | (126,685) | 10,772 |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Net increase in non-interest bearing deposits | 30,331 | 14,977 |
| Net decrease in interest-bearing deposits | (73,417) | (62,329) |
| Net increase in mortgagors' escrow deposits | 6,079 | 5,939 |
| Net proceeds from short-term borrowed funds | 19,000 | - |
| Proceeds from long-term borrowings | 162,518 | 245,447 |
| Repayment of long-term borrowings | (80,000) | (245,149) |
| Purchases of treasury stock | (2,955) | (4,508) |
| Excess tax benefit from stock-based payment arrangements | 111 | 260 |

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| | | |
|---|-----------|-----------|
| Proceeds from issuance of common stock upon exercise of stock options | 836 | 2,039 |
| Cash dividends paid | (11,885) | (11,973) |
| Net cash provided by (used in) financing activities | 50,618 | (55,297) |
| Net decrease in cash and cash equivalents | (19,623) | 3,113 |
| Cash and cash equivalents, beginning of period | 55,721 | 47,789 |
| Cash and cash equivalents, end of period | \$ 36,098 | \$ 50,902 |
| SUPPLEMENTAL CASH FLOW DISCLOSURE | | |
| Interest paid | \$ 48,365 | \$ 58,427 |
| Income taxes paid | 15,520 | 19,334 |
| Taxes paid if excess tax benefits were not tax deductible | 15,631 | 19,594 |
| Non-cash activities: | | |
| Securities purchased, not yet settled | - | 1,000 |
| Loans transferred to real estate owned | 3,541 | 4,750 |
| Loans provided for the sale of real estate owned | 1,646 | 1,345 |
| Loans held for investment transferred to held for sale | 8,780 | - |

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

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

| (Dollars in thousands, except per share data) | For the nine months ended September 30, | |
|---|--|-------------|
| | 2012 | 2011 |
| Common Stock | | |
| Balance, beginning of period | \$ 315 | \$ 313 |
| Issuance upon exercise of stock options (155,061 common shares for the nine months ended September 30, 2011) | - | 1 |
| Shares issued upon vesting of restricted stock unit awards (119,600 common shares for the nine months ended September 30, 2011) | - | 1 |
| Balance, end of period | \$ 315 | \$ 315 |
| Additional Paid-In Capital | | |
| Balance, beginning of period | \$ 195,628 | \$ 189,348 |
| Award of common shares released from Employee Benefit Trust (154,543 and 140,298 common shares for the nine months ended September 30, 2012 and 2011, respectively) | 1,442 | 1,505 |
| Shares issued upon vesting of restricted stock unit awards (113,272 and 119,800 common shares for the nine months ended September 30, 2012 and 2011, respectively) | 317 | 1,668 |
| Issuance upon exercise of stock options (154,543 and 155,061 common shares for the nine months ended September 30, 2012 and 2011, respectively) | 160 | 1,825 |
| Stock-based compensation activity, net | 670 | 532 |
| Stock-based income tax benefit | 111 | 260 |
| Balance, end of period | \$ 198,328 | \$ 195,138 |
| Treasury Stock | | |
| Balance, beginning of period | \$ (7,355) | \$ - |
| Purchases of shares outstanding(181,000 and 362,050 common shares for the nine months ended September 30, 2012 and 2011, respectively) | (2,444) | (4,132) |
| Shares issued upon vesting of restricted stock unit awards (142,222 and 200 common shares for the nine months ended September 30, 2012 and 2011, respectively) | 1,686 | 3 |
| Issuance upon exercise of stock options (138,025 and 23,129 common shares for the nine months ended September 30, 2012 and 2011, respectively) | 1,665 | 324 |
| Purchases of shares to fund options exercised (60,571 and 3,794 common shares for the nine months ended September 30, 2012 and 2011, respectively) | (835) | (54) |
| Repurchase of shares to satisfy tax obligations (38,723 and 27,441 common shares for the nine months ended September 30, 2012 and 2011, respectively) | (511) | (376) |
| Balance, end of period | \$ (7,794) | \$ (4,235) |
| Retained Earnings | | |
| Balance, beginning of period | \$ 223,510 | \$ 204,128 |
| Net income | 25,131 | 27,177 |
| Cash dividends declared and paid on common shares (\$0.39 per common share for the nine months ended September 30, 2012 and 2011) | (11,885) | (11,973) |
| Issuance upon exercise of stock options (10,480 and 23,129 common shares for the nine months ended September 30, 2012 and 2011, respectively) | (37) | (50) |
| Shares issued upon vesting of restricted stock unit awards (28,950 common shares for the nine months ended September 30, 2012) | (97) | - |
| Balance, end of period | \$ 236,622 | \$ 219,282 |

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Accumulated Other Comprehensive Income (Loss)

| | | |
|--|------------|-------------|
| Balance, beginning of period | \$ 4,813 | \$ (3,744) |
| Change in net unrealized gains on securities available for sale, net of taxes of approximately (\$6,401) and (\$8,707) for the nine months ended September 30, 2012 and 2011, respectively | 8,303 | 11,137 |
| Amortization of actuarial losses, net of taxes of approximately (\$347) and (\$183) for the nine months ended September 30, 2012 and 2011, respectively | 447 | 233 |
| Amortization of prior service credits, net of taxes of approximately \$15 for nine months ended September 30, 2012 and 2011 | (19) | (19) |
| OTTI charges included in income, net of taxes of approximately (\$339) and (\$693) for the nine months ended September 30, 2012 and 2011, respectively | 437 | 885 |
| Reclassification adjustment for gains included in net income, net of taxes of approximately \$42 for the nine months ended September 30, 2012 | (54) | - |
| Balance, end of period | \$ 13,927 | \$ 8,492 |
| Total Stockholders' Equity | \$ 441,398 | \$ 418,992 |

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

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

1. Basis of Presentation

The primary business of Flushing Financial Corporation (the “Holding Company”) is the operation of its wholly-owned subsidiary, Flushing Savings Bank, FSB (the “Savings Bank”). The Holding Company and its direct and indirect wholly-owned subsidiaries, the Savings Bank, Flushing Commercial Bank, Flushing Preferred Funding Corporation, Flushing Service Corporation, and FSB Properties Inc., are collectively herein referred to as the “Company.” The unaudited consolidated financial statements presented in this Quarterly Report on Form 10-Q (“Quarterly Report”) include the collective results of the Company on a consolidated basis.

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

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

The accompanying unaudited consolidated financial statements have been prepared in conformity with the instructions to Quarterly Report on Form 10-Q and Article 10, Rule 10-01 of Regulation S-X for interim financial statements. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). The unaudited consolidated interim financial information should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2011.

When necessary, certain reclassifications have been made to the prior-period consolidated financial statements to conform to the current-period presentation.

2. Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenue and expenses during the reporting period. Estimates that are particularly susceptible to change in the near term are used in connection with the determination of the allowance for loan losses, the evaluation of goodwill for impairment, the evaluation of the need for a valuation allowance of the Company’s deferred tax assets and the evaluation of other-than-temporary impairment (“OTTI”) on securities. The current economic environment has increased the degree of uncertainty inherent in these material estimates. Actual results could differ from these estimates.

3. Earnings Per Share

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

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

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

| | For the three months ended | | For the nine months ended | |
|--|---------------------------------------|----------|---------------------------|-----------|
| | September 30, 2012 | 2011 | September 30, 2012 | 2011 |
| | (In thousands, except per share data) | | | |
| Net income, as reported | \$9,365 | \$10,150 | \$ 25,131 | \$ 27,177 |
| Divided by: | | | | |
| Weighted average common shares outstanding | 30,432 | 30,679 | 30,434 | 30,707 |
| Weighted average common stock equivalents | 30 | 14 | 30 | 37 |
| Total weighted average common shares outstanding and common stock equivalents | 30,462 | 30,693 | 30,464 | 30,744 |
| Basic earnings per common share | \$0.31 | \$0.33 | \$ 0.83 | \$ 0.89 |
| Diluted earnings per common share (1) (2) | \$0.31 | \$0.33 | \$ 0.82 | \$ 0.88 |
| Dividend payout ratio | 41.9 | % 39.4 | % 47.0 | % 43.8 |

(1) For the three months ended September 30, 2012, options to purchase 557,140 shares at an average exercise price of \$17.62 were not included in the computation of diluted earnings per common share since they were anti-dilutive. For the three months ended September 30, 2011, options to purchase 869,200 shares at an average exercise price of \$15.99 were not included in the computation of diluted earnings per common share since they were anti-dilutive.

(2) For the nine months ended September 30, 2012, options to purchase 557,140 shares at an average exercise price of \$17.62 were not included in the computation of diluted earnings per common share since they were anti-dilutive. For the nine months ended September 30, 2011, options to purchase 721,240 shares at an average exercise price of \$16.71 were not included in the computation of diluted earnings per common share since they were anti-dilutive.

4. Debt and Equity Securities

The Company's investments are classified in one of the following three categories and accounted for accordingly: (1) trading securities, (2) securities available for sale and (3) securities held-to-maturity.

The Company did not hold any trading securities or securities held-to-maturity during the three and nine month periods ended September 30, 2012 and 2011. Securities available for sale are recorded at fair value.

The following table summarizes the Company's portfolio of securities available for sale at September 30, 2012:

| | Amortized Cost | Fair Value | Gross Unrealized Gains | Gross Unrealized Losses |
|--------------------------|-------------------|------------|------------------------------|-------------------------------|
| | (In thousands) | | | |
| U.S. government agencies | \$31,578 | \$ 31,799 | \$ 221 | \$ - |

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| | | | | |
|-------------------------------------|-----------|------------|-----------|----------|
| Corporate | 83,117 | 86,726 | 3,609 | - |
| Municipals | 73,594 | 75,067 | 1,556 | 83 |
| Mutual funds | 21,856 | 21,856 | - | - |
| Other | 22,432 | 17,511 | 14 | 4,935 |
| Total other securities | 232,577 | 232,959 | 5,400 | 5,018 |
| REMIC and CMO | 449,921 | 470,910 | 25,303 | 4,314 |
| GNMA | 48,653 | 53,081 | 4,428 | - |
| FNMA | 169,359 | 178,903 | 9,544 | - |
| FHLMC | 24,802 | 25,643 | 841 | - |
| Total mortgage-backed securities | 692,735 | 728,537 | 40,116 | 4,314 |
| Total securities available for sale | \$925,312 | \$ 961,496 | \$ 45,516 | \$ 9,332 |

Mortgage-backed securities shown in the table above include two private issue collateralized mortgage obligations (“CMOs”) that are collateralized by commercial real estate mortgages with amortized cost and market values totaling \$15.8 million and \$16.3 million, respectively, at September 30, 2012. The remaining private issue mortgage-backed securities are backed by one-to-four family residential mortgage loans.

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The following table shows the Company’s available for sale securities with gross unrealized losses and their fair value aggregated by category and length of time the individual securities have been in a continuous unrealized loss position, at September 30, 2012:

| | Total | | Less than 12 months | | 12 months or more | |
|------------------------|----------------|-------------------|---------------------|-------------------|-------------------|-------------------|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | (In thousands) | | | | | |
| Municipals | \$9,825 | \$ 83 | \$9,825 | \$ 83 | \$- | \$ - |
| Other | 4,627 | 4,935 | - | - | 4,627 | 4,935 |
| Total other securities | 14,452 | 5,018 | 9,825 | 83 | 4,627 | 4,935 |
| REMIC and CMO | 37,964 | 4,314 | 11,862 | 94 | 26,102 | 4,220 |
| Total | \$52,416 | \$ 9,332 | \$21,687 | \$ 177 | \$30,729 | \$ 9,155 |

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

The Company reviewed each investment that had an unrealized loss at September 30, 2012. An unrealized loss exists when the current fair value of an investment is less than its amortized cost basis. Unrealized losses on available for sale securities, that are deemed to be temporary, are recorded in AOCI, net of tax. Unrealized losses that are considered to be other-than-temporary are split between credit related and noncredit related impairments, with the credit related impairment being recorded as a charge against earnings and the noncredit related impairment being recorded in AOCI, net of tax.

The Company evaluates its pooled trust preferred securities, included in the table above in the row labeled “Other”, using an impairment model through an independent third party, which includes evaluating the financial condition of each counterparty. For single issuer trust preferred securities, the Company evaluates the issuer’s financial condition. The Company evaluates its mortgage-backed securities by reviewing the characteristics of the securities, including delinquency and foreclosure levels, projected losses at various loss severity levels and credit enhancement and coverage. In addition, private issue CMOs are evaluated using an impairment model through an independent third party. When an OTTI is identified, the portion of the impairment that is credit related is determined by management using the following methods: (1) for trust preferred securities, the credit related impairment is determined by using a discounted cash flow model from an independent third party, with the difference between the present value of the projected cash flows and the amortized cost basis of the security recorded as a credit related loss against earnings; (2) for mortgage-backed securities, credit related impairment is determined for each security by estimating losses based

on a set of assumptions, which includes delinquency and foreclosure levels, projected losses at various loss severity levels, credit enhancement and coverage; and (3) for private issue CMOs, through an impairment model from an independent third party and then recording those estimated losses as a credit related loss against earnings.

Municipals:

The unrealized losses in Municipal securities at September 30, 2012, consist of losses on four municipal securities. The unrealized losses were caused by movements in interest rates. It is not anticipated that these securities would be settled at a price that is less than the amortized cost of the Company's investment. Each of these securities is performing according to its terms and, in the opinion of management, will continue to perform according to its terms. The Company does not have the intent to sell these securities and it is more likely than not the Company will not be required to sell the securities before recovery of the securities amortized cost basis. This conclusion is based upon considering the Company's cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the securities. Therefore, the Company did not consider these investments to be other-than-temporarily impaired at September 30, 2012.

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Other Securities:

The unrealized losses in Other Securities at September 30, 2012, consist of losses on one single issuer trust preferred security and two pooled trust preferred securities. The unrealized losses on such securities were caused by market interest volatility, a significant widening of credit spreads across markets for these securities and illiquidity and uncertainty in the financial markets. These securities are currently rated below investment grade. The pooled trust preferred securities do not have collateral that is subordinate to the classes the Company owns. The Company's management evaluates these securities using an impairment model, through an independent third party, that is applied to debt securities. In estimating OTTI losses, management considers: (1) the length of time and the extent to which the fair value has been less than amortized cost; (2) the current interest rate environment; (3) the financial condition and near-term prospects of the issuer, if applicable; and (4) the intent and ability of the Company to retain its investment in the security for a period of time sufficient to allow for any anticipated recovery in fair value. Additionally, management reviews the financial condition of each individual issuer within the pooled trust preferred securities. All of the issuers of the underlying collateral of the pooled trust preferred securities we reviewed are banks.

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

- § Ratio of tangible equity to assets
- § Tier 1 Risk Weighted Capital
- § Net interest margin
- § Efficiency ratio for most recent two quarters
- § Return on average assets for most recent two quarters
- § Texas Ratio (ratio of non-performing assets plus assets past due over 90 days divided by tangible equity plus the reserve for loan losses)
- § Credit ratings (where applicable)
- § Capital issuances within the past year (where applicable)
- § Ability to complete Federal Deposit Insurance Corporation ("FDIC") assisted acquisitions (where applicable)

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

- § All of the performing issuers in our pools are well capitalized banks and do not appear likely to be closed by their regulators.
- § All of the performing issuers in our pools will continue as a going concern and will not default on their securities.

In order to estimate potential future defaults and deferrals, we segregated the performing underlying issuers by their Texas Ratio. We then reviewed performing issuers with Texas Ratios in excess of 50%. The Texas Ratio is a key indicator of the health of the institution and the likelihood of failure. This ratio compares the problem assets of the institution to the institution's available capital and reserves to absorb losses that are likely to occur in these assets.

There was one performing issuer in our pooled trust preferred securities which had a Texas Ratio in excess of 50.00%. We estimated 25% of the related cash flows of this issuer would not be realized. We concluded that issuers with a Texas Ratio below 50.00% are considered healthy and with minimal risk of default. We assigned a zero default rate to these issuers. Our analysis also assumed that issuers currently deferring would default with no recovery and issuers that have defaulted will have no recovery.

We had an independent third party prepare a discounted cash flow analysis for each of these pooled trust preferred securities based on the assumptions discussed above. Other significant assumptions were: (1) two issuers totaling \$21.5 million will prepay in five years and two issuers totaling \$18.7 million will prepay at their next quarterly payment date; (2) senior classes will not call the debt on their portions; and (3) use of the forward London Interbank Offered Rate (“LIBOR”) curve. The cash flows were discounted at the effective rate for each security. For each issuer that we assumed a 25% shortfall in the cash flows, the cash flow analysis eliminates 25% of the cash flow for each issuer effective immediately.

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

It is not anticipated at this time that the one single issuer trust preferred security and the two pooled trust preferred securities would be settled at a price that is less than the amortized cost of the Company’s investment. Each of these securities is performing according to its terms; except for the pooled trust preferred securities for which the Company has stopped accruing interest as discussed above and, in the opinion of management based on the review performed at September 30, 2012, will continue to perform according to its terms. The Company does not have the intent to sell these securities and it is more likely than not the Company will not be required to sell the securities before recovery of the securities’ amortized cost basis. This conclusion is based upon considering the Company’s cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the securities. Therefore, the Company did not consider the one single issuer trust preferred security and the two pooled trust preferred securities to be other-than-temporarily impaired at September 30, 2012.

At September 30, 2012, the Company held six trust preferred issues which had a current credit rating of at least one rating below investment grade. Two of those issues are carried under the fair value option and therefore, changes in fair value are included in the Consolidated Statement of Income – Net gain (loss) from fair value adjustments.

The following table details the remaining four trust preferred issues that were evaluated to determine if they were other-than-temporarily impaired at September 30, 2012. The class the Company owns in pooled trust preferred securities does not have any excess subordination.

| Issuer Type | Class | Performing Banks | Amortized Cost | Fair Value | Cumulative Credit Related OTTI | Deferrals/Defaults (1) | | Current Lowest Rating |
|---------------|-------|------------------|------------------|-----------------|--------------------------------|---|--|-----------------------|
| | | | | | | Actual as a Percentage of Original Security | Expected Percentage of Performing Collateral | |
| Single issuer | n/a | 1 | \$ 300 | \$ 277 | \$ - | None | None | BB- |
| Single issuer | n/a | 1 | 500 | 514 | - | None | None | B+ |
| Pooled issuer | B1 | 18 | 5,617 | 2,400 | 2,196 | 24.8% | 0.4% | C |
| Pooled issuer | C1 | 18 | 3,645 | 1,950 | 1,542 | 22.6% | 0.0% | C |
| Total | | | \$ 10,062 | \$ 5,141 | \$ 3,738 | | | |

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

REMIC and CMO:

The unrealized losses in Real Estate Mortgage Investment Conduit (“REMIC”) and CMO securities at September 30, 2012 consist of one issue from the Federal Home Loan Mortgage Corporation (“FHLMC”), one issue from the Federal National Mortgage Association (“FNMA”), one issue from the Government National Mortgage Association (“GNMA”),

and six private issues.

The unrealized losses on the REMIC and CMO securities issued by FHLMC, FNMA and GNMA were caused by movements in interest rates. It is not anticipated that these securities would be settled at a price that is less than the amortized cost of the Company's investment. Each of these securities is performing according to its terms and, in the opinion of management, will continue to perform according to its terms. The Company does not have the intent to sell these securities and it is more likely than not the Company will not be required to sell the securities before recovery of the securities amortized cost basis. This conclusion is based upon considering the Company's cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the securities. Therefore, the Company did not consider these investments to be other-than-temporarily impaired at September 30, 2012.

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The unrealized losses on the six REMIC and CMO securities issued by private issuers were caused by movements in interest rates, a significant widening of credit spreads across markets for these securities and illiquidity and uncertainty in the financial markets. Each of these securities has some level of credit enhancements and none are collateralized by sub-prime loans. Currently, two of these securities are performing according to their terms, with four of these securities remitting less than the full principal amount due. The principal loss for these four securities totaled \$0.9 million for the nine months ended September 30, 2012. These losses were anticipated in the cumulative credit related OTTI charges recorded for these four securities.

Credit related impairment for mortgage-backed securities are determined for each security by estimating losses based on the following set of assumptions: (1) delinquency and foreclosure levels; (2) projected losses at various loss severity levels; and (3) credit enhancement and coverage. Based on these reviews, an OTTI charge was recorded during the nine months ended September 30, 2012 on five private issue CMOs of \$4.1 million before tax, of which \$0.8 million was charged against earnings in the Consolidated Statements of Income and \$3.3 million before tax (\$1.9 million after-tax) was recorded in AOCI. There was no OTTI charge recorded against earnings in the Consolidated Statements of Income during the three months ended September 30, 2012.

The portion of the above mentioned OTTI, recorded during the nine months ended September 30, 2012, that was related to credit losses was calculated using the following significant assumptions: (1) delinquency and foreclosure levels of 11%-18%; (2) projected loss severity of 40%-50%; (3) assumed default rates of 6%-10% for the first 12 months, 2%-7% for the next 12 months, 2%-8% for the next 12 months and 2% thereafter; and (4) prepayment speeds of 6%-20%.

It is not anticipated at this time that the one private issue CMO, for which an OTTI charge during the nine months ended September 30, 2012 was not recorded, would be settled at a price that is less than the current amortized cost of the Company's investment. This security was performing according to their terms and in the opinion of management, will continue to perform according to its terms. The Company does not have the intent to sell this security and it is more likely than not the Company will not be required to sell the security before recovery of the security's amortized cost basis. This conclusion is based upon considering the Company's cash and working capital requirements and contractual and regulatory obligations, none of which the Company believes would cause the sale of the security. Therefore, the Company did not consider the security to be other-than-temporarily impaired at September 30, 2012.

At September 30, 2012, the Company held 15 private issue CMOs which had a current credit rating of at least one rating below investment grade. Five of those issues are carried under the fair value option and therefore, changes in fair value are included in the Consolidated Statement of Income – Net gain (loss) from fair value adjustments.

The following table details the remaining 10 private issue CMOs that were evaluated to determine if they were other-than-temporarily impaired at September 30, 2012:

| Security | Amortized Cost | Fair Value | Outstanding Principal | Cumulative OTTI Charges Recorded | Year of Issuance | Maturity | Current Lowest Rating | Collateral Located in: | | | | | | | Average FICO Score |
|------------------------|----------------|------------|-----------------------|----------------------------------|------------------|----------|-----------------------|------------------------|----|----|----|----|----|----|--------------------|
| | | | | | | | | CA | FL | VA | NY | NJ | TX | MD | |
| (Dollars in thousands) | | | | | | | | | | | | | | | |

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| | | | | | | | | | | | | |
|-------|----------|----------|----------|---------|------|--------------|-----|-----|-----|-----|-----|---------|
| 1 | \$10,322 | \$8,419 | \$11,470 | \$3,470 | 2006 | 05/25/36 D | 42% | | 16% | | | 719 |
| 2 | 4,554 | 4,001 | 4,797 | 727 | 2006 | 08/19/36 D | 54% | | | | | 735 |
| 3 | 4,783 | 4,191 | 5,318 | 1,107 | 2006 | 08/25/36 D | 36% | 15% | | | | 714 |
| 4 | 3,588 | 3,365 | 4,161 | 780 | 2006 | 08/25/36 D | 40% | 14% | 13% | 11% | | 724 |
| 5 | 2,777 | 2,722 | 3,087 | 249 | 2006 | 03/25/36 CC | 37% | | | | | 726 |
| 6 | 1,245 | 1,265 | 1,252 | - | 2005 | 12/25/35 B- | 40% | | | | | 733 |
| 7 | 4,298 | 3,404 | 4,573 | 222 | 2006 | 05/25/36 CC | 25% | | 21% | 12% | 11% | 710 |
| 8 | 427 | 434 | 431 | - | 2006 | 08/25/36 CCC | 28% | | | | | 737 |
| 9 | 1,000 | 1,028 | 1,014 | - | 2005 | 11/25/35 B- | 41% | | 15% | | | 14% 727 |
| 10 | 817 | 820 | 819 | - | 2005 | 11/25/35 CC | 47% | 10% | | | | 738 |
| Total | \$33,811 | \$29,649 | \$36,922 | \$6,555 | | | | | | | | |

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The following table details gross unrealized losses recorded in AOCI and the ending credit loss amount on debt securities, as of September 30, 2012, for which the Company has recorded a credit related OTTI charge in the Consolidated Statements of Income:

| (in thousands) | Amortized Cost | Fair Value | Gross Unrealized Losses Recorded In AOCI | Cumulative Credit OTTI Losses |
|--------------------------------|-------------------|------------------|--|--|
| Private issued CMO's (1) | \$ 30,322 | \$ 26,102 | \$ 4,220 | \$ 3,015 |
| Trust preferred securities (1) | 9,262 | \$ 4,350 | 4,912 | 3,738 |
| Total | \$ 39,584 | \$ 30,452 | \$ 9,132 | \$ 6,753 |

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

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

| (in thousands) | For the nine months ended September 30, 2012 |
|--|--|
| Beginning balance | \$ 6,922 |
| Recognition of actual losses | (945) |
| OTTI charges due to credit loss recorded in earnings | 776 |
| Securities sold during the period | - |
| Securities where there is an intent to sell or requirement to sell | - |
| Ending balance | \$ 6,753 |

The following table details the amortized cost and estimated fair value of the Company's securities classified as available for sale at September 30, 2012, by contractual maturity. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | Amortized Cost | Fair Value (In thousands) |
|--|-------------------|------------------------------|
| Due in one year or less | \$28,389 | \$ 28,408 |
| Due after one year through five years | 58,782 | 61,261 |
| Due after five years through ten years | 29,840 | 30,754 |
| Due after ten years | 115,566 | 112,536 |

| | | |
|-------------------------------------|-----------|------------|
| Total other securities | 232,577 | 232,959 |
| Mortgage-backed securities | 692,735 | 728,537 |
| Total securities available for sale | \$925,312 | \$ 961,496 |

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The following table summarizes the Company's portfolio of securities available for sale at December 31, 2011:

| | Amortized Cost | Fair Value | Gross Unrealized Gains | Gross Unrealized Losses |
|-------------------------------------|-------------------|------------|------------------------------|-------------------------------|
| (In thousands) | | | | |
| U.S. government agencies | \$1,980 | \$ 2,039 | \$ 59 | \$ - |
| Corporate | 20,777 | 20,592 | - | 185 |
| Municipals | 4,534 | 4,532 | - | 2 |
| Mutual funds | 21,369 | 21,369 | - | - |
| Other | 22,023 | 16,710 | 9 | 5,322 |
| Total other securities | 70,683 | 65,242 | 68 | 5,509 |
| REMIC and CMO | 460,824 | 473,639 | 22,796 | 9,981 |
| GNMA | 62,040 | 67,632 | 5,592 | - |
| FNMA | 175,627 | 182,630 | 7,003 | - |
| FHLMC | 22,556 | 23,387 | 831 | - |
| Total mortgage-backed securities | 721,047 | 747,288 | 36,222 | 9,981 |
| Total securities available for sale | \$791,730 | \$ 812,530 | \$ 36,290 | \$ 15,490 |

Mortgage-backed securities shown in the table above include two private issue CMOs that are collateralized by commercial real estate mortgages with amortized cost and market values of \$19.0 million and \$19.2 million, respectively, at December 31, 2011. The remaining private issue mortgage-backed securities are backed by one-to-four family residential mortgage loans.

The following table shows the Company's available for sale securities with gross unrealized losses and their fair value, aggregated by category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2011.

| | Fair Value | Total Unrealized Losses | Less than 12 months Fair Value | Less than 12 months Unrealized Losses | 12 months or more Fair Value | 12 months or more Unrealized Losses |
|------------------------|---------------|-------------------------------|--------------------------------------|---|------------------------------------|---|
| (In thousands) | | | | | | |
| Corporate | \$17,980 | \$ 185 | \$17,980 | \$ 185 | \$- | \$ - |
| Municipals | 1,997 | 2 | 1,997 | 2 | - | - |
| Other | 4,241 | 5,322 | - | - | 4,241 | 5,322 |
| Total other securities | 24,218 | 5,509 | 19,977 | 187 | 4,241 | 5,322 |
| REMIC and CMO | 38,684 | 9,981 | 12,560 | 124 | 26,124 | 9,857 |
| Total | \$62,902 | \$ 15,490 | \$32,537 | \$ 311 | \$30,365 | \$ 15,179 |

5. Loans held for sale

Loans held for sale are carried at the lower of cost or estimated fair value. At September 30, 2012, loans held for sale consists of four non-performing multi-family residential loans totaling \$3.0 million and three non-performing

commercial business loans totaling \$5.8 million. There were no loans held for sale at December 31, 2011.

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

The Company sold delinquent and non-performing loans totaling \$33.1 million, net of charge-offs of \$4.9 million, during the nine months ended September 30, 2012 and sold delinquent and non-performing loans totaling \$16.5 million, net of charge-offs of \$2.2 million during the nine months ended September 30, 2011. There were no net gains from the sale of delinquent and non-performing loans during the three months ended September 30, 2012. There was \$150,000 in net gains from the sale of delinquent and non-performing loans during the three months ended September 30, 2011. There were net gains from the sale of delinquent and non-performing loans totaling \$31,000 and \$150,000 for the nine months ended September 30, 2012 and 2011, respectively.

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6. Loans

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

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

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

The Company recognizes a loan as non-performing when the borrower has indicated the inability to bring the loan current, or due to other circumstances which, in the Company's opinion, indicate the borrower will be unable to bring the loan current within a reasonable time. All loans classified as non-performing, which includes all loans past due 90 days or more, are classified as non-accrual unless there is, in the Company's opinion, compelling evidence the borrower will bring the loan current in the immediate future. Appraisals and/or updated internal evaluations are obtained as soon as practical and before the loan becomes 90 days delinquent. The loan balances of collateral dependent impaired loans are compared to the loan's updated fair value. The balance which exceeds fair value is generally charged-off. Management reviews the allowance for loan losses on a quarterly basis and records as a provision the amount deemed appropriate, after considering current year charge-offs, charge-off trends, new loan production, current balance by particular loan categories and delinquent loans by particular loan categories.

A loan is considered impaired when, based upon the most current information, the Company believes it is probable that it will be unable to collect all amounts due, both principal and interest, according to the contractual terms of the loan. Impaired loans are measured based on the present value of the expected future cash flows discounted at the loan's

effective interest rate, or at the loan's observable market price, or the fair value of the collateral if the loan is collateral dependent. The Company considers fair value of collateral dependent loans to be 85% of the appraised or internally estimated value of the property. Interest income on impaired loans is recorded on a cash basis. The Company's management considers all non-accrual loans impaired.

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

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

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

As of September 30, 2012, the Company utilized recent third party appraisals of the collateral to measure impairment for \$103.7 million, or 75.0%, of collateral dependent impaired loans and used internal evaluations of the property's value for \$34.6 million, or 25.0%, of collateral dependent impaired loans.

The Company may restructure a loan to enable a borrower to continue making payments when it is deemed that the restructure will allow borrowers to become current and remain current on their loans. This restructure may include reducing the interest rate or amount of the monthly payment for a specified period of time, after which the interest rate and repayment terms revert to the original terms of the loan. We classify these loans as Troubled Debt Restructured ("TDR") when the Savings Bank grants a concession to a borrower who is experiencing financial difficulties.

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

The allocation of a portion of the allowance for loan losses for a performing TDR loan is based upon the present value of the future expected cash flows discounted at the loan's original effective rate, or for a non-performing TDR which is collateral dependent, the fair value of the collateral. At September 30, 2012, there were no commitments to lend additional funds to borrowers whose loans were modified to a TDR. The modification of loans to a TDR did not have a significant effect on our operating results, nor did it require a significant allocation of the allowance for loan losses.

The following table shows loans modified and classified as TDR for the three months ended September 30, 2012 and 2011:

| | For the thee months ended September 30, 2012 | | For the thee months ended September 30, 2011 |
|--------|---|--------|---|
| Number | Balance | Number | Balance |

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| (Dollars in thousands) | | | Modification description | | Modification description |
|----------------------------------|---|----------|--|---|--------------------------|
| One-to-four family - residential | 1 | \$ 400 | Received a below market interest rate | - | \$ - |
| Commercial business and other | 2 | 1,900 | Received a below market interest rate and the loan amortization was extended | - | - |
| Total | 3 | \$ 2,300 | | - | \$ - |

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The following table shows loans modified and classified as TDR for the nine months ended September 30, 2012 and 2011:

| (Dollars in thousands) | For the nine months ended September 30, 2012 | | | For the nine months ended September 30, 2011 | | |
|---|--|-----------------|--|--|------------------|--|
| | Number | Balance | Modification description | Number | Balance | Modification description |
| Multi-family residential | - | \$ - | | 6 | \$ 1,800 | Received a below market interest rate and the loan amortization was extended |
| Commercial real estate | 3 | 5,300 | Received a below market interest rate and the loan amortization was extended | 1 | 2,000 | Received a below market interest rate |
| One-to-four family - mixed-use property | 3 | 1,200 | Received a below market interest rate | 2 | 500 | Received a below market interest rate and loan amortization term extended |
| One-to-four family - residential | 1 | 400 | Received a below market interest rate | | | |
| Construction loans | | | | 2 | 24,200 | Received a below market interest rate |
| Commercial business and other | 2 | 1,900 | Received a below market interest rate and the loan amortization was extended | - | - | |
| Total | 9 | \$ 8,800 | | 11 | \$ 28,500 | |

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

| (Dollars in thousands) | September 30, 2012 | | December 31, 2011 | |
|------------------------|--------------------|----------|-------------------|----------|
| | Number | Recorded | Number | Recorded |

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| | of contracts | investment | of contracts | investment |
|---|-----------------|------------|-----------------|------------|
| Multi-family residential | 8 | \$ 2,340 | 11 | \$ 9,412 |
| Commercial real estate | 5 | 8,517 | 2 | 2,499 |
| One-to-four family - mixed-use property | 7 | 2,350 | 3 | 795 |
| One-to-four family - residential | 1 | 376 | | |
| Construction | 1 | 3,805 | 1 | 5,888 |
| Commercial business and other | 2 | 2,553 | 1 | 2,000 |
| Total performing troubled debt restructured | 24 | \$ 19,941 | 18 | \$ 20,594 |

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

| (Dollars in thousands) | September 30, 2012 | | December 31, 2011 | |
|--|---------------------------|------------------------|---------------------------|------------------------|
| | Number of contracts | Recorded investment | Number of contracts | Recorded investment |
| Multi-family residential | 2 | \$ 323 | - | \$ - |
| Commercial real estate | 2 | 3,163 | 2 | 4,340 |
| One-to-four family - mixed-use property | 2 | 815 | 3 | 1,193 |
| Construction | 1 | 9,455 | 1 | 11,673 |
| Total troubled debt restructurings that subsequently defaulted | 7 | \$ 13,756 | 6 | \$ 17,206 |

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During the three months ended September 30, 2012, there were no loans which were modified and classified as TDR within the previous 12 months, that were reclassified to non-accrual status as it was no longer performing in accordance with its modified terms. During the three months ended September 30, 2011, one construction loan for \$11.5 million, which was modified and classified as TDR within the previous 12 months, was reclassified to non-accrual status as it was no longer performing in accordance with its modified terms.

During the nine months ended September 30, 2012, three multi-family TDR totaling \$6.9 million and one commercial TDR totaling \$0.4 million were transferred to non-accrual status as they were no longer performing in accordance with their modified terms. During the nine months ended September 30, 2011, one construction loan for \$11.5 million, one commercial loan for \$3.3 million and two one-to-four family – mixed-use property loan for \$0.7 million which were modified and classified as TDR within the previous 12 months, were reclassified to non-accrual status as they were no longer performing in accordance with their modified terms.

The following table shows our non-performing loans, including Loans held for sale, at the periods indicated:

| (Dollars in thousands) | September 30, 2012 | December 31, 2011 |
|--|--------------------------|-------------------------|
| Loans ninety days or more past due and still accruing: | | |
| Multi-family residential | \$ - | \$ 6,287 |
| Commercial real estate | 540 | 92 |
| Commercial Business and other | 748 | - |
| Total | 1,288 | 6,379 |
| Non-accrual mortgage loans: | | |
| Multi-family residential | 18,242 | 19,946 |
| Commercial real estate | 18,051 | 19,895 |
| One-to-four family - mixed-use property | 20,250 | 28,429 |
| One-to-four family - residential | 13,068 | 12,766 |
| Co-operative apartments | 234 | 152 |
| Construction | 9,787 | 14,721 |
| Total | 79,632 | 95,909 |
| Non-accrual non-mortgage loans: | | |
| Small Business Administration | 294 | 493 |
| Commercial business and other | 19,589 | 14,660 |
| Total | 19,883 | 15,153 |
| Total non-accrual loans | 99,515 | 111,062 |
| Total non-performing loans | \$ 100,803 | \$ 117,441 |

The interest foregone on non-accrual loans and loans classified as TDR totaled \$1.9 million and \$2.2 million for the three months ended September 30, 2012 and 2011, respectively, and \$5.5 million and \$6.3 million for the nine months ended September 30, 2012 and 2011, respectively.

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The following table shows an age analysis of our recorded investment in loans, including Loans held for sale, at September 30, 2012:

| (in thousands) | 30 - 59 Days Past Due | 60 - 89 Days Past Due | Greater than 90 Days | Total Past Due | Current | Total Loans |
|---|-----------------------------|-----------------------------|----------------------------|-------------------|--------------|--------------|
| Multi-family residential | \$ 17,253 | \$ 4,522 | \$ 16,739 | \$ 38,514 | \$ 1,447,135 | \$ 1,485,649 |
| Commercial real estate | 10,798 | 2,065 | 18,051 | 30,914 | 496,423 | 527,337 |
| One-to-four family - mixed-use property | 19,383 | 5,575 | 20,022 | 44,980 | 608,171 | 653,151 |
| One-to-four family - residential | 3,751 | 952 | 12,851 | 17,554 | 184,737 | 202,291 |
| Co-operative apartments | - | - | 234 | 234 | 6,398 | 6,632 |
| Construction loans | 2,462 | - | 9,787 | 12,249 | 4,070 | 16,319 |
| Small Business Administration | - | 789 | 294 | 1,083 | 9,681 | 10,764 |
| Taxi medallion | - | - | - | - | 13,103 | 13,103 |
| Commercial business and other | 2 | 3,979 | 18,747 | 22,728 | 244,166 | 266,894 |
| Total | \$ 53,649 | \$ 17,882 | \$ 96,725 | \$ 168,256 | \$ 3,013,884 | \$ 3,182,140 |

The following table shows an age analysis of our recorded investment in loans at December 31, 2011:

| (in thousands) | 30 - 59 Days Past Due | 60 - 89 Days Past Due | Greater than 90 Days | Total Past Due | Current | Total Loans |
|---|-----------------------------|-----------------------------|----------------------------|-------------------|--------------|--------------|
| Multi-family residential | \$ 20,083 | \$ 6,341 | \$ 26,233 | \$ 52,657 | \$ 1,338,564 | \$ 1,391,221 |
| Commercial real estate | 10,804 | 1,797 | 19,987 | 32,588 | 548,195 | 580,783 |
| One-to-four family - mixed-use property | 20,480 | 3,027 | 27,950 | 51,457 | 642,475 | 693,932 |
| One-to-four family - residential | 4,699 | 1,769 | 12,766 | 19,234 | 201,197 | 220,431 |
| Co-operative apartments | - | - | 152 | 152 | 5,353 | 5,505 |
| Construction loans | 5,065 | - | 14,721 | 19,786 | 27,354 | 47,140 |
| Small Business Administration | 16 | 41 | 452 | 509 | 13,530 | 14,039 |
| Taxi medallion | 71 | - | - | 71 | 54,257 | 54,328 |
| Commercial business and other | 5,476 | 966 | 10,241 | 16,683 | 189,931 | 206,614 |
| Total | \$ 66,694 | \$ 13,941 | \$ 112,502 | \$ 193,137 | \$ 3,020,856 | \$ 3,213,993 |

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

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

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The following table shows our recorded investment, unpaid principal balance and allocated allowance for loan losses, average recorded investment and interest income recognized for loans that were considered impaired at or for the nine month period ended September 30, 2012:

| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment | Interest Income Recognized |
|--|------------------------|--------------------------------|----------------------|-----------------------------------|----------------------------------|
| (In thousands) | | | | | |
| With no related allowance recorded: | | | | | |
| Mortgage loans: | | | | | |
| Multi-family residential | \$20,152 | \$23,908 | \$ - | \$ 30,375 | \$ 200 |
| Commercial real estate | 36,493 | 41,464 | - | 47,077 | 441 |
| One-to-four family mixed-use property | 27,025 | 29,750 | - | 28,340 | 416 |
| One-to-four family residential | 15,053 | 18,352 | - | 14,954 | 116 |
| Co-operative apartments | 237 | 298 | - | 153 | 2 |
| Construction | 12,685 | 15,177 | - | 16,052 | 130 |
| Non-mortgage loans: | | | | | |
| Small Business Administration | 1,404 | 1,628 | - | 1,106 | 9 |
| Taxi Medallion | - | - | - | - | - |
| Commercial Business and other | 3,656 | 4,472 | - | 5,339 | 29 |
| Total loans with no related allowance recorded | 116,705 | 135,049 | - | 143,396 | 1,343 |
| With an allowance recorded: | | | | | |
| Mortgage loans: | | | | | |
| Multi-family residential | 2,897 | 2,897 | 62 | 3,591 | 134 |
| Commercial real estate | 7,795 | 7,861 | 385 | 6,116 | 308 |
| One-to-four family mixed-use property | 4,183 | 4,183 | 713 | 4,741 | 194 |
| One-to-four family residential | 376 | 376 | 95 | 125 | 15 |
| Co-operative apartments | - | - | - | 134 | - |
| Construction | 3,805 | 3,805 | 50 | 4,432 | 105 |
| Non-mortgage loans: | | | | | |
| Small Business Administration | - | - | - | - | - |
| Taxi Medallion | - | - | - | - | - |
| Commercial Business and other | 2,553 | 2,553 | 304 | 2,184 | 88 |
| Total loans with an allowance recorded | 21,609 | 21,675 | 1,609 | 21,323 | 844 |
| Total Impaired Loans: | | | | | |
| Total mortgage loans | \$130,701 | \$148,071 | \$ 1,305 | \$ 156,090 | \$ 2,061 |
| Total non-mortgage loans | \$7,613 | \$8,653 | \$ 304 | \$ 8,629 | \$ 126 |

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The following table shows our recorded investment, unpaid principal balance and allocated allowance for loan losses, average recorded investment and interest income recognized for loans that were considered impaired at or for the year ended December 31, 2011:

| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment | Interest Income Recognized |
|--|------------------------|--------------------------------|----------------------|-----------------------------------|----------------------------------|
| (In thousands) | | | | | |
| With no related allowance recorded: | | | | | |
| Mortgage loans: | | | | | |
| Multi-family residential | \$ 18,403 | \$ 19,200 | \$ - | \$ 16,930 | \$ 838 |
| Commercial real estate | 12,474 | 12,547 | - | 10,008 | 443 |
| One-to-four family mixed-use property | 7,107 | 7,455 | - | 6,976 | 104 |
| One-to-four family residential | 8,394 | 8,394 | - | 6,556 | 97 |
| Co-operative apartments | - | - | - | 20 | - |
| Construction | 30,589 | 32,340 | - | 22,258 | 1,116 |
| Non-mortgage loans: | | | | | |
| Small Business Administration | - | - | - | - | - |
| Taxi Medallion | - | - | - | - | - |
| Commercial Business and other | 8,745 | 8,825 | - | 4,271 | 558 |
| Total loans with no related allowance recorded | 85,712 | 88,761 | - | 67,019 | 3,156 |
| With an allowance recorded: | | | | | |
| Mortgage loans: | | | | | |
| Multi-family residential | 33,223 | 37,649 | 5,290 | 27,507 | 396 |
| Commercial real estate | 19,646 | 22,443 | 3,100 | 14,799 | 401 |
| One-to-four family mixed-use property | 26,432 | 28,622 | 3,960 | 23,551 | 290 |
| One-to-four family residential | 2,480 | 2,681 | 290 | 2,041 | - |
| Co-operative apartments | - | - | - | - | - |
| Construction | - | - | - | 1,750 | - |
| Non-mortgage loans: | | | | | |
| Small Business Administration | 1,432 | 1,432 | 768 | 1,233 | 82 |
| Taxi Medallion | - | - | - | - | - |
| Commercial Business and other | 6,121 | 6,842 | 2,449 | 4,739 | 193 |
| Total loans with an allowance recorded | 89,334 | 99,669 | 15,857 | 75,620 | 1,362 |
| Total Impaired Loans: | | | | | |
| Total mortgage loans | \$ 158,748 | \$ 171,331 | \$ 12,640 | \$ 132,396 | \$ 3,685 |
| Total non-mortgage loans | \$ 16,298 | \$ 17,099 | \$ 3,217 | \$ 10,243 | \$ 833 |

In accordance with our policy and the current regulatory guidelines, we designate loans as “Special Mention,” which is considered “Criticized Loans,” and “Substandard,” “Doubtful,” or “Loss,” which are considered “Classified Loans”. If a loan does not fall within one of the previous mentioned categories then the loan would be considered “Pass.” We designate a

loan as Substandard when a well-defined weakness is identified that jeopardizes the orderly liquidation of the debt. We designate a loan as Doubtful when it displays the inherent weakness of a Substandard loan with the added provision that collection of the debt in full, on the basis of existing facts, is highly improbable. We designate a loan as Loss if it is deemed the debtor is incapable of repayment. Loans that are designated as Loss are charged to the Allowance for Loan Losses. Loans that are non-accrual are designated as Substandard, Doubtful or Loss. We designate a loan as Special Mention if the asset does not warrant classification within one of the other classifications, but does contain a potential weakness that deserves closer attention.

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The following table sets forth the recorded investment in loans designated as Criticized or Classified at September 30, 2012:

| (In thousands) | Special Mention | Substandard | Doubtful | Loss | Total |
|---|--------------------|-------------------|----------------|------------|------------------|
| Multi-family residential | \$ 15,847 | \$ 23,689 | \$- | \$- | \$39,536 |
| Commercial real estate | 15,228 | 29,668 | - | - | 44,896 |
| One-to-four family - mixed-use property | 9,879 | 30,394 | - | - | 40,273 |
| One-to-four family - residential | 2,966 | 15,430 | - | - | 18,396 |
| Co-operative apartments | 198 | 237 | - | - | 435 |
| Construction loans | 3,805 | 12,685 | - | - | 16,490 |
| Small Business Administration | 199 | 459 | 244 | - | 902 |
| Commercial business and other | 5,184 | 23,460 | 1,169 | - | 29,813 |
| Total | \$ 53,306 | \$ 136,022 | \$1,413 | \$- | \$190,741 |

The following table sets forth the recorded investment in loans designated as Criticized or Classified at December 31, 2011:

| (In thousands) | Special Mention | Substandard | Doubtful | Loss | Total |
|---|--------------------|-------------------|----------------|------------|------------------|
| Multi-family residential | \$ 17,135 | \$ 41,393 | \$- | \$- | \$58,528 |
| Commercial real estate | 12,264 | 41,247 | - | - | 53,511 |
| One-to-four family - mixed-use property | 17,393 | 33,831 | - | - | 51,224 |
| One-to-four family - residential | 3,127 | 14,343 | - | - | 17,470 |
| Co-operative apartments | 203 | 153 | - | - | 356 |
| Construction loans | 2,570 | 28,555 | - | - | 31,125 |
| Small Business Administration | 666 | 256 | 214 | - | 1,136 |
| Commercial business and other | 13,585 | 17,613 | 1,169 | - | 32,367 |
| Total | \$ 66,943 | \$ 177,391 | \$1,383 | \$- | \$245,717 |

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

| (In thousands) | For the nine months ended September 30, | |
|-------------------------------|--|-----------------|
| | 2012 | 2011 |
| Balance, beginning of period | \$30,344 | \$27,699 |
| Provision for loan losses | 16,000 | 15,000 |
| Charge-off's | (16,524) | (13,534) |
| Recoveries | 867 | 438 |
| Balance, end of period | \$30,687 | \$29,603 |

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

| (In thousands) | Three Months Ended | | Nine Months Ended | |
|---|--------------------------|--------------------------|--------------------------|--------------------------|
| | September 30, 2012 | September 30, 2011 | September 30, 2012 | September 30, 2011 |
| Multi-family residential | \$3,081 | \$ 2,188 | \$5,163 | \$ 3,984 |
| Commercial real estate | 55 | 1,549 | 2,152 | 4,071 |
| One-to-four family – mixed-use property | 814 | 808 | 3,064 | 1,288 |
| One-to-four family – residential | 198 | - | 1,067 | 1,928 |
| Co-operative apartments | 19 | - | 62 | - |
| Construction | 59 | - | 2,500 | 703 |
| Small Business Administration | 23 | 137 | 265 | 608 |
| Commercial business and other | 963 | 73 | 1,384 | 514 |
| Total net loan charge-offs | \$5,212 | \$ 4,755 | \$15,657 | \$ 13,096 |

7. Other Real Estate Owned

The following are changes in Other Real Estate Owned (“OREO”) during the periods indicated:

| | For the nine months ended September 30, | |
|--------------------------------|--|----------|
| | 2012 | 2011 |
| | (In thousands) | |
| Balance at beginning of period | \$ 3,179 | \$ 1,588 |
| Acquisitions | 3,541 | 4,750 |
| Write-down of carrying value | (285) | (176) |
| Sales | (2,775) | (1,912) |
| Balance at end of period | \$ 3,660 | \$ 4,250 |

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

| | For the three months ended | | For the nine months ended | |
|------------------------------|-------------------------------|-----------------------|---------------------------|-----------------------|
| | September 30, 2012 | September 30, 2011 | September 30, 2012 | September 30, 2011 |
| | (In thousands) | | | |
| Gross gains | \$12 | \$36 | \$ 57 | \$ 287 |
| Gross losses | - | - | (189) | (12) |
| Write-down of carrying value | (82) | (176) | (285) | (176) |
| Total | \$(70) | \$(140) | \$ (417) | \$ 99 |

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8. Stock-Based Compensation

For the three months ended September 30, 2012 and 2011, the Company's net income, as reported, included \$0.6 million and \$0.4 million, respectively, of stock-based compensation costs and \$0.3 million and \$0.2 million, respectively, of income tax benefits related to the stock-based compensation plans. For the nine months ended September 30, 2012 and 2011, the Company's net income, as reported, included \$2.9 million and \$2.1 million, respectively, of stock-based compensation costs and \$1.1 million and \$0.8 million, respectively, of income tax benefits related to the stock-based compensation plans.

The Company estimates the fair value of stock options using the Black-Scholes valuation model. Key assumptions used to estimate the fair value of stock options include the exercise price of the award, the expected option term, the expected volatility of the Company's stock price, the risk-free interest rate over the options' expected term and the annual dividend yield. The Company uses the fair value of the common stock on the date of award to measure compensation cost for restricted stock unit awards. Compensation cost is recognized over the vesting period of the award using the straight line method. There were no restricted stock units granted during the three months ended September 30, 2012. During the three months ended September 30, 2011, the Company granted 1,000 restricted stock units. During the nine months ended September 30, 2012 and 2011, the Company granted 230,675 and 214,095 restricted stock units, respectively. There were no stock options granted during the three and nine month periods ended September 30, 2012 and 2011.

The 2005 Omnibus Incentive Plan ("Omnibus Plan") became effective on May 17, 2005 after approval by the stockholders. The Omnibus Plan authorizes the Compensation Committee of the Company's Board of Directors (the "Compensation Committee") to grant a variety of equity compensation awards as well as long-term and annual cash incentive awards, all of which can be structured so as to comply with Section 162(m) of the Internal Revenue Code of 1986, as amended (the "Internal Revenue Code"). On May 17, 2011, stockholders approved an amendment to the Omnibus Plan authorizing an additional 625,000 shares for use for full value awards. As of September 30, 2012, there are 539,027 shares available for full value awards and 49,580 shares available for non-full value awards. To satisfy stock option exercises or fund restricted stock and restricted stock unit awards, shares are issued from treasury stock, if available, otherwise new shares are issued. The Company will maintain separate pools of available shares for full value as opposed to non-full value awards, except that shares can be moved from the non-full value pool to the full value pool on a 3-for-1 basis. The exercise price per share of a stock option grant may not be less than the fair market value of the common stock of the Company, as defined in the Omnibus Plan, on the date of grant and may not be re-priced without the approval of the Company's stockholders. Options, stock appreciation rights, restricted stock, restricted stock units and other stock based awards granted under the Omnibus Plan are generally subject to a minimum vesting period of three years with stock options having a 10-year contractual term. Other awards do not have a contractual term of expiration. Restricted stock unit awards include participants who have reached or are close to reaching retirement eligibility, at which time such awards fully vest. These amounts are included in stock-based compensation expense.

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

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

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The following table summarizes the Company's full value awards at or for the nine months ended September 30, 2012:

| Full Value Awards | Shares | Weighted-Average Grant-Date Fair Value |
|---|-----------|--|
| Non-vested at December 31, 2011 | 363,589 | \$ 13.52 |
| Granted | 230,675 | 13.28 |
| Vested | (201,494) | 13.62 |
| Forfeited | (6,809) | 13.59 |
| Non-vested at September 30, 2012 | 385,961 | \$ 13.32 |
| Vested but unissued at September 30, 2012 | 147,176 | \$ 13.43 |

As of September 30, 2012, there was \$3.6 million of total unrecognized compensation cost related to non-vested full value awards granted under the Omnibus Plan. That cost is expected to be recognized over a weighted-average period of 3.2 years. The total fair value of awards vested for the three months ended September 30, 2012 and 2011 were \$2,000 and \$3,000, respectively. The total fair value of awards vested for the nine months ended September 30, 2012 and 2011 were \$2.7 million and \$1.7 million, respectively. The vested but unissued full value awards consist of awards made to employees and directors who are eligible for retirement. According to the terms of the Omnibus Plan, these employees and directors have no risk of forfeiture. These shares will be issued at the original contractual vesting dates.

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

The following table summarizes certain information regarding the non-full value awards, all of which have been granted as stock options, at or for the nine months ended September 30, 2012:

| Non-Full Value Awards | Shares | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term | Aggregate Intrinsic Value \$(000) * |
|---|-----------|---------------------------------------|--|--|
| Outstanding at December 31, 2011 | 975,640 | \$ 15.16 | | |
| Granted | - | - | | |
| Exercised | (138,025) | 12.10 | | |
| Forfeited | (48,200) | 12.87 | | |
| Outstanding at September 30, 2012 | 789,415 | \$ 15.84 | 3.2 | \$ 990 |
| Exercisable shares at September 30, 2012 | 727,275 | \$ 16.22 | 3.0 | \$ 658 |
| Vested but unexercisable shares at September 30, 2012 | 11,120 | \$ 11.59 | 6.2 | \$ 58 |

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

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As of September 30, 2012, there was \$0.1 million of total unrecognized compensation cost related to unvested non-full value awards granted under the Omnibus Plan. That cost is expected to be recognized over a weighted-average period of 0.9 years. The vested but unexercisable non-full value awards were made to employees who are eligible for retirement. According to the terms of the Omnibus Plan, these employees have no risk of forfeiture. These awards will be exercisable at the original contractual vesting dates.

Cash proceeds, fair value received, tax benefits, intrinsic value related to stock options exercised and the weighted average grant date fair value for options granted during the nine months ended September 30, 2012 are provided in the following table:

| (In thousands) | For the three months ended | | For the nine months ended | |
|---|----------------------------|--------------------|---------------------------|--------------------|
| | September 30, 2012 | September 30, 2011 | September 30, 2012 | September 30, 2011 |
| Proceeds from stock options exercised | \$ 21 | \$ 22 | \$ 835 | \$ 2,039 |
| Fair value of shares received upon exercised of stock options | 287 | - | 835 | 54 |
| Tax benefit related to stock options exercised | 3 | 1 | 30 | 184 |
| Intrinsic value of stock options exercised | 56 | 7 | 186 | 426 |

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

The following table summarizes the Phantom Stock Plan at or for the nine months ended September 30, 2012:

| Phantom Stock Plan | Shares | Fair Value |
|-----------------------------------|--------|------------|
| Outstanding at December 31, 2011 | 39,255 | \$ 12.63 |
| Granted | 11,209 | 13.24 |
| Forfeited | - | - |
| Distributions | (491) | 13.11 |
| Outstanding at September 30, 2012 | 49,973 | \$ 15.80 |

Vested at September 30, 2012

49,599 \$ 15.80

The Company recorded stock-based compensation expense for the Phantom Stock Plan of \$114,000 and \$79,000 for the three months ended September 30, 2012 and 2011, respectively. The total fair value of the distributions from the Phantom Stock Plan was \$1,000 for the three months ended September 30, 2012 and 2011.

For the nine months ended September 30, 2012 and 2011, the Company recorded stock-based compensation expense (benefit) for the Phantom Stock Plan of \$171,000 and \$(110,000), respectively. The total fair value of the distributions from the Phantom Stock Plan during the nine months ended September 30, 2012 and 2011 were \$6,000 and \$2,000, respectively.

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9. Pension and Other Postretirement Benefit Plans

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

| (In thousands) | Three months ended September 30, | | Nine months ended September 30, | |
|--|-------------------------------------|--------|------------------------------------|--------|
| | 2012 | 2011 | 2012 | 2011 |
| Employee Pension Plan: | | | | |
| Interest cost | \$220 | \$246 | \$660 | \$738 |
| Amortization of unrecognized loss | 263 | 153 | 789 | 459 |
| Expected return on plan assets | (310) | (308) | (930) | (924) |
| Net employee pension expense | \$173 | \$91 | \$519 | \$273 |
| Outside Director Pension Plan: | | | | |
| Service cost | \$20 | \$17 | \$60 | \$51 |
| Interest cost | 28 | 31 | 84 | 93 |
| Amortization of unrecognized gain | (7) | (13) | (21) | (39) |
| Amortization of past service liability | 9 | 10 | 27 | 30 |
| Net outside director pension expense | \$50 | \$45 | \$150 | \$135 |
| Other Postretirement Benefit Plans: | | | | |
| Service cost | \$100 | \$78 | \$300 | \$234 |
| Interest cost | 54 | 52 | 162 | 156 |
| Amortization of unrecognized loss | 10 | - | 30 | - |
| Amortization of past service credit | (21) | (21) | (63) | (63) |
| Net other postretirement expense | \$143 | \$109 | \$429 | \$327 |

The Company previously disclosed in its Consolidated Financial Statements for the year ended December 31, 2011 that it expects to contribute \$0.5 million to the Company's Employee Pension Plan (the "Employee Pension Plan") and \$0.2 million to each of the Outside Director Pension Plan (the "Outside Director Pension Plan") and the other postretirement benefit plans (the "Other Postretirement Benefit Plans") during the year ending December 31, 2012. As of September 30, 2012, the Company has contributed \$0.6 million to the Employee Pension Plan, \$66,000 to the Outside Director Pension Plan and \$50,000 to the Other Postretirement Benefit Plans. As of September 30, 2012, the Company has revised its expected contribution for the Employee Pension Plan to \$0.7 million for the year ending December 31, 2012. As of September 30, 2012, the Company has not revised its expected contributions for the Outside Director Pension Plan and the Other Postretirement Benefit Plans for the year ending December 31, 2012.

10. Fair Value of Financial Instruments

The Company carries certain financial assets and financial liabilities at fair value in accordance with ASC Topic 825, "Financial Instruments" ("ASC Topic 825") and values those financial assets and financial liabilities in accordance with ASC Topic 820, "Fair Value Measurements and Disclosures" ("ASC Topic 820"). ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market

participants at the measurement date, establishes a framework for measuring fair value and expands disclosures about fair value measurements. ASC Topic 825 permits entities to choose to measure many financial instruments and certain other items at fair value. At September 30, 2012, the Company carried financial assets and financial liabilities under the fair value option with fair values of \$57.6 million and \$23.7 million, respectively. At December 31, 2011, the Company carried financial assets and financial liabilities under the fair value option with fair values of \$68.7 million and \$26.3 million, respectively. During the nine months ended September 30, 2012, the Company did not elect to carry any additional financial assets or financial liabilities under the fair value option. The Company elected to measure at fair value securities with a cost of \$10.0 million that were purchased during the nine months ended September 30, 2011.

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

| | Fair Value Measurements at September 30, | Fair Value Measurements at December 31, | Changes in Fair Values For Items Measured at Fair Value Pursuant to Election of the Fair Value Option | | | |
|---|---|--|---|-----------------------|---------------------------------------|-----------------------|
| | | | Three Months Ended September 30, | | Nine Months Ended September 30, | |
| (In thousands) | 2012 | 2011 | 2012 | September 30, 2011 | September 30, 2012 | September 30, 2011 |
| Mortgage-backed securities | \$ 28,365 | \$ 37,787 | \$ (14) | \$ (159) | \$ (175) | \$ (554) |
| Other securities | 29,226 | 30,942 | 325 | (364) | 571 | (1,133) |
| Borrowed funds | 23,709 | 26,311 | 374 | 3,517 | 2,279 | 5,038 |
| Net gain from fair value adjustments (1) (2) | | | \$ 685 | \$ 2,994 | \$ 2,675 | \$ 3,351 |

- (1) The net gain from fair value adjustments presented in the above table does not include net gains (losses) of \$0.1 million and (\$0.9) million for the three months ended September 30, 2012 and 2011, respectively, from the change in the fair value of interest rate caps/swaps.
- (2) The net gain from fair value adjustments presented in the above table does not include net losses of \$2.9 million and \$2.1 million for the nine months ended September 30, 2012 and 2011, respectively, from the change in the fair value of interest rate caps/swaps.

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

The borrowed funds had a contractual principal amount of \$61.9 million at September 30, 2012 and December 31, 2011. The fair value of borrowed funds includes accrued interest payable of \$0.1 million and \$0.4 million at September 30, 2012 and December 31, 2011, respectively.

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

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

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

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

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

Level 1 – where quoted market prices are available in an active market. The Company did not value any of its assets or liabilities that are carried at fair value on a recurring basis as Level 1 at September 30, 2012 and December 31, 2011.

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Level 2 – when quoted market prices are not available, fair value is estimated using quoted market prices for similar financial instruments and adjusted for differences between the quoted instrument and the instrument being valued. Fair value can also be estimated by using pricing models, or discounted cash flows. Pricing models primarily use market-based or independently sourced market parameters as inputs, including, but not limited to, yield curves, interest rates, equity or debt prices and credit spreads. In addition to observable market information, models also incorporate maturity and cash flow assumptions. At September 30, 2012, Level 2 included mortgage related securities, corporate debt and interest rate caps/swaps. At December 31, 2011, Level 2 included mortgage related securities, corporate debt and interest rate caps.

Level 3 – when there is limited activity or less transparency around inputs to the valuation, financial instruments are classified as Level 3. At September 30, 2012 and December 31, 2011, Level 3 included trust preferred securities owned by and junior subordinated debentures issued by the Company.

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

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

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

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The following table sets forth the assets and liabilities that are carried at fair value on a recurring basis and the method that was used to determine their fair value, at September 30, 2012 and December 31, 2011:

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | | Significant Other Observable Inputs (Level 2) | | Significant Other Unobservable Inputs (Level 3) | | Total carried at fair value on a recurring basis | |
|----------------------------|--|-------------------------|---|-------------------------|---|-------------------------|--|-------------------------|
| | September 30, 2012 | December 31, 2011 | September 30, 2012 | December 31, 2011 | September 30, 2012 | December 31, 2011 | September 30, 2012 | December 31, 2011 |
| | (in thousands) | | | | | | | |
| Assets: | | | | | | | | |
| Mortgage-backed Securities | \$ - | \$ - | \$ 728,537 | \$ 747,288 | \$ - | \$ - | 728,537 | 747,288 |
| Other securities | - | - | 226,863 | 59,610 | 6,096 | 5,632 | 232,959 | 65,242 |
| Interest rate caps | - | - | 41 | 356 | - | - | 41 | 356 |
| Total assets | \$ - | \$ - | \$ 955,441 | \$ 807,254 | \$ 6,096 | \$ 5,632 | \$ 961,537 | \$ 812,886 |
| Liabilities: | | | | | | | | |
| Borrowings | | \$ - | | \$ - | \$ 23,709 | \$ 26,311 | \$ 23,709 | \$ 26,311 |
| Interest rate swaps | | - | 2,546 | - | - | - | 2,546 | - |
| Total liabilities | \$ - | \$ - | \$ 2,546 | \$ - | \$ 23,709 | \$ 26,311 | \$ 26,255 | \$ 26,311 |

The following table sets forth the Company's assets that are carried at fair value on a non-recurring basis and the method that was used to determine their fair value, at September 30, 2012 and December 31, 2011:

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | | Significant Other Observable Inputs (Level 2) | | Significant Other Unobservable Inputs (Level 3) | | Total carried at fair value on a non-recurring basis | |
|---------------------|--|-------------------------|---|-------------------------|---|-------------------------|---|-------------------------|
| | September 30, 2012 | December 31, 2011 | September 30, 2012 | December 31, 2011 | September 30, 2012 | December 31, 2011 | September 30, 2012 | December 31, 2011 |
| | (in thousands) | | | | | | | |
| Assets: | | | | | | | | |
| Loans held for sale | \$- | \$ - | \$- | \$ - | \$ 8,780 | \$ - | \$ 8,780 | \$ - |
| Impaired loans | - | - | - | - | 58,858 | 48,555 | 58,858 | 48,555 |
| | - | - | - | - | 3,660 | 3,179 | 3,660 | 3,179 |

Other Real Estate
Owned

| | | | | | | | | |
|--------------|-----|------|-----|------|----------|-----------|-----------|-----------|
| Total assets | \$- | \$ - | \$- | \$ - | \$71,298 | \$ 51,734 | \$ 71,298 | \$ 51,734 |
|--------------|-----|------|-----|------|----------|-----------|-----------|-----------|

The Company did not have any liabilities that were carried at fair value on a non-recurring basis at September 30, 2012 and December 31, 2011.

The estimated fair value of each material class of financial instruments at September 30, 2012 and December 31, 2011 and the related methods and assumptions used to estimate fair value are as follows:

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

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

FHLB-NY stock:

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

Securities Available for Sale:

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

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Loans held for sale:

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

Loans:

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

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

Due to Depositors:

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

Borrowings:

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

Interest Rate Caps:

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

Interest Rate Swaps:

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

Other Real Estate Owned:

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

Other Financial Instruments:

The fair values of commitments to sell, lend or borrow are estimated using the fees currently charged or paid to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of

the counterparties or on the estimated cost to terminate them or otherwise settle with the counterparties at the reporting date. For fixed-rate loan commitments to sell, lend or borrow, fair values also consider the difference between current levels of interest rates and committed rates (where applicable).

At September 30, 2012 and December 31, 2011, the fair values of the above financial instruments approximate the recorded amounts of the related fees and were not considered to be material.

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The following table sets forth the carrying amounts and estimated fair values of selected financial instruments as well as assumptions used by the Company in estimating fair value at September 30, 2012 and December 31, 2011:

| | Carrying Amount | September 30, 2012 | | | | December 31, 2011 | |
|----------------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|--------------------|
| | | Fair Value | Level 1 | Level 2 | Level 3 | Carrying Amount | Fair Value |
| (in thousands) | | | | | | | |
| Assets: | | | | | | | |
| Cash and due from banks | \$36,098 | \$36,098 | \$36,098 | \$- | \$- | \$55,721 | \$55,721 |
| Mortgage-backed Securities | 728,537 | 728,537 | - | 728,537 | - | 747,288 | 747,288 |
| Other securities | 232,959 | 232,959 | - | 226,863 | 6,096 | 65,242 | 65,242 |
| Loans held for sale | 8,780 | 8,780 | - | - | 8,780 | - | - |
| Loans | 3,186,648 | 3,408,588 | - | - | 3,408,588 | 3,228,881 | 3,407,454 |
| FHLB-NY stock | 35,002 | 35,002 | - | 35,002 | - | 30,245 | 30,245 |
| Interest rate caps | 41 | 41 | - | 41 | - | 356 | 356 |
| OREO | 3,660 | 3,660 | - | - | 3,660 | 3,179 | 3,179 |
| Total assets | \$4,231,725 | \$4,453,665 | \$36,098 | \$990,443 | \$3,427,124 | \$4,130,912 | \$4,309,485 |
| Liabilities: | | | | | | | |
| Deposits | \$3,110,035 | 3,168,929 | \$1,627,780 | \$1,541,149 | \$- | \$3,146,245 | \$3,211,405 |
| Borrowings | 784,906 | 832,479 | - | 808,770 | 23,709 | 685,139 | 728,067 |
| Interest rate swaps | 2,546 | 2,546 | - | 2,546 | - | - | - |
| Total liabilities | \$3,897,487 | \$4,003,954 | \$1,627,780 | \$2,352,465 | \$23,709 | \$3,831,384 | \$3,939,472 |

11. Derivative Financial Instruments

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

These derivatives are not designated as hedges and have a combined notional amount of \$118.0 million at September 30, 2012. Changes in the fair value of these derivatives are reflected in "Net loss from fair value adjustments" in the Consolidated Statements of Income.

The following table sets forth information regarding the Company's derivative financial instruments at September 30, 2012:

| | Notional | September 30, 2012 Cumulative | Net Gain |
|--|----------|----------------------------------|----------|
|--|----------|----------------------------------|----------|

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| | Amount | Purchase Price | Unrealized | | (loss) Position (1) |
|---------------------|-----------|-------------------|------------|----------|------------------------|
| | | | Gain | Loss | |
| (In thousands) | | | | | |
| Interest rate caps | \$100,000 | \$ 9,035 | \$- | \$8,994 | \$ 41 |
| Interest rate swaps | 18,000 | - | - | 2,546 | (2,546) |
| Total derivatives | \$118,000 | \$ 9,035 | \$- | \$11,540 | \$ (2,505) |

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

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The following table displays a summary of the terms of the interest rate caps and interest rate swaps currently held by the Company:

| | Interest Rate Cap 1 | Interest Rate Cap 2 | Interest Rate Swap 1 | Interest Rate Swap 2 | Interest Rate Swap 3 |
|--------------------------------------|---------------------------|------------------------|-------------------------|----------------------------|-------------------------|
| | (Dollars in thousands) | | | | |
| Notional Amount | \$50,000 | \$ 50,000 | \$ 6,000 | \$ 6,000 | \$ 6,000 |
| Trade Date | August 12, 2009 | August 24, 2009 | March 19, 2012 | March 20, 2012 | March 20, 2012 |
| Effective Date | August 14, 2009 | August 26, 2009 | September 1, 2012 | July 30, 2012 | June 15, 2012 |
| Fixed Rate Paid By Savings Bank | n/a | n/a | 3.18 % | 3.21 % | 3.22 % |
| Adjustable rate paid by counterparty | 3 month LIBOR | 3 month LIBOR | 3 month LIBOR | 3 month LIBOR | 3 month LIBOR |
| Strike price (3 month LIBOR) | 1.47 % | 1.47 % | n/a | n/a | n/a |
| Maturity Date | August 14, 2014 | August 26, 2014 | September 1, 2037 | July 30, 2037 | September 15, 2037 |

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

| (In thousands) | Three months ended September 30, | | Nine months ended September 30, | |
|------------------------|-------------------------------------|----------|------------------------------------|------------|
| | 2012 | 2011 | 2012 | 2011 |
| Financial Derivatives: | | | | |
| Interest rate caps | \$(52) | \$(909) | \$(314) | \$(2,086) |
| Interest rate swaps | 192 | - | (2,546) | - |
| Net gain (loss) | \$140 | \$(909) | \$(2,860) | \$(2,086) |

12. Income Taxes

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

Income tax provisions are summarized as follows:

| (In thousands) | For the Three months ended September 30, | | For the Nine months ended September 30, | |
|----------------|---|---------|--|----------|
| | 2012 | 2011 | 2012 | 2011 |
| Federal: | | | | |
| Current | \$4,578 | \$4,959 | \$12,807 | \$13,825 |

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| | | | | |
|-------------------------------------|---------|---------|----------|----------|
| Deferred | (35) | 140 | (404) | (250) |
| Total federal tax provision | 4,543 | 5,099 | 12,403 | 13,575 |
| State and Local: | | | | |
| Current | 1,460 | 1,564 | 3,793 | 4,316 |
| Deferred | (15) | 93 | (131) | (86) |
| Total state and local tax provision | 1,445 | 1,657 | 3,662 | 4,230 |
| Total income tax provision | \$5,988 | \$6,756 | \$16,065 | \$17,805 |

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The income tax provision in the Consolidated Statements of Income has been provided at effective rates of 39.0% and 40.0% for the three months ended September 30, 2012 and 2011, respectively, and 39.0% and 39.6% for the nine months ended September 30, 2012 and 2011, respectively.

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

| (dollars in thousands) | For the three months ended September 30, | | | For the nine months ended September 30, | | | | |
|---|---|--------|---------|--|----------|--------|----------|--------|
| | 2012 | 2011 | | 2012 | 2011 | | | |
| Taxes at federal statutory rate | \$5,374 | 35.0 % | \$5,917 | 35.0 % | \$14,419 | 35.0 % | 15,744 | 35.0 % |
| Increase (reduction) in taxes resulting from: | | | | | | | | |
| State and local income tax, net of Federal income tax benefit | 938 | 6.1 | 1,078 | 6.4 | 2,380 | 5.8 | 2,750 | 6.1 |
| Other | (324) | (2.1) | (239) | (1.4) | (734) | (1.8) | (689) | (1.5) |
| Taxes at effective rate | \$5,988 | 39.0 % | \$6,756 | 40.0 % | \$16,065 | 39.0 % | \$17,805 | 39.6 % |

The Company has recorded a deferred tax asset of \$33.8 million at September 30, 2012, which is included in “Other liabilities” in the Consolidated Statements of Financial Condition. This represents the anticipated net federal, state and local tax benefits expected to be realized in future years upon the utilization of the underlying tax attributes comprising this balance. The Company has reported taxable income for federal, state, and local tax purposes in each of the past three fiscal years. In management’s opinion, in view of the Company’s previous, current and projected future earnings trend, the probability that some of the Company’s \$36.2 million deferred tax liability can be used to offset a portion of the deferred tax asset, as well as certain tax planning strategies, it is more likely than not that the deferred tax asset will be fully realized. Accordingly, no valuation allowance was deemed necessary for the deferred tax asset at September 30, 2012.

13. Accumulated Other Comprehensive Income:

The components of accumulated other comprehensive income at September 30, 2012 and December 31, 2011 and the changes during the periods are as follows:

| | September 30, 2012 | Other Comprehensive Income (loss) | December 31, 2011 |
|---|--------------------------|---|-------------------------|
| | (In thousands) | | |
| Net unrealized gain on securities available for sale | \$20,365 | \$ 8,686 | \$ 11,679 |
| Net actuarial loss on pension plans and other postretirement benefits | (6,769) | 447 | (7,216) |
| Prior service cost on pension plans and other postretirement benefits | 331 | (19) | 350 |
| Accumulated other comprehensive income | \$13,927 | \$ 9,114 | \$ 4,813 |

14. Regulatory

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

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At September 30, 2012, the Savings Bank exceeded each of the three capital requirements and is categorized as “well-capitalized” under the prompt corrective action regulations. Set forth below is a summary of the Savings Bank’s compliance:

| (Dollars in thousands) | Amount | Percent of Assets | |
|-----------------------------------|-----------|----------------------|---|
| Core Capital: | | | |
| Capital level | \$421,146 | 9.69 | % |
| Well capitalized | 217,293 | 5.00 | |
| Excess | 203,853 | 4.69 | |
| Tier 1 Risk-Based Capital: | | | |
| Capital level | \$421,146 | 14.38 | % |
| Well capitalized | 175,693 | 6.00 | |
| Excess | 245,453 | 8.38 | |
| Risk-Based Capital: | | | |
| Capital level | \$451,833 | 15.43 | % |
| Well capitalized | 292,804 | 10.00 | |
| Excess | 159,029 | 5.43 | |

15. New Authoritative Accounting Pronouncements

In April 2011, the FASB issued ASU No. 2011-03, which amends the authoritative accounting guidance under ASC Topic 860 “Transfers and Servicing.” The amendments in this update remove from the assessment of effective control (1) the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms, even in the event of default by the transferee and (2) the collateral maintenance implementation guidance related to that criterion. The amendments in this update are effective for the first interim or annual period beginning on or after December 15, 2011 and should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted. Adoption of this update did not have a material effect on the Company’s consolidated results of operations or financial condition.

In May 2011, the FASB issued ASU No. 2011-04, which amends the authoritative accounting guidance under ASC Topic 820 “Fair Value Measurement.” The amendments in this update clarify how to measure and disclose fair value under ASC Topic 820. The amendments in this update are effective for the first interim or annual period beginning on or after December 15, 2011 and should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted. Adoption of this update did not have a material effect on the Company’s consolidated results of operations or financial condition.

In June 2011, the FASB issued ASU No. 2011-05, which amends the authoritative accounting guidance under ASC Topic 220 “Comprehensive Income.” The amendments eliminate the option to present components of other comprehensive income in the statement of stockholders’ equity. Instead, the new guidance requires entities to present all nonowner changes in stockholders’ equity either as a single continuous statement of comprehensive income or as two separate but consecutive statements. The amendments in this update are effective for the first interim or annual

period beginning on or after December 15, 2011 and must be applied retrospectively. Early adoption is permitted. Adoption of this update did not have a material effect on the Company's consolidated results of operations or financial condition. See the Consolidated Statements of Comprehensive Income.

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In September 2011, the FASB issued ASU No. 2011-08, which amends the authoritative accounting guidance under ASC Topic 350 “Intangibles – Goodwill and Other.” The amendments in the update permit an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in Topic 350. The more-likely-than-not threshold is defined as having a likelihood of more than 50 percent. The amendments in this update are effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity’s financial statements for the most recent annual or interim period have not yet been issued. Adoption of this update did not have a material effect on the Company’s consolidated results of operations or financial condition.

16. Subsequent Events

On October 29 and 30, 2012, the New York City metropolitan area suffered severe damage from Hurricane Sandy. The Company continues to assess the impact of the storm on the Company's facilities, operations and customers in the affected areas and what impact, if any, the storm could have on the Company's results of operations for the fourth quarter of 2012.

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

This Quarterly Report should be read in conjunction with the more detailed and comprehensive disclosures included in our Annual Report on Form 10-K for the year ended December 31, 2011. In addition, please read this section in conjunction with our Consolidated Financial Statements and Notes to Consolidated Financial Statements contained herein.

As used in this Quarterly Report, the words “we,” “us,” “our” and the “Company” are used to refer to Flushing Financial Corporation and its direct and indirect wholly-owned subsidiaries, Flushing Savings Bank, FSB (the “Savings Bank”), Flushing Commercial Bank (the “Commercial Bank,” and together with the Savings Bank, the “Banks”), Flushing Preferred Funding Corporation, Flushing Service Corporation and FSB Properties, Inc.

Statements contained in this Quarterly Report relating to plans, strategies, objectives, economic performance and trends, projections of results of specific activities or investments and other statements that are not descriptions of historical facts may be forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking information is inherently subject to risks and uncertainties and actual results could differ materially from those currently anticipated due to a number of factors, which include, but are not limited to, factors discussed elsewhere in this Quarterly Report and in other documents filed by us with the Securities and Exchange Commission from time to time, including, without limitation, our Annual Report on Form 10-K for the year ended December 31, 2011. Forward-looking statements may be identified by terms such as “may,” “will,” “should,” “could,” “expects,” “plans,” “intends,” “anticipates,” “believes,” “estimates,” “predicts,” “forecasts,” “continues,” “may continue” or similar terms or the negative of these terms. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We have no obligation to update these forward-looking statements.

Executive Summary

We are a Delaware corporation organized in May 1994 at the direction of the Savings Bank. The Savings Bank was organized in 1929 as a New York State chartered mutual savings bank. In 1994, the Savings Bank converted to a federally chartered mutual savings bank and changed its name from Flushing Savings Bank to Flushing Savings Bank, FSB. The Savings Bank converted from a federally chartered mutual savings bank to a federally chartered stock savings bank in 1995. On July 21, 2011, as a result of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the Savings Bank’s primary regulator became the Office of the Comptroller of the Currency (“OCC”). The Banks’ deposits are insured to the maximum allowable amount by the Federal Deposit Insurance Corporation (“FDIC”). The primary business of Flushing Financial Corporation at this time is the operation of its wholly owned subsidiary, the Savings Bank. The Savings Bank owns four subsidiaries: Flushing Commercial Bank, Flushing Preferred Funding Corporation, Flushing Service Corporation and FSB Properties Inc. In November 2006, the Savings Bank launched an internet branch, iGObanking.com®. The activities of Flushing Financial Corporation are primarily funded by dividends, if any, received from the Savings Bank, issuances of junior subordinated debt and issuances of equity securities. Flushing Financial Corporation’s common stock is traded on the NASDAQ Global Select Market under the symbol “FFIC.”

On October 11, 2012, the Savings Bank filed an application with the New York State Department of Financial Services (“NYDFS”) to combine with the Commercial Bank which will have the effect of converting the Savings Bank

from a federally-chartered savings bank to a New York State-chartered commercial bank. Prior to or simultaneously with the combination, Flushing Commercial Bank's charter will be amended such that the Commercial Bank will become a full-service commercial bank, rather than a limited purpose commercial bank, which it currently is, and its name will be changed to "Flushing Bank." The Savings Bank also filed a notice of the proposed combination and charter change with the OCC, and filed an application with respect to the combination with the Federal Deposit Insurance Corporation. In due course, the Company will be filing an application with the Federal Reserve to change from a savings and loan holding company to a bank holding company under federal banking laws in connection with the transaction.

Subject to receiving the necessary regulatory approvals, the Savings Bank and the Commercial Bank will be combined, and the resulting combined institution will be a full service New York State-chartered commercial bank operating under the name "Flushing Bank," and the Company will be a bank holding company under the Bank Holding Company Act of 1956, as amended. After the combination, the NYSDFS, which is currently the primary regulator of the Commercial Bank, will become the primary regulator of the combined bank, Flushing Bank, and the FDIC, which is currently the primary federal regulator of the Commercial Bank, will become the primary federal regulator of Flushing Bank. The Federal Reserve will remain the Company's primary federal regulator. The transaction is expected to be completed in either the fourth quarter of 2012 or the first quarter of 2013.

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Our principal business is attracting retail deposits from the general public and investing those deposits together with funds generated from ongoing operations and borrowings, primarily in (1) originations and purchases of multi-family residential properties and business loans and, to a lesser extent, one-to-four family (focusing on mixed-use properties, which are properties that contain both residential dwelling units and commercial units) and commercial real estate mortgage loans; (2) construction loans, primarily for residential properties; (3) Small Business Administration (“SBA”) loans; (4) mortgage loan surrogates such as mortgage-backed securities; and (5) U.S. government securities, corporate fixed-income securities and other marketable securities. We also originate certain other consumer loans including overdraft lines of credit.

Our results of operations depend primarily on net interest income, which is the difference between the income earned on its interest-earning assets and the cost of our interest-bearing liabilities. Net interest income is the result of our interest rate margin, which is the difference between the average yield earned on interest-earning assets and the average cost of interest-bearing liabilities, adjusted for the difference in the average balance of interest-earning assets compared to the average balance of interest-bearing liabilities. We also generate non-interest income from loan fees, service charges on deposit accounts, mortgage servicing fees, and other fees, income earned on Bank Owned Life Insurance (“BOLI”), dividends on Federal Home Bank of New York (“FHLB-NY”) stock and net gains and losses on sales of securities and loans. Our operating expenses consist principally of employee compensation and benefits, occupancy and equipment costs, other general and administrative expenses and income tax expense. Our results of operations also can be significantly affected by our periodic provision for loan losses and specific provision for losses on real estate owned.

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

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

- manage enterprise-wide risk.

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

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

We carry a portion of our financial assets and financial liabilities at fair value and record changes in their fair value through earnings in non-interest income on our Consolidated Statements of Income and Comprehensive Income. A description of the financial assets and financial liabilities that are carried at fair value through earnings can be found in Note 9 of the Notes to the Consolidated Financial Statements.

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Credit quality improved during the third quarter of 2012 as we saw reductions in all areas of problem loans. Non-performing loans decreased by \$11.4 million, or 10%, to \$100.8 million. Loans delinquent over 30 days decreased \$12.2 million, or 7%, during the third quarter, and are at their lowest level since the third quarter of 2009. Loans delinquent over 90 days decreased \$14.0 million, or 13%, and are at their lowest level since the first quarter of 2010. Classified assets and criticized assets continued their improving trend that began over a year ago, which resulted in a 9% reduction in these categories in the third quarter of 2012, a 20% reduction in the nine months ended September 30, 2012, and a 28% reduction since December 31, 2010.

Our net interest margin for the third quarter of 2012 was 3.62%, an increase of two basis points from 3.60% in the third quarter of 2011, but a decrease of six basis points from 3.68% in the second quarter of 2012. Excluding prepayment penalty income received on loans and mortgage-backed securities, our net interest margin for the third quarter of 2012 was 3.48%, a decrease of 11 basis points from 3.59% for the second quarter of 2012. While we saw a decrease in our funding costs of four basis points for the quarter, excluding prepayment penalty income, the yield on interest-earning assets decreased 16 basis points. In the current interest rate environment, new loans and securities are added at rates well below our portfolio average yield, and higher yielding loans and securities are prepaid. We also experienced significantly higher than average activity in loans refinancing during the third quarter of 2012, which further reduced the yield on our loan portfolio. In addition, an increase in the average balance of interest-earning deposits reduced our net interest margin by two basis points.

We recorded a provision for loan losses of \$16.0 million during the nine months ended September 30, 2012, which was an increase of \$1.0 million from \$15.0 million recorded during the nine months ended September 30, 2011. The provision was deemed necessary as a result of the regular quarterly analysis of the allowance for loan losses. The regular quarterly analysis is based on management’s evaluation of the risks inherent in the various components of the loan portfolio and other factors, including historical loan loss experience (which is updated quarterly), changes in the composition and volume of the portfolio, collection policies and experience, trends in the volume of non-accrual loans and local and national economic conditions. See “-ALLOWANCE FOR LOAN LOSSES.”

The Savings Bank continues to be well-capitalized under regulatory requirements, with Core, Tier 1 risk-based and Total risk-based capital ratios of 9.69%, 14.38% and 15.43%, respectively, at September 30, 2012.

COMPARISON OF OPERATING RESULTS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011

General. Net income for the three months ended September 30, 2012 was \$9.4 million, a decrease of \$0.8 million, or 7.7%, compared to \$10.2 million for the three months ended September 30, 2011. Diluted earnings per common share were \$0.31 for the three months ended September 30, 2012, a decrease of \$0.02, or 6.1%, from \$0.33 for the three months ended September 30, 2011. Return on average equity was 8.7% for the three months ended September 30, 2012 compared to 9.9% for the three months ended September 30, 2011. Return on average assets was 0.9% for the three month periods ended September 30, 2012 and 2011.

Interest Income. Total interest and dividend income decreased \$3.1 million, or 5.6%, to \$53.2 million for the three months ended September 30, 2012 from \$56.3 million for the three months ended September 30, 2011. The decrease in interest income was attributable to a 35 basis point decline in the yield of interest-earning assets to 5.12% for the three months ended September 30, 2012 from 5.47% in the comparable prior year period combined with a \$30.4 million decrease in the average balance of total loans to \$3,175.3 million for the three months ended September 30,

2012, from \$3,205.6 million for the comparable prior year period. The 35 basis point decline in the yield of interest-earning assets was primarily due to a 31 basis point reduction in the yield of the loan portfolio to 5.65% for the three months ended September 30, 2012 from 5.96% for the three months ended September 30, 2011, combined with a 48 basis point decline in the yield on total securities to 3.59% for the three months ended September 30, 2012 from 4.07% for the comparable prior year period. In addition, the yield of interest-earning assets was negatively impacted by a \$88.6 million increase in the average balances of the lower yielding securities portfolio for the three months ended September 30, 2012, as compared to the comparable prior year period. These factors that reduced the yield were partially offset by a \$17.6 million decrease in the average balance of lower yielding interest-earning deposits to \$56.8 million for the three months ended September 30, 2012 from \$74.4 million for the comparable prior year period. The 31 basis point decrease in the yield of the loan portfolio was primarily due to the current interest rate environment, as new loans are added at rates well below the portfolio average yield, and higher yielding loans are prepaid. In addition, we experienced significantly higher than average activity in loans refinancing during the third quarter of 2012. The yield on the mortgage loan portfolio decreased 12 basis points to 5.73% for the three months ended September 30, 2012 from 5.85% for the three months ended June 30, 2012. The yield on the mortgage loan portfolio, excluding prepayment penalty income, decreased 34 basis points to 5.60% for the three months ended September 30, 2012 from 5.94% for the three months ended September 30, 2011. The 48 basis point decrease in the securities portfolio yield was primarily due to the purchase of new securities at lower yields than the existing portfolio.

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Interest Expense. Interest expense decreased \$3.6 million, or 18.8%, to \$15.6 million for the three months ended September 30, 2012 from \$19.2 million for the three months ended September 30, 2011. The decrease in interest expense was due to the reduction in the cost of interest-bearing liabilities, which decreased 38 basis points to 1.65% for the three months ended September 30, 2012 from 2.03% for the comparable prior year period. The 38 basis point decrease in the cost of interest-bearing liabilities was primarily attributable to the Bank reducing the rates it pays on its deposit products and a reduction in the cost of borrowed funds. The cost of certificates of deposit, money market accounts, savings accounts and NOW accounts decreased 22 basis points, 35 basis points, 41 basis points and 19 basis points, respectively, for the three months ended September 30, 2012 from the comparable prior year period. This resulted in a decrease in the cost of due to depositors of 26 basis points to 1.36% for the three months ended September 30, 2012 from 1.62% for the three months ended September 30, 2011. The cost of borrowed funds decreased 101 basis points from the comparable prior year period to 2.82% for the three months ended September 30, 2012. This decrease in the cost of borrowed funds was primarily due to maturing borrowings being replaced at lower rates and new borrowings being obtained at lower rates, and adjustable rate borrowings resetting to a lower rate during the three months ended September 30, 2012.

Net Interest Income. For the three months ended September 30, 2012, net interest income was \$37.6 million, an increase of \$0.5 million, or 1.3%, from \$37.1 million for the three months ended September 30, 2011. The increase in net interest income was attributable to a three basis point increase in the net-interest spread to 3.47% for the three months ended September 30, 2012 from 3.44% for the three months ended September 30, 2011, combined with an increase of \$40.7 million in the average balance of interest-earning assets to \$4,157.8 million for the three months ended September 30, 2012 from \$4,117.1 million for the comparable prior year period. The yield on interest-earning assets decreased 35 basis points to 5.12% for the three months ended September 30, 2012 from 5.47% for the three months ended September 30, 2011. However, this was more than offset by a decline in the cost of funds of 38 basis points to 1.65% for the three months ended September 30, 2012 from 2.03% for the comparable prior year period. The net interest margin improved two basis points to 3.62% for the three months ended September 30, 2012 from 3.60% for the three months ended September 30, 2011. Excluding prepayment penalty income from loans and mortgage-backed securities, the net interest margin would have decreased six basis points to 3.48% for the three months ended September 30, 2012 from 3.54% for the three months ended September 30, 2011.

Provision for Loan Losses. A provision for loan losses of \$5.0 million was recorded for the three months ended September 30, 2012, which was the same as that recorded for the three months ended September 30, 2011. During the three months ended September 30, 2012, non-performing loans decreased \$11.4 million to \$100.8 million from \$112.2 million at June 30, 2012. Net charge-offs for the three months ended September 30, 2012 totaled \$5.2 million, or 66 basis points of average loans. During the three months ended September 30, 2012, the Bank sold 28 non-performing loans, with a book value of \$17.6 million. The current loan-to-value ratio for our non-performing loans collateralized by real estate was 58.1% at September 30, 2012. When we have obtained properties through foreclosure, we have been able to quickly sell the properties at amounts that approximate book value. We anticipate that we will continue to see low loss content in our loan portfolio. The Bank continues to maintain conservative underwriting standards. However, given the level of non-performing loans, the current economic uncertainties, and the charge-offs recorded in the third quarter of 2012, management, as a result of the regular quarterly analysis of the allowance for loans losses, deemed it necessary to record a \$5.0 million provision for possible loan losses in the third quarter of 2012. See “-ALLOWANCE FOR LOAN LOSSES.”

Non-Interest Income. Non-interest income for the three months ended September 30, 2012 was \$3.5 million, a decrease of \$0.8 million from \$4.3 million for the three months ended September 30, 2011. The decrease in

non-interest income was primarily due to a \$1.3 million decrease in net gains recorded from fair value adjustments, partially offset by a \$0.7 million decrease in other-than-temporary impairment (“OTTI”) charges recorded during the three months ended September 30, 2012 from the comparable prior year period.

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Non-Interest Expense. Non-interest expense was \$20.7 million for the three months ended September 30, 2012, an increase of \$1.3 million, or 6.4%, from \$19.5 million for the three months ended September 30, 2011. The increase was primarily due to the growth of the Bank over the past year, which included the opening of a new branch in January 2012. Salaries and benefits increased \$1.0 million for the three months ended September 30, 2012 compared to the three months ended September 30, 2011 primarily due to the opening of a new branch in 2012, an increase in stock based compensation expense and increased employee benefits expense. In addition, other operating expense and other real estate owned/foreclosure expense increased \$0.3 million and \$0.1 million, respectively. The efficiency ratio was 51.3% for the three months ended September 30, 2012 compared to 48.3% for the three months ended September 30, 2011.

Income before Income Taxes. Income before the provision for income taxes decreased \$1.6 million, or 9.2%, to \$15.4 million for the three months ended September 30, 2012 from \$16.9 million for the three months ended September 30, 2011 for the reasons discussed above.

Provision for Income Taxes. Income tax expense decreased \$0.8 million to \$6.0 million for the three months ended September 30, 2012 from \$6.8 million for the three months ended September 30, 2011. The effective tax rate was 39.0% and 40.0% for the three months ended September 30, 2012 and 2011, respectively.

COMPARISON OF OPERATING RESULTS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011

General. Net income for the nine months ended September 30, 2012 was \$25.1 million, a decrease of \$2.0 million, or 7.5%, compared to \$27.2 million for the nine months ended September 30, 2011. Diluted earnings per common share were \$0.82 for the nine months ended September 30, 2012, a decrease of \$0.06, or 6.8%, from \$0.88 for the nine months ended September 30, 2011. Return on average equity was 7.9% for the nine months ended September 30, 2012 compared to 9.1% for the nine months ended September 30, 2011. Return on average assets was 0.8% for the nine months ended September 30, 2012 and 2011.

Interest Income. Total interest and dividend income decreased \$7.9 million, or 4.6%, to \$162.0 million for the nine months ended September 30, 2012 from \$169.9 million for the nine months ended September 30, 2011. The decrease in interest income was attributable to a 28 basis point decline in the yield of interest-earning assets to 5.24% for the nine months ended September 30, 2012 from 5.52% in the comparable prior year period. The decrease in the yield was partially offset by a \$24.2 million increase in the average balance of interest-earning assets to \$4,125.5 million for the nine months ended September 30, 2012 from \$4,101.2 million for the comparable prior year period. The 28 basis point decline in the yield of interest-earning assets was primarily due to a 23 basis point reduction in the yield of the loan portfolio to 5.75% for the nine months ended September 30, 2012 from 5.98% for the nine months ended September 30, 2011, combined with a 49 basis point decline in the yield on total securities to 3.65% for the nine months ended September 30, 2012 from 4.14% for the comparable prior year period. In addition, the yield of interest-earning assets was negatively impacted by a \$33.9 million decrease in the average balance of the higher yielding loan portfolio for the nine months ended September 30, 2012 and a \$78.6 million increase in the average balances of the lower yielding securities portfolio for the nine months ended September 30, 2012. These factors that reduced the yield were partially offset by a \$20.5 million decrease in the average balance of lower yielding interest-earning deposits to \$43.9 million for the nine months ended September 30, 2012 from \$64.4 million for the comparable prior year period. The 23 basis point decrease in the loan portfolio was primarily due to the current interest rate environment, as new loans are added at rates well below the portfolio average yield, and higher yielding

loans are prepaid. In addition, we experienced a significantly higher than average activity in loans refinancing during the third quarter of 2012. The 49 basis point decrease in the securities portfolio was primarily due to new securities being purchased at lower yields than the existing portfolio. The yield on the mortgage loan portfolio decreased 22 basis points to 5.84% for the nine months ended September 30, 2012 from 6.06% for the nine months ended September 30, 2011. The yield on the mortgage loan portfolio, excluding prepayment penalty income, decreased 27 basis points to 5.71% for the nine months ended September 30, 2012 from 5.98% for the nine months ended September 30, 2011.

Interest Expense. Interest expense decreased \$10.0 million, or 17.1%, to \$48.8 million for the nine months ended September 30, 2012 from \$58.8 million for the nine months ended September 30, 2011. The decrease in interest expense was due to the reduction in the cost of interest-bearing liabilities, which decreased 35 basis points to 1.72% for the nine months ended September 30, 2012 from 2.07% for the comparable prior year period. The 35 basis point decrease in the cost of interest-bearing liabilities was primarily attributable to the Bank reducing the rates it pays on its deposit products. The cost of certificates of deposit, money market accounts, savings accounts and NOW accounts decreased 16 basis points, 25 basis points, 40 basis points and 21 basis points, respectively, for the nine months ended September 30, 2012 from the comparable prior year period. This resulted in a decrease in the cost of due to depositors of 22 basis points to 1.39% for the nine months ended September 30, 2012 from 1.61% for the nine months ended September 30, 2011. The cost of borrowed funds decreased 108 basis points to 3.12% for the nine months ended September 30, 2012 from 4.20% for the nine months ended September 30, 2011 with the average balance increasing \$56.6 million to \$749.9 million for the nine months ended September 30, 2012 from \$693.3 million for the nine months ended September 30, 2011. The decrease in the cost of borrowed funds was primarily due to maturing borrowings being replaced at lower rates and new borrowings being obtained at lower rates, and to a lesser extent adjustable rate borrowings resetting to a lower rate during the three months ended September 30, 2012.

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Net Interest Income. For the nine months ended September 30, 2012, net interest income was \$113.2 million, an increase of \$2.2 million, or 2.0%, from \$111.1 million for the nine months ended September 30, 2011. The increase in net interest income was attributable to a seven basis point increase in the net-interest spread to 3.52% for the nine months ended September 30, 2012 from 3.45% for the nine months ended September 30, 2011, combined with an increase of \$24.2 million in the average balance of interest-earning assets to \$4,125.5 million for the nine months ended September 30, 2012 from \$4,101.2 million for the comparable prior year period. The yield on interest-earning assets decreased 28 basis points to 5.24% for the nine months ended September 30, 2012 from 5.52% for the nine months ended September 30, 2011. However, this was more than offset by a decline in the cost of funds of 35 basis points to 1.72% for the nine months ended September 30, 2012 from 2.07% for the comparable prior year period. The net interest margin improved five basis points to 3.66% for the nine months ended September 30, 2012 from 3.61% for the nine months ended September 30, 2011. Excluding prepayment penalty income on loans and mortgage-backed securities, the net interest margin would have been 3.54% for the nine months ended September 30, 2012, a one basis point decline from the nine months ended September 30, 2011.

Provision for Loan Losses. A provision for loan losses of \$16.0 million was recorded for the nine months ended September 30, 2012, which was an increase of \$1.0 million from \$15.0 million recorded in the nine months ended September 30, 2011. During the nine months ended September 30, 2012, non-performing loans decreased \$16.6 million to \$100.8 million from \$117.4 million at December 31, 2011. Net charge-offs for the nine months ended September 30, 2012 totaled \$15.7 million, or 65 basis points of average loans. During the nine months ended September 30, 2012, the Bank sold 60 non-performing loans, with a book value of \$35.7 million. The current loan-to-value ratio for our non-performing loans collateralized by real estate was 58.1% at September 30, 2012. When we have obtained properties through foreclosure, we have been able to quickly sell the properties at amounts that approximate book value. We anticipate that we will continue to see low loss content in our loan portfolio. The Bank continues to maintain conservative underwriting standards. However, given the level of non-performing loans, the current economic uncertainties, and the charge-offs recorded during the nine months ended September 30, 2012, management, as a result of the regular quarterly analysis of the allowance for loans losses, deemed it necessary to record a \$16.0 million provision for possible loan losses for the nine months ended September 30, 2012. See “-ALLOWANCE FOR LOAN LOSSES.”

Non-Interest Income. Non-interest income for the nine months ended September 30, 2012 was \$6.5 million, a decrease of \$0.8 million, or 11.0% from \$7.3 million for the nine months ended September 30, 2011. The decrease was primarily due to a \$1.5 million decrease in net gains recorded from fair value adjustments, partially offset by a \$0.8 million decrease in OTTI charges recorded for the nine months ended September 30, 2012 from the comparable prior year period.

Non-Interest Expense. Non-interest expense was \$62.5 million for the nine months ended September 30, 2012, an increase of \$4.1 million, or 7.1%, from \$58.4 million for the nine months ended September 30, 2011. The increase was primarily due to the growth of the Bank over the past year, which included the opening of a new branch in January 2012. Salaries and benefits increased \$2.8 million for the nine months ended September 30, 2012 compared to the nine months ended September 30, 2011 primarily due to the opening of a new branch in January 2012, an increase in stock based compensation expense and increased employee benefits expense. Other operating expense for the nine months ended September 30, 2012 increased \$1.2 million primarily due to \$0.4 million in net losses recorded from the sale of other real estate owned (“OREO”) during the nine months ended September 30, 2012 compared to \$0.3 million in net gains from the sale of OREO recorded during the nine months ended September 30, 2011. In addition, other real estate owned/foreclosure expense increased \$0.6 million in the nine months ended September 30, 2012 compared to

the nine months ended September 30, 2011. The efficiency ratio was 51.2% for the nine months ended September 30, 2012 compared to 49.2% for the nine months ended September 30, 2011.

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Income before Income Taxes. Income before the provision for income taxes decreased \$3.8 million, or 8.4%, to \$41.2 million for the nine months ended September 30, 2012 from \$45.0 million for the nine months ended September 30, 2011 for the reasons discussed above.

Provision for Income Taxes. Income tax expense decreased \$1.7 million, or 9.8% to \$16.1 million for the nine months ended September 30, 2012 from \$17.8 million for the nine months ended September 30, 2011. The effective tax rate was 39.0% and 39.6% for the nine months ended September 30, 2012 and 2011, respectively.

FINANCIAL CONDITION

Assets. Total assets at September 30, 2012 were \$4,380.5 million, an increase of \$92.5 million, or 2.2%, from \$4,287.9 million at December 31, 2011. Total loans, net decreased \$42.6 million, during the nine months ended September 30, 2012 to \$3,156.0 million from \$3,198.5 million at December 31, 2011. Loan originations and purchases were \$433.2 million for the nine months ended September 30, 2012, an increase of \$150.0 million from \$283.3 million for the nine months ended September 30, 2011. During the nine months ended September 30, 2012, we continued to focus on the origination of multi-family properties and business loans with a full relationship and deemphasize non-owner occupied commercial real estate and construction lending. Loan applications in process have remained strong, totaling \$198.0 million at September 30, 2012 compared to \$194.4 million at December 31, 2011 and \$214.4 million at September 30, 2011.

The following table shows loan originations and purchases for the periods indicated. The table includes loan purchases of \$3.5 million and \$14.5 million for the nine months ended September 30, 2012 and 2011, respectively. There were no loans purchased during the three months ended September 30, 2012 and 2011.

| (In thousands) | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|---|-----------|--|-----------|
| | 2012 | 2011 | 2012 | 2011 |
| Multi-family residential | \$69,299 | \$61,038 | \$211,052 | \$161,518 |
| Commercial real estate | 1,943 | 4,050 | 21,756 | 7,062 |
| One-to-four family – mixed-use property | 3,474 | 5,907 | 13,955 | 18,552 |
| One-to-four family – residential | 7,382 | 8,362 | 18,076 | 15,571 |
| Co-operative apartments | 100 | - | 1,726 | - |
| Construction | 83 | 80 | 653 | 1,283 |
| Small Business Administration | 180 | 332 | 513 | 3,170 |
| Taxi Medallion | - | - | 3,464 | 26,234 |
| Commercial business and other | 68,452 | 26,158 | 162,053 | 49,875 |
| Total | \$150,913 | \$105,927 | \$433,248 | \$283,265 |

We continue to maintain conservative underwriting standards that include, among other things, a loan-to-value ratio of 75% or less and a debt coverage ratio of at least 125%. Multi-family residential, commercial real estate and one-to-four family mixed-use property mortgage loans originated during the three months ended September 30, 2012 had an average loan-to-value ratio of 42.4% and an average debt coverage ratio of 237%.

Non-performing assets totaled \$107.4 million at September 30, 2012, a decrease of \$15.7 million from \$123.2 million at December 31, 2011. Total non-performing assets as a percentage of total assets were 2.45% at September 30, 2012

compared to 2.87% at December 31, 2011. The ratio of allowance for loan losses to total non-performing loans was 30.4% at September 30, 2012 compared to 25.8% at December 31, 2011. See – “TROUBLED DEBT RESTRUCUTURED AND NON-PERFORMING ASSETS.”

During the nine months ended September 30, 2012, mortgage-backed securities decreased \$18.8 million, or 2.5%, to \$728.5 million from \$747.3 million at December 31, 2011. The decrease in mortgage-backed securities during the nine months ended September 30, 2012 was primarily due to principal repayments of \$113.8 million partially offset by purchases of \$95.5 million and a \$9.5 million improvement in fair value. Additionally, during the nine months ended September 30, 2012, \$0.8 million in OTTI charges were recorded on five private issue CMOs. During the nine months ended September 30, 2012, other securities increased \$167.7 million, or 257.1%, to \$233.0 million from \$65.2 million at December 31, 2011. The increase in other securities during the nine months ended September 30, 2012 was primarily due to purchases of \$169.0 million. Other securities primarily consist of securities issued by government agencies, mutual or bond funds that invest in government and government agency securities and corporate bonds.

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Liabilities. Total liabilities were \$3,939.1 million at September 30, 2012, an increase of \$68.0 million, or 1.8%, from \$3,871.0 million at December 31, 2011. During the nine months ended September 30, 2012, due to depositors decreased \$42.3 million, or 1.4%, to \$3,074.2 million, as a result of a \$46.9 million decrease in certificates of deposit partially offset by a \$4.6 million increase in core deposits. Borrowed funds increased \$99.8 million during the nine months ended September 30, 2012. The increase in borrowed funds was primarily due to a net increase of \$82.5 million in long term borrowings combined with a \$19.0 million increase in short-term borrowings.

Equity. Total stockholders’ equity increased \$24.5 million, or 5.9%, to \$441.4 million at September 30, 2012 from \$416.9 million at December 31, 2011. Stockholders’ equity increased primarily due to net income of \$25.1 million for the nine months ended September 30, 2012, an increase in other comprehensive income of \$9.1 million primarily due to an increase in the fair value of the securities portfolio and \$1.4 million due to the issuance of shares from the annual funding of certain employee retirement plans through the release of common shares from the Employee Benefit Trust. In addition, the exercise of stock options increase stockholders’ equity by \$0.8 million, including the income tax benefit realized. These increases were partially offset by the declaration and payment of dividends on the Company’s common stock of \$12.0 million and the purchase of 181,000 treasury shares at a cost of \$2.4 million. Book value per common share was \$14.28 at September 30, 2012 compared to \$13.49 at December 31, 2011. Tangible book value per common share was \$13.76 at September 30, 2012 compared to \$12.96 at December 31, 2011.

On September 28, 2011, the Company announced the authorization by the Board of Directors of a new common stock repurchase program, which authorizes the purchase of up to 1,000,000 shares of the Company’s common stock. During the nine months ended September 30, 2012, the Company repurchased 181,000 shares of the Company’s common stock at an average cost of \$13.50 per share. At September 30, 2012, 556,962 shares remain to be repurchased under the current stock repurchase program. Stock will be purchased under the current stock repurchase program from time to time, in the open market or through private transactions, subject to market conditions. There is no expiration or maximum dollar amount under this authorization.

Cash flow. During the nine months ended September 30, 2012, funds provided by the Company's operating activities amounted to \$56.4 million. These funds, together with \$50.6 million provided by financing activities and funds available at the beginning of the period, were utilized to fund net investing activities of \$126.7 million. The Company's primary business objective is the origination and purchase of one-to-four family (including mixed-use properties), multi-family residential and commercial real estate mortgage loans and commercial, business and SBA loans. During the nine months ended September 30, 2012, the net total of loan originations and purchases less loan repayments and sales was a \$14.2 million inflow of cash. During the nine months ended September 30, 2012, the Company also funded \$264.5 million in purchases of securities available for sale. During the nine months ended September 30, 2012, funds were primarily provided by an increase of \$19.0 million in short-term borrowed funds and an \$82.5 million net increase in long-term borrowed funds. Additionally, funds were provided by \$128.1 million in proceeds from maturities, sales, calls and prepayments of securities available for sale. These increases funded a \$37.0 million decrease in deposits. The Company also used funds of 11.9 million and \$3.0 million for dividend payments and purchases of treasury stock, respectively, during the three months ended September 30, 2012.

INTEREST RATE RISK

The Consolidated Statements of Financial Position have been prepared in accordance with generally accepted accounting principles in the United States of America, which require the measurement of financial position and operating results in terms of historical dollars without considering the changes in fair value of certain investments due

to changes in interest rates. Generally, the fair value of financial investments such as loans and securities fluctuates inversely with changes in interest rates. As a result, increases in interest rates could result in decreases in the fair value of the Company's interest-earning assets which could adversely affect the Company's results of operation if such assets were sold, or, in the case of securities classified as available-for-sale, decreases in the Company's stockholders' equity, if such securities were retained.

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The Company manages the mix of interest-earning assets and interest-bearing liabilities on a continuous basis to maximize return and adjust its exposure to interest rate risk. On a quarterly basis, management prepares the “Earnings and Economic Exposure to Changes in Interest Rate” report for review by the Board of Directors, as summarized below. This report quantifies the potential changes in net interest income and net portfolio value should interest rates go up 400 basis points or down 200 basis points (shocked), assuming the yield curves of the rate shocks will be parallel to each other. Net portfolio value is defined as the market value of assets net of the market value of liabilities. The market value of assets and liabilities is determined using a discounted cash flow calculation. The net portfolio value ratio is the ratio of the net portfolio value to the market value of assets. All changes in income and value are measured as percentage changes from the projected net interest income and net portfolio value at the base interest rate scenario. The base interest rate scenario assumes interest rates at September 30, 2012. Various estimates regarding prepayment assumptions are made at each level of rate shock. However, prepayment penalty income is included in this analysis. Actual results could differ significantly from these estimates. At September 30, 2012, the Company was within the guidelines set forth by the Board of Directors for each interest rate level.

The following table presents the Company’s interest rate shock as of September 30, 2012:

| Change in Interest Rate | Projected Percentage Change | | | | | |
|-------------------------|-----------------------------|---|-----------|---|-------------|---|
| | In | | Net | | Net | |
| | Net Interest | | Portfolio | | Portfolio | |
| | Income | | Value | | Value Ratio | |
| -200 Basis points | -3.20 | % | 20.77 | % | 15.78 | % |
| -100 Basis points | -1.45 | | 11.79 | | 14.83 | |
| Base interest rate | - | | - | | 13.63 | |
| +100 Basis points | -4.04 | | -13.52 | | 12.19 | |
| +200 Basis points | -7.33 | | -26.74 | | 10.69 | |
| +300 Basis points | -11.49 | | -39.55 | | 9.13 | |
| +400 Basis points | -16.47 | | -42.27 | | 7.77 | |

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AVERAGE BALANCES

Net interest income represents the difference between income on interest-earning assets and expense on interest-bearing liabilities. Net interest income depends upon the relative amount of interest-earning assets and interest-bearing liabilities and the interest rate earned or paid on them. The following table sets forth certain information relating to the Company’s Consolidated Statements of Financial Condition and Consolidated Statements of Income for the three months ended September 30, 2012 and 2011, and reflects the average yield on assets and average cost of liabilities for the periods indicated. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods shown. Average balances are derived from average daily balances. The yields include amortization of deferred fees and costs, late charges, and prepayment penalties, which are considered adjustments to yields.

| | Average Balance | For the three months ended September 30, | | Yield/ Cost (Dollars in thousands) | 2011 | | Yield/ Cost |
|--|--------------------|--|----------|--|-------------|--------------------|----------------|
| | | 2012 | Interest | | Interest | Average Balance | |
| Assets | | | | | | | |
| Interest-earning assets: | | | | | | | |
| Mortgage loans, net (1) | \$2,889,894 | 41,373 | 5.73 | % | \$2,923,686 | 44,082 | 6.03 |
| Other loans, net (1) | 285,360 | 3,484 | 4.88 | | 281,941 | 3,685 | 5.23 |
| Total loans, net | 3,175,254 | 44,857 | 5.65 | | 3,205,627 | 47,767 | 5.96 |
| Mortgage-backed securities | 693,001 | 6,765 | 3.90 | | 777,186 | 8,036 | 4.14 |
| Other securities | 232,684 | 1,546 | 2.66 | | 59,868 | 491 | 3.28 |
| Total securities | 925,685 | 8,311 | 3.59 | | 837,054 | 8,527 | 4.07 |
| Interest-earning deposits and federal funds sold | 56,813 | 25 | 0.18 | | 74,388 | 35 | 0.19 |
| Total interest-earning assets | 4,157,752 | 53,193 | 5.12 | | 4,117,069 | 56,329 | 5.47 |
| Other assets | 244,556 | | | | 223,280 | | |
| Total assets | \$4,402,308 | | | | \$4,340,349 | | |
| Liabilities and Equity | | | | | | | |
| Interest-bearing liabilities: | | | | | | | |
| Deposits: | | | | | | | |
| Savings accounts | \$306,573 | 150 | 0.20 | | \$368,026 | 560 | 0.61 |
| NOW accounts | 989,644 | 1,446 | 0.58 | | 833,403 | 1,600 | 0.77 |
| Money market accounts | 172,013 | 75 | 0.17 | | 239,270 | 309 | 0.52 |
| Certificate of deposit accounts | 1,504,736 | 8,417 | 2.24 | | 1,589,433 | 9,783 | 2.46 |
| Total due to depositors | 2,972,966 | 10,088 | 1.36 | | 3,030,132 | 12,252 | 1.62 |
| Mortgagors' escrow accounts | 35,729 | 9 | 0.10 | | 33,358 | 14 | 0.17 |
| Total deposits | 3,008,695 | 10,097 | 1.34 | | 3,063,490 | 12,266 | 1.60 |
| Borrowed funds | 782,614 | 5,513 | 2.82 | | 726,736 | 6,962 | 3.83 |
| Total interest-bearing liabilities | 3,791,309 | 15,610 | 1.65 | | 3,790,226 | 19,228 | 2.03 |
| Non interest-bearing deposits | 139,562 | | | | 110,800 | | |
| Other liabilities | 38,279 | | | | 30,664 | | |
| Total liabilities | 3,969,150 | | | | 3,931,690 | | |
| Equity | 433,158 | | | | 408,659 | | |

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| | | | | | | |
|--|-------------|------|---|-------------|------|---|
| Total liabilities and equity | \$4,402,308 | | | \$4,340,349 | | |
| Net interest income / net interest rate spread | \$37,583 | 3.47 | % | \$37,101 | 3.44 | % |
| Net interest-earning assets / net interest margin | \$366,443 | 3.62 | % | \$326,843 | 3.60 | % |
| Ratio of interest-earning assets to interest-bearing liabilities | | 1.10 | X | | 1.09 | X |

(1) Loan interest income includes loan fee income (which includes net amortization of deferred fees and costs, late charges, and prepayment penalties) of approximately \$0.8 million and \$0.4 million for the three months ended September 30, 2012 and 2011, respectively.

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| | For the nine months ended September 30, | | | | | |
|---|---|------------------|--|--------------------|------------------|----------------|
| | Average Balance | Interest | Yield/ Cost (Dollars in thousands) | Average Balance | Interest | Yield/ Cost |
| Assets | | | | | | |
| Interest-earning assets: | | | | | | |
| Mortgage loans, net (1) | \$2,902,201 | 127,111 | 5.84 % | \$2,932,399 | 133,326 | 6.06 % |
| Other loans, net (1) | 288,834 | 10,429 | 4.81 | 292,502 | 11,252 | 5.13 |
| Total loans, net | 3,191,035 | 137,540 | 5.75 | 3,224,901 | 144,578 | 5.98 |
| Mortgage-backed securities | 704,347 | 20,652 | 3.91 | 752,362 | 23,740 | 4.21 |
| Other securities | 186,165 | 3,747 | 2.68 | 59,524 | 1,447 | 3.24 |
| Total securities | 890,512 | 24,399 | 3.65 | 811,886 | 25,187 | 4.14 |
| Interest-earning deposits and federal funds sold | 43,913 | 53 | 0.16 | 64,446 | 89 | 0.18 |
| Total interest-earning assets | 4,125,460 | 161,992 | 5.24 | 4,101,233 | 169,854 | 5.52 |
| Other assets | 240,724 | | | 217,902 | | |
| Total assets | \$4,366,184 | | | \$4,319,135 | | |
| Liabilities and Equity | | | | | | |
| Interest-bearing liabilities: | | | | | | |
| Deposits: | | | | | | |
| Savings accounts | \$325,333 | 546 | 0.22 | \$373,676 | 1,732 | 0.62 |
| NOW accounts | 1,001,843 | 4,685 | 0.62 | 823,074 | 5,100 | 0.83 |
| Money market accounts | 182,978 | 340 | 0.25 | 300,956 | 1,118 | 0.50 |
| Certificate of deposit accounts | 1,475,118 | 25,634 | 2.32 | 1,557,212 | 28,966 | 2.48 |
| Total due to depositors | 2,985,272 | 31,205 | 1.39 | 3,054,918 | 36,916 | 1.61 |
| Mortgagors' escrow accounts | 41,179 | 27 | 0.09 | 38,958 | 38 | 0.13 |
| Total deposits | 3,026,451 | 31,232 | 1.38 | 3,093,876 | 36,954 | 1.59 |
| Borrowed funds | 749,878 | 17,545 | 3.12 | 693,292 | 21,849 | 4.20 |
| Total interest-bearing liabilities | 3,776,329 | 48,777 | 1.72 | 3,787,168 | 58,803 | 2.07 |
| Non interest-bearing deposits | 128,912 | | | 105,405 | | |
| Other liabilities | 35,076 | | | 27,664 | | |
| Total liabilities | 3,940,317 | | | 3,920,237 | | |
| Equity | 425,867 | | | 398,898 | | |
| Total liabilities and equity | \$4,366,184 | | | \$4,319,135 | | |
| Net interest income / net interest rate spread | | \$113,215 | 3.52 % | | \$111,051 | 3.45 % |

| | | | | | | |
|--|-----------|------|---|-----------|------|---|
| Net interest-earning assets / net interest margin | \$349,131 | 3.66 | % | \$314,065 | 3.61 | % |
| Ratio of interest-earning assets to interest-bearing liabilities | | 1.09 | X | | 1.08 | X |

(1) Loan interest income includes loan fee income (which includes net amortization of deferred fees and costs, late charges, and prepayment penalties) of approximately \$2.2 million and \$1.2 million for the nine months ended September 30, 2012 and 2011, respectively.

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LOANS

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

| (In thousands) | For the nine months ended September | |
|--|-------------------------------------|--------------|
| | 2012 | 30, 2011 |
| Mortgage Loans | | |
| At beginning of period | \$ 2,939,012 | \$ 2,966,890 |
| Mortgage loans originated: | | |
| Multi-family residential | 211,052 | 161,518 |
| Commercial real estate | 21,756 | 7,062 |
| One-to-four family – mixed-use property | 13,955 | 18,552 |
| One-to-four family – residential | 18,076 | 15,571 |
| Co-operative apartments | 1,726 | - |
| Construction | 653 | 1,283 |
| Total mortgage loans originated | 267,218 | 203,986 |
| Less: | | |
| Principal and other reductions | 284,687 | 231,741 |
| Sales and loans transferred to loans held for sale | 33,048 | 14,976 |
| At end of period | \$ 2,888,495 | \$ 2,924,159 |
| Commercial Business and Other Loans | | |
| At beginning of period | \$ 274,981 | \$ 292,936 |
| Other loans originated: | | |
| Small business administration | 513 | 3,170 |
| Taxi Medallion | 8 | 46,229 |
| Commercial business | 158,730 | 11,779 |
| Other | 3,323 | 3,646 |
| Total other loans originated | 162,574 | 64,824 |
| Other loans purchased: | | |
| Taxi Medallion | 3,456 | 14,455 |
| Total other loans purchased | 3,456 | 14,455 |
| Less: | | |
| Principal and other reductions | 148,967 | 78,620 |

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| | | |
|--|------------|------------|
| Sales and loans transferred to loans held for sale | 7,179 | 4,005 |
| At end of period | \$ 284,865 | \$ 289,590 |

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TROUBLED DEBT RESTRUCUTURED AND NON-PERFORMING ASSETS

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

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

| (In thousands) | September 30, 2012 | June 30, 2012 | December 31, 2011 |
|---|--------------------------|------------------|-------------------------|
| Accrual Status: | | | |
| Multi-family residential | \$ 2,339 | \$2,348 | \$ 9,412 |
| Commercial real estate | 3,268 | 1,898 | 2,413 |
| One-to-four family - mixed-use property | 1,245 | 1,080 | 795 |
| One-to-four family - residential | 376 | - | - |
| Construction | 3,500 | 3,874 | 5,584 |
| Commercial business and other | 3,870 | 2,000 | 2,000 |
| Total | 14,598 | 11,200 | 20,204 |
| Non-accrual status: | | | |
| Commercial real estate | 3,887 | 5,287 | - |
| One-to-four family - mixed-use property | 1,098 | 1,275 | - |
| Total | 4,985 | 6,562 | - |
| Total performing TDR | \$ 19,583 | \$17,762 | \$ 20,204 |

During the nine months ended September 30, 2012, four TDR totaling \$7.2 million were transferred to non-performing status and nine loans totaling \$8.8 million were restructured as TDR.

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

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

| (In thousands) | September 30, 2012 | June 30, 2012 | December 31, 2011 |
|---|--------------------------|-------------------|-------------------------|
| Loans 90 days or more past due and still accruing: | | | |
| Multi-family residential | \$ - | \$- | \$ 6,287 |
| Commercial real estate | 540 | - | 92 |
| Commercial business and other | 748 | - | - |
| Total | 1,288 | - | 6,379 |
| Non-accrual loans: | | | |
| Multi-family residential | 18,242 | 27,972 | 19,946 |
| Commercial real estate | 18,051 | 19,585 | 19,895 |
| One-to-four family - mixed-use property | 20,250 | 20,437 | 28,429 |
| One-to-four family - residential | 13,068 | 12,450 | 12,766 |
| Co-operative apartments | 234 | 109 | 152 |
| Construction | 9,787 | 9,845 | 14,721 |
| Small business administration | 294 | 392 | 493 |
| Commercial business and other | 19,589 | 21,403 | 14,660 |
| Total | 99,515 | 112,193 | 111,062 |
| Total non-performing loans | 100,803 | 112,193 | 117,441 |
| Other non-performing assets: | | | |
| Real estate acquired through foreclosure | 3,660 | 2,094 | 3,179 |
| Investment securities | 2,984 | 2,761 | 2,562 |
| Total | 6,644 | 4,855 | 5,741 |
| Total non-performing assets | \$ 107,447 | \$ 117,048 | \$ 123,182 |

Included in non-accrual loans were nine loans totaling \$13.3 million, nine loans totaling \$20.9 million and six loans totaling \$17.1 million which were restructured as TDR which were not performing in accordance with their restructured terms at September 30, 2012, June 30, 2012 and December 31, 2011, respectively.

The Bank’s non-performing assets totaled \$107.4 million at September 30, 2012, a decrease of \$9.6 million from \$117.0 million at June 30, 2012 and a decrease of \$15.7 million from \$123.2 million at December 31, 2011. Total non-performing assets as a percentage of total assets were 2.45% at September 30, 2012 compared to 2.64% at June 30, 2012 and 2.87% at December 31, 2011. The ratio of allowance for loan losses to total non-performing loans was 30.4% at September 30, 2012 compared to 27.5% at June 30, 2012 and 25.8% at December 31, 2011.

During the three months ended September 30, 2012, 43 loans totaling \$13.8 million (net of \$0.2 million in charge-offs) were added to non-accrual loans, six loans totaling \$2.2 million were returned to performing status, seven loans totaling \$2.4 million (net of \$0.3 million in charge-offs) were paid in full, 28 loans totaling \$14.4 million (net of \$3.2 million in charge-offs) were sold, four loans totaling \$1.8 million (net of \$0.1 million in charge-offs) were

transferred to other real estate owned, and charge-offs of \$2.0 million were recorded on non-accrual loans that were non-accrual at the beginning of the third quarter of 2012.

Non-performing investment securities include two pooled trust preferred securities for which we are not receiving payments. At September 30, 2012, these investment securities had a combined amortized cost and market value of \$8.3 million and \$3.0 million, respectively.

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

| | September 30, 2012 | | December 31, 2011 | |
|---|--------------------|-----------------|-------------------|-----------------|
| | 60 - 89 days | 30 - 59 days | 60 - 89 days | 30 - 59 days |
| | (In thousands) | | | |
| Multi-family residential | \$3,019 | \$17,253 | \$6,341 | \$20,083 |
| Commercial real estate | 2,065 | 10,798 | 1,797 | 10,712 |
| One-to-four family - mixed-use property | 5,346 | 19,383 | 3,027 | 20,480 |
| One-to-four family - residential | 952 | 3,751 | 1,769 | 4,699 |
| Co-operative apartments | - | - | - | - |
| Construction loans | - | 2,462 | - | 5,065 |
| Small Business Administration | 789 | - | - | 16 |
| Taxi medallion | - | - | - | 71 |
| Commercial business and other | 3,630 | 2 | 966 | 1,056 |
| Total delinquent loans | \$15,801 | \$53,649 | \$13,900 | \$62,182 |

CRITICIZED AND CLASSIFIED ASSETS

Our policy is to review our assets, focusing primarily on the loan portfolio, other real estate owned and the investment portfolios, to ensure that the credit quality is maintained at the highest levels. When weaknesses are identified, immediate action is taken to correct the problem through direct contact with the borrower or issuer. We then monitor these assets and, in accordance with our policy and current regulatory guidelines, we designate them as “Special Mention,” which is considered a “Criticized Asset,” and “Substandard,” “Doubtful,” or “Loss,” which are considered “Classified Assets,” as deemed necessary. We designate an asset as Substandard when a well-defined weakness is identified that jeopardizes the orderly liquidation of the debt. We designate an asset as Doubtful when it displays the inherent weakness of a Substandard asset with the added provision that collection of the debt in full, on the basis of existing facts, is highly improbable. We designate an asset as Loss if it is deemed the debtor is incapable of repayment. Loans that are designated as Loss are charged to the Allowance for Loan Losses. Assets that are non-accrual are designated as Substandard, Doubtful or Loss. We designate an asset as Special Mention if the asset does not warrant designation within one of the other categories, but does contain a potential weakness that deserves closer attention. Our total Criticized and Classified assets were \$244.3 million at September 30, 2012, a decrease of \$60.9 million from \$305.1 million at December 31, 2011.

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The following table sets forth the Banks’ assets designated as Criticized and Classified at September 30, 2012:

| (In thousands) | Special Mention | Substandard | Doubtful | Loss | Total |
|---|--------------------|-------------------|-----------------|------------|------------------|
| Loans: | | | | | |
| Multi-family residential | \$ 15,847 | \$ 23,689 | \$- | \$- | \$39,536 |
| Commercial real estate | 15,228 | 29,668 | - | - | 44,896 |
| One-to-four family - mixed-use property | 9,879 | 30,394 | - | - | 40,273 |
| One-to-four family - residential | 2,966 | 15,430 | - | - | 18,396 |
| Co-operative apartments | 198 | 237 | - | - | 435 |
| Construction loans | 3,805 | 12,685 | - | - | 16,490 |
| Small Business Administration | 199 | 459 | 244 | - | 902 |
| Commercial business and other | 5,184 | 23,460 | 1,169 | - | 29,813 |
| Total loans | 53,306 | 136,022 | 1,413 | - | 190,741 |
| Investment Securities: (1) | | | | | |
| Pooled trust preferred securities | - | 15,831 | - | - | 15,831 |
| Private issue CMO | - | 34,037 | - | - | 34,037 |
| Total investment securities | - | 49,868 | - | - | 49,868 |
| Other Real Estate Owned | - | 3,660 | - | - | 3,660 |
| Total | \$ 53,306 | \$ 189,550 | \$ 1,413 | \$- | \$244,269 |

The following table sets forth the Banks’ assets designated as Criticized and Classified at December 31, 2011:

| (In thousands) | Special Mention | Substandard | Doubtful | Loss | Total |
|---|--------------------|----------------|--------------|----------|----------------|
| Loans: | | | | | |
| Multi-family residential | \$ 17,135 | \$ 41,393 | \$- | \$- | \$58,528 |
| Commercial real estate | 12,264 | 41,247 | - | - | 53,511 |
| One-to-four family - mixed-use property | 17,393 | 33,831 | - | - | 51,224 |
| One-to-four family - residential | 3,127 | 14,343 | - | - | 17,470 |
| Co-operative apartments | 203 | 153 | - | - | 356 |
| Construction loans | 2,570 | 28,555 | - | - | 31,125 |
| Small Business Administration | 666 | 256 | 214 | - | 1,136 |
| Commercial business and other | 13,585 | 17,613 | 1,169 | - | 32,367 |
| Total loans | 66,943 | 177,391 | 1,383 | - | 245,717 |
| Investment Securities: (1) | | | | | |
| Pooled trust preferred securities | - | 15,344 | - | - | 15,344 |
| Private issue CMO | - | 40,905 | - | - | 40,905 |
| Total investment securities | - | 56,249 | - | - | 56,249 |

| | | | | | |
|-------------------------|-----------|------------|----------|-----|-----------|
| Other Real Estate Owned | - | 3,179 | - | - | 3,179 |
| Total | \$ 66,943 | \$ 236,819 | \$ 1,383 | \$- | \$305,145 |

(1) Our investment securities are classified as securities available for sale and as such are carried at their fair value in our Consolidated Financial Statements. The securities above had a fair value of \$40.8 million and \$41.1 million at September 30, 2012 and December 31, 2011, respectively. Under current applicable regulatory guidelines, we are required to disclose the classified investment securities, as shown in the tables above, at their book values (amortized cost, or fair value for securities that are carried under the fair value option). Additionally, the requirement is only for the Banks' securities. Flushing Financial Corporation had two private issue trust preferred securities classified as Substandard with a combined market value of \$0.8 million at September 30, 2012 and December 31, 2011.

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

We designate investment securities as Substandard when the investment grade rating by one or more of the rating agencies is below investment grade. We have designated a total of 19 investment securities that are held at the Savings Bank as Substandard at September 30, 2012. Our classified investment securities at September 30, 2012 held by the Savings Bank include 15 private issue CMOs rated below investment grade by one or more of the rating agencies, three issues of pooled trust preferred securities and one private issue trust preferred security. The Investment Securities which are classified as Substandard at September 30, 2012 are securities that were rated investment grade when we purchased them. These securities have each been subsequently downgraded by at least one rating agency to below investment grade. Through September 30, 2012, two of the pooled trust preferred securities and nine private issue CMOs are not paying principal and interest as scheduled. We test each of these securities quarterly for impairment, through an independent third party.

ALLOWANCE FOR LOAN LOSSES

We have established and maintain on our books an allowance for loan losses that is designed to provide a reserve against estimated losses inherent in our overall loan portfolio. The allowance is established through a provision for loan losses based on management’s evaluation of the risk inherent in the various components of the loan portfolio and other factors, including historical loan loss experience (which is updated quarterly), changes in the composition and volume of the portfolio, collection policies and experience, trends in the volume of non-accrual and classified loans and local and national economic conditions. The determination of the amount of the allowance for loan losses includes estimates that are susceptible to significant changes due to changes in appraisal values of collateral, national and local economic conditions and other factors. We incurred total net charge-offs of \$5.2 million and \$4.8 million during the three months ended September 30, 2012 and 2011, respectively, and \$15.7 million and \$13.1 million during the nine months ended September 30, 2012 and 2011, respectively. The national and regional economies were generally considered to be in a recession from December 2007 through the middle of 2009. This has resulted in increased unemployment and declining property values, although the property value declines in the New York City metropolitan area have not been as great as many other areas of the country. While the national and regional economies have shown signs of improvement since the second half of 2009, unemployment has remained at elevated levels. The deterioration in the economy has resulted in an elevated level of non-performing loans, which totaled \$100.8 million at September 30, 2012 and \$117.4 million at December 31, 2011. The Savings Bank’s underwriting standards generally require a loan-to-value ratio of no more than 75% at the time the loan is originated. At September 30, 2012, the average outstanding principal balance of our non-performing loans was 58.1% of the estimated current value of the supporting collateral, after considering the charge-offs that have been recorded. A provision for loan losses of \$16.0 million and \$15.0 million was recorded for the nine months ended September 30, 2012 and 2011, respectively.

We review our loan portfolio by separate categories with similar risk and collateral characteristics, e.g., multi-family residential, commercial real estate, one-to-four family mixed-use property, one-to-four family residential, co-operative apartment, construction, SBA, commercial business, taxi medallion and consumer loans. Impaired loans are segregated and reviewed separately. All non-accrual loans and TDRs are considered impaired. Impaired loans secured by real estate are reviewed based on the fair value of their collateral. In connection with the determination of the allowance, the market value of collateral ordinarily is evaluated by our staff appraiser. On a quarterly basis, the

estimated values of impaired mortgage loans are internally reviewed based on updated cash flows for income producing properties and, at times, an updated independent appraisal is obtained. The loan balances of collateral dependent impaired loans are then compared to the loans updated fair value. The balance which exceeds fair value is generally charged-off. We do not allocate additional reserves to loans which have been written down to their fair value. When evaluating a loan for impairment, we do not rely on guarantees and the amount of impairment, if any, is based on the fair value of the collateral. We do not carry loans at a value in excess of the fair value due to a guarantee from the borrower. Impaired mortgage loans that were written down resulted from quarterly reviews or updated appraisals that indicated the properties' estimated value had declined from when the loan was originated. Loans classified as TDR which are performing in accordance with their modified terms are evaluated based on the projected discounted cash flow of the restructured loan at the loans effective interest rate prior to restructuring. A portion of the allowance for loan losses is allocated in the amount by which the recorded investment in the TDR exceeds the discounted cash flow. For non-collateralized impaired loans, management estimates any recoveries that are anticipated for each loan. A portion of the allowance is allocated to non-collateralized loans based on these estimates. Based on the review of impaired loans, which includes loans classified as TDR, a portion of the allowance was allocated to impaired loans in the amount of \$1.6 million and \$4.2 million at September 30, 2012 and December 31, 2011, respectively.

PART I – FINANCIAL INFORMATION
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General provisions are established against performing loans in our portfolio in amounts deemed prudent by management. A portion of the allowance is allocated to the remaining portfolio based on historical loss experience. The historical loss period used for this allocation was three years. Management also prepared an additional analysis to ensure that the remaining portion of the allowance for possible loan losses is sufficient to cover losses inherent in the loan portfolio. This analysis considered: (1) the current economic environment, (2) delinquency and non-accrual trends, (3) classified loan trends, (4) the risk inherent in our loan portfolio and volume and trends of loan types, (5) recent trends in charge-offs, (6) changes in underwriting standards, (7) the experience, ability and depth of our lenders, and (8) collection policies and experience. Based on these reviews, management concluded the general portion of the allowance should be \$29.1 million and \$26.1 million at September 30, 2012 and December 31, 2011, respectively, resulting in a total allowance of \$30.7 million and \$30.3 million at September 30, 2012 and December 31, 2011, respectively. The Board of Directors reviews and approves the adequacy of the allowance for loan losses on a quarterly basis. Management has concluded and the Board of Directors has concurred, that at September 30, 2012, the allowance was sufficient to absorb losses inherent in our loan portfolio.

PART I – FINANCIAL INFORMATION
 FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
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The following table sets forth the activity in the Company's allowance for loan losses for the periods indicated:

| (Dollars in thousands) | For the nine months ended September | | | | |
|---|-------------------------------------|-----------|-------------|-----------|---|
| | 2012 | | 30, 2011 | | |
| Balance at beginning of period | \$ | 30,344 | \$ | 27,699 | |
| Provision for loan losses | | 16,000 | | 15,000 | |
| Charge-offs: | | | | | |
| Multi-family residential | | (5,252) | | (4,093) | |
| Commercial real estate | | (2,401) | | (4,194) | |
| One-to-four family – mixed-use property | | (3,401) | | (1,401) | |
| One-to-four family – residential | | (1,096) | | (1,991) | |
| Co-operative apartments | | (62) | | - | |
| Construction | | (2,500) | | (703) | |
| Small Business Administration | | (324) | | (628) | |
| Commercial business and other | | (1,488) | | (524) | |
| Total charge-offs | | (16,524) | | (13,534) | |
| Recoveries: | | | | | |
| Multi-family residential | | 89 | | 109 | |
| Commercial real estate | | 249 | | 123 | |
| One-to-four family – mixed-use property | | 337 | | 113 | |
| One-to-four family – residential | | 29 | | 63 | |
| Small Business Administration | | 59 | | 20 | |
| Commercial business and other | | 104 | | 10 | |
| Total recoveries | | 867 | | 438 | |
| Net charge-offs | | (15,657) | | (13,096) | |
| Balance at end of period | \$ | 30,687 | \$ | 29,603 | |
| Ratio of net charge-offs during the period to average loans outstanding during the period | | 0.65 | % | 0.54 | % |
| Ratio of allowance for loan losses to gross loans at end of period | | 0.97 | % | 0.92 | % |
| Ratio of allowance for loan losses to non-performing assets at end of period | | 28.56 | % | 24.04 | % |
| Ratio of allowance for loan losses to non-performing loans at end of period | | 30.44 | % | 25.44 | % |

RECENT PROPOSED CHANGES TO REGULATORY CAPITAL RULES

During the second quarter of 2012, the federal bank regulatory agencies jointly issued three notices of proposed rulemaking ("NPRs") that would revise and replace the agencies' current capital rules. The NPRs include numerous revisions to the existing capital regulations, including, but not limited to, the following:

- Revises the definition of regulatory capital components and related calculations.

- Adds a new common equity tier 1 capital ratio.
- Increases the minimum tier 1 capital ratio requirement from four percent to six percent.
- Incorporates the revised regulatory capital requirements into the Prompt Corrective Action framework.
- Implements a new capital conservation buffer that would limit payment of capital distributions and certain discretionary bonus payments to executive officers and key risk takers if the banking organization does not hold certain amounts of common equity tier 1 capital in addition to those needed to meet its minimum risk-based capital requirements.
- Provides a transition period for several aspects of the proposed rule, including the phase-out period for certain non-qualifying capital instruments, the new minimum capital ratio requirements, the capital conservation buffer, and the regulatory capital adjustments and deductions.

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- Revises risk weights for residential mortgages based on loan-to-value ratios and certain product and underwriting features.
- Increases capital requirements for past-due loans, high volatility commercial real estate exposures, and certain short-term loan commitments.
 - Removes references to credit ratings consistent with Section 939A of the Dodd-Frank Act.
 - Establishes due diligence requirements for securitization exposures.

The proposed NPRs will result in the Company, in addition to the Banks, becoming subject to capital requirements. Based on our preliminary assessment of the NPRs, we believe we will see an increase in our total risk-weighted assets. However, the Company and the Banks, based on our preliminary assessment, would meet the requirements of the NPRs and will continue to be considered well-capitalized.

PART I – FINANCIAL INFORMATION
FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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

ITEM 4. CONTROLS AND PROCEDURES

The Company carried out, under the supervision and with the participation of the Company's management, including its Chief Executive Officer and Chief Financial Officer, an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this Quarterly Report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of September 30, 2012, the design and operation of these disclosure controls and procedures were effective. During the period covered by this Quarterly Report, there have been no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II – OTHER INFORMATION
FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

ITEM 1. LEGAL PROCEEDINGS

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

ITEM 1A. RISK FACTORS

There have been no material changes from the risk factors disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

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

The following table sets forth information regarding the shares of common stock repurchased by the Company during the three months ended September 30, 2012:

| Period | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Number of Shares That May Yet Be Purchased Under the Plans or Programs |
|--------------------------------------|---|---------------------------------|--|--|
| July 1 to July 31, 2012 | - | \$ - | - | 607,062 |
| August 1 to August 31, 2012 | 50,100 | 14.43 | 50,100 | 556,962 |
| September 1 to September 30, 2012 | - | - | - | 556,962 |
| Total | 50,100 | \$ - | 50,100 | |

On September 28, 2011, the Company announced the authorization by the Board of Directors of a new common stock repurchase program, which authorizes the purchase of up to 1,000,000 shares of the Company's common stock. During the three months ended September 30, 2012, the Company repurchased 50,100 shares of the Company's common stock at an average cost of \$14.43 per share. At September 30, 2012, 556,962 shares remain to be repurchased under the current stock repurchase program. Stock will be purchased under the current stock repurchase program from time to time, in the open market or through private transactions subject to market conditions. There is no expiration or maximum dollar amount under this authorization.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

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PART II – OTHER INFORMATION
 FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES

ITEM 6. EXHIBITS

Exhibit No. Description

| | |
|---------|---|
| 2.1 | Agreement and Plan of Merger dated as of December 20, 2005 by and between Flushing Financial Corporation and Atlantic Liberty Financial Corp. (7) |
| 3.1 | Certificate of Incorporation of Flushing Financial Corporation (1) |
| 3.2 | Certificate of Amendment to Certificate of Incorporation of Flushing Financial Corporation (3) |
| 3.3 | Certificate of Amendment to Certificate of Incorporation of Flushing Financial Corporation (6) |
| 3.4 | Certificate of Designations of Series A Junior Participating Preferred Stock of Flushing Financial Corporation (4) |
| 3.5 | Certificate of Increase of Shares Designated as Series A Junior Participating Preferred Stock of Flushing Financial Corporation (2) |
| 3.6 | By-Laws of Flushing Financial Corporation (1) |
| 4.1 | Rights Agreement, dated as of September 8, 2006, between Flushing Financial Corporation and Computershare Trust Company N.A., as Rights Agent, which includes the form of Certificate of Increase of Shares Designated as Series A Junior Participating Preferred Stock as Exhibit A, form of Right Certificate as Exhibit B and the Summary of Rights to Purchase Preferred Stock as Exhibit C (5) |
| 4.2 | Flushing Financial Corporation has outstanding certain long-term debt. None of such debt exceeds ten percent of Flushing Financial Corporation's total assets; therefore, copies of constituent instruments defining the rights of the holders of such debt are not included as exhibits. Copies of instruments with respect to such long-term debt will be furnished to the Securities and Exchange Commission upon request. |
| 31.1 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Chief Executive Officer (filed herewith) |
| 31.2 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Chief Financial Officer (filed herewith) |
| 32.1 | Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002 by the Chief Executive Officer (filed herewith) |
| 32.2 | Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002 by the Chief Financial Officer (filed herewith) |
| 101.INS | XBRL Instance Document (furnished herewith) |
| 101.SCH | XBRL Taxonomy Extension Schema Document (furnished herewith) |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document (furnished herewith) |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document (furnished herewith) |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document (furnished herewith) |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document (furnished herewith) |

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

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
SIGNATURES

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

Flushing Financial Corporation,

Dated: November 9, 2012

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

Dated: November 9, 2012

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

FLUSHING FINANCIAL CORPORATION and SUBSIDIARIES
EXHIBIT INDEX

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- (3) Incorporated by reference to Exhibits filed with Form S-8 filed May 31, 2002.
- (4) Incorporated by reference to Exhibits filed with Form 10-Q for the quarter ended September 30, 2002.
- (5) Incorporated by reference to Exhibit filed with Form 8-K filed September 11, 2006.
- (6) Incorporated by reference to Exhibit filed with Form 10-K filed March 15, 2012.
- (7) Incorporated by reference to Exhibit filed with Form 8-K filed December 23, 2005.

