CITY NATIONAL CORP
Form 10-Q
August 07, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2015

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

For the transition period from to

Commission file number 1-10521

CITY NATIONAL CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**95-2568550**
(State of Incorporation)	(I.R.S. Employer Identification No.)

City National Plaza

555 South Flower Street, Los Angeles, California, 90071

(Address of principal executive offices)(Zip Code)

(213) 673-7700

(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

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

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

As of July 31, 2015, there were 55,750,611 shares of Common Stock outstanding (including unvested restricted shares).

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CITY NATIONAL CORPORATION

CONSOLIDATED BALANCE SHEETS

(Unaudited)

(in thousands, except share amounts)	June 30, 2015	December 31, 2014
Assets		
Cash and due from banks	$ 433,629	$ 336,470
Due from banks - interest-bearing	704,258	119,981
Federal funds sold and securities purchased under resale agreements	200,000	200,000
Securities available-for-sale - cost $4,943,133 and $5,894,509 at June 30, 2015 and December 31, 2014, respectively:		
Securities pledged as collateral	10,964	14,654
Held in portfolio	4,929,879	5,868,329
Securities held-to-maturity - fair value $3,460,942 and $3,484,647 at June 30, 2015 and December 31, 2014, respectively:		
Securities pledged as collateral	518,952	521,262
Held in portfolio	2,903,227	2,905,769
Trading securities	110,136	173,188
Loans and leases, excluding covered loans	21,929,328	20,337,206
Less: Allowance for loan and lease losses	316,922	310,149
Loans and leases, excluding covered loans, net	21,612,406	20,027,057
Covered loans, net of allowance for loan losses	425,958	502,371
Net loans and leases	22,038,364	20,529,428
Premises and equipment, net	205,507	207,700
Deferred tax asset	237,853	233,811
Goodwill	637,918	635,868
Customer-relationship intangibles, net	32,227	34,831
Affordable housing investments	194,443	186,423
Customers acceptance liability	3,462	17,664
Other real estate owned ($11,311 and $12,760 covered by FDIC loss share at June 30, 2015 and December 31, 2014, respectively)	17,268	23,496
FDIC indemnification asset	34,799	50,511
Other assets	547,612	537,847
Total assets	$ 33,760,498	$ 32,597,232
Liabilities		
Demand deposits	$ 19,648,595	$ 18,030,021
Interest checking deposits	2,462,289	2,736,391
Money market deposits	6,323,160	6,198,798
Savings deposits	483,794	469,931
Time deposits-under $100,000	147,138	155,568
Time deposits-$100,000 and over	416,254	517,394
Total deposits	29,481,230	28,108,103
Short-term borrowings	6,322	322,861

Long-term debt		640,617		638,600
Reserve for off-balance sheet credit commitments		30,024		27,811
Acceptances outstanding		3,462		17,664
Other liabilities		488,940		499,514
Total liabilities		30,650,595		29,614,553
Redeemable noncontrolling interest		37,755		39,978
Commitments and contingencies				
Shareholders equity				
Preferred stock, par value $1.00 per share; 5,000,000 shares authorized; 275,000 shares issued at June 30, 2015 and December 31, 2014		267,616		267,616
Common stock, par value $1.00 per share; 75,000,000 shares authorized; 55,664,127 and 55,162,455 shares issued at June 30, 2015 and December 31, 2014, respectively		55,664		55,162
Additional paid-in capital		615,371		578,046
Accumulated other comprehensive loss		(1,760)		(7,074)
Retained earnings		2,153,871		2,071,230
Treasury shares, at cost - 311,068 and 377,224 shares at June 30, 2015 and December 31, 2014, respectively		(18,614)		(22,279)
Total common shareholders equity		2,804,532		2,675,085
Total shareholders equity		3,072,148		2,942,701
Total liabilities and shareholders equity	$	33,760,498	$	32,597,232

See accompanying Notes to the Unaudited Consolidated Financial Statements.

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CITY NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(in thousands, except per share amounts)	For the three months ended June 30, 2015	2014	For the six months ended June 30, 2015	2014
Interest income				
Loans and leases	$ 204,525	$ 186,999	$ 388,557	$ 356,696
Securities	41,196	43,471	83,268	85,046
Due from banks - interest-bearing	433	378	569	820
Federal funds sold and securities purchased under resale agreements	1,134	1,477	2,375	2,848
Total interest income	247,288	232,325	474,769	445,410
Interest expense				
Deposits	1,880	2,060	3,800	4,194
Federal funds purchased and securities sold under repurchase agreements	8		79	
Subordinated debt	3,746	6,117	7,492	12,221
Other long-term debt	5,144	5,046	10,308	10,095
Total interest expense	10,778	13,223	21,679	26,510
Net interest income	236,510	219,102	453,090	418,900
(Reversal of) provision for credit losses on loans and leases, excluding covered loans	10,000	(1,000)	10,000	(1,000)
(Reversal of) provision for losses on covered loans	1,091	(1,461)	1,588	3,194
Net interest income after provision	225,419	221,563	441,502	416,706
Noninterest income				
Trust and investment fees	58,487	54,599	114,008	107,905
Brokerage and mutual fund fees	11,424	14,240	22,022	24,282
Cash management and deposit transaction charges	12,861	12,128	25,494	24,161
International services	11,774	11,483	22,442	21,878
FDIC loss sharing expense, net	(10,808)	(24,161)	(17,496)	(31,244)
Gain on disposal of assets	1,538	6,838	1,648	9,664
Gain on sale of securities	1,924	5,367	5,300	7,489
Other	25,975	20,853	50,897	38,460
Impairment loss on securities:				
Total other-than-temporary impairment loss on securities	(634)	(565)	(699)	(565)
Less: Portion of loss recognized in other comprehensive income	363	317	363	317
Net impairment loss recognized in earnings	(271)	(248)	(336)	(248)
Total noninterest income	112,904	101,099	223,979	202,347
Noninterest expense				
Salaries and employee benefits	144,681	138,859	289,249	275,692
Net occupancy of premises	16,179	16,595	32,252	32,689
Legal and professional fees	17,348	18,393	34,286	31,343
Information services	10,648	9,463	20,508	18,809
Depreciation and amortization	9,508	7,885	24,490	15,713
Amortization of intangibles	1,226	1,454	2,603	2,941
Marketing and advertising	8,938	8,982	17,768	18,757
Office services and equipment	5,102	5,287	10,238	10,197
Other real estate owned	1,094	2,372	3,825	3,805
FDIC assessments	5,276	2,765	10,370	4,156

Other operating	11,660	9,527	20,513	18,332
Total noninterest expense	231,660	221,582	466,102	432,434
Income before income taxes	106,663	101,080	199,379	186,619
Income taxes	37,684	35,109	68,281	66,119
Net income	$ 68,979	$ 65,971	$ 131,098	$ 120,500
Less: Net income attributable to noncontrolling interest	480	510	1,033	1,209
Net income attributable to City National Corporation	$ 68,499	$ 65,461	$ 130,065	$ 119,291
Less: Dividends on preferred stock	4,094	4,094	8,188	8,188
Net income available to common shareholders	$ 64,405	$ 61,367	$ 121,877	$ 111,103
Net income per common share, basic	$ 1.15	$ 1.11	$ 2.17	$ 2.01
Net income per common share, diluted	$ 1.13	$ 1.09	$ 2.14	$ 1.98
Weighted-average common shares outstanding, basic	55,748	54,957	55,586	54,824
Weighted-average common shares outstanding, diluted	56,663	55,632	56,484	55,541
Dividends per common share	$ 0.35	$ 0.33	$ 0.70	$ 0.66

See accompanying Notes to the Unaudited Consolidated Financial Statements.

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CITY NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

(in thousands)	For the three months ended June 30, 2015	For the three months ended June 30, 2014	For the six months ended June 30, 2015	For the six months ended June 30, 2014
Net income	$ 68,979	$ 65,971	$ 131,098	$ 120,500
Other comprehensive (loss) income, net of tax:				
Securities available-for-sale:				
Net unrealized (losses) gains arising during the period	(6,406)	9,764	7,679	22,317
Reclassification adjustment for net gains included in net income	(178)	(3,117)	(2,147)	(4,392)
Non-credit related impairment loss	(211)	(184)	(211)	(184)
Foreign currency translation adjustments	4		(7)	
Total other comprehensive (loss) income	(6,791)	6,463	5,314	17,741
Comprehensive income	$ 62,188	$ 72,434	$ 136,412	$ 138,241
Less: Comprehensive income attributable to noncontrolling interest	480	510	1,033	1,209
Comprehensive income attributable to City National Corporation	$ 61,708	$ 71,924	$ 135,379	$ 137,032

See accompanying Notes to the Unaudited Consolidated Financial Statements.

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CITY NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(in thousands)	For the six months ended June 30, 2015	2014
Cash Flows From Operating Activities		
Net income	$ 131,098	$ 120,500
Adjustments to net income:		
(Reversal of) provision for credit losses on loans and leases, excluding covered loans	10,000	(1,000)
Provision for losses on covered loans	1,588	3,194
Depreciation and amortization	24,490	15,713
Amortization of intangibles	2,603	2,941
Share-based employee compensation expense	11,246	10,636
Deferred income tax benefit	(7,905)	(3,492)
Gain on disposal of assets	(1,648)	(9,664)
Gain on sale of securities	(5,300)	(7,489)
Impairment loss on securities	336	248
Other, net	16,367	17,383
Net change in:		
Trading securities	62,949	(3,802)
Other assets and other liabilities, net	(38,204)	(22,392)
Net cash provided by operating activities	207,620	122,776
Cash Flows From Investing Activities		
Purchase of securities available-for-sale	(823,320)	(820,540)
Sales of securities available-for-sale	400,803	626,055
Maturities and paydowns of securities available-for-sale	1,366,066	1,133,677
Purchase of securities held-to-maturity	(148,849)	(537,894)
Maturities and paydowns of securities held-to-maturity	151,613	75,409
Loan originations, net of principal collections	(1,492,182)	(1,171,116)
Net payments for premises and equipment	(22,714)	(22,614)
Other investing activities, net	(140)	19,224
Net cash used in investing activities	(568,723)	(697,799)
Cash Flows From Financing Activities		
Net increase in deposits	1,373,127	972,088
Net (decrease) increase in federal funds purchased	(320,000)	50,000
Issuance of long-term debt	29,609	18,070
Repayment of long-term debt	(24,126)	(19,765)
Proceeds from exercise of stock options	28,996	16,387
Tax benefit from exercise of stock options	5,521	3,240
Cash dividends paid	(47,042)	(44,374)
Other financing activities, net	(3,546)	(16,252)
Net cash provided by financing activities	1,042,539	979,394
Net increase in cash and cash equivalents	681,436	404,371
Cash and cash equivalents at beginning of year	656,451	935,946
Cash and cash equivalents at end of period	$ 1,337,887	$ 1,340,317
Supplemental Disclosures of Cash Flow Information:		
Cash paid during the period for:		

Interest	$	21,656	$	26,484
Income taxes		62,645		55,461
Non-cash investing activities:				
Transfer of loans to other real estate owned	$	3,915	$	4,131

See accompanying Notes to the Unaudited Consolidated Financial Statements.

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CITY NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

(Unaudited)

(in thousands, except share amounts)	Common shares issued	Preferred stock	Common stock	Additional paid-in capital	Accumulated other comprehensive income (loss)	Retained earnings	Treasury shares	Total shareholders equity
Balance, December 31, 2013	54,667,295	$ 267,616	$ 54,667	$ 541,210	$ (15,641)	$ 1,918,163	$ (25,029)	$ 2,740,986
Adjustment to initially apply Accounting Standards Update 2014-01						(11,941)		(11,941)
Balance, January 1, 2014	54,667,295	267,616	54,667	541,210	(15,641)	1,906,222	(25,029)	2,729,045
Net income (1)						119,291		119,291
Other comprehensive income, net of tax					17,741			17,741
Issuance of shares under share-based compensation plans	289,544		290	9,653			2,581	12,524
Share-based employee compensation expense				8,875				8,875
Tax benefit from share-based compensation plans				3,306				3,306
Dividends:								
Preferred						(8,188)		(8,188)
Common						(36,541)		(36,541)
Net change in deferred compensation plans				741			(2)	739
Change in redeemable noncontrolling interest				(7,501)				(7,501)
Balance, June 30, 2014	54,956,839	$ 267,616	$ 54,957	$ 556,284	$ 2,100	$ 1,980,784	$ (22,450)	$ 2,839,291
Balance, December 31, 2014	55,162,455	$ 267,616	$ 55,162	$ 578,046	$ (7,074)	$ 2,071,230	$ (22,279)	$ 2,942,701
Net income (1)						130,065		130,065
Other comprehensive income, net of tax					5,314			5,314
Issuance of shares under share-based compensation plans	501,192		501	21,793			3,666	25,960
Share-based employee compensation expense				8,279				8,279
Tax benefit from share-based compensation plans				7,906				7,906
Dividends:								
Preferred						(8,188)		(8,188)
Common						(39,236)		(39,236)
Net change in deferred compensation plans	480		1	782			(1)	782
Change in redeemable noncontrolling interest				(1,435)				(1,435)
Balance, June 30, 2015	55,664,127	$ 267,616	$ 55,664	$ 615,371	$ (1,760)	$ 2,153,871	$ (18,614)	$ 3,072,148

(1) Net income excludes net income attributable to redeemable noncontrolling interest of $1,033 and $1,209 for the six-month periods ended June 30, 2015 and 2014, respectively. Redeemable noncontrolling interest is reflected in the mezzanine section of the consolidated balance sheets. See Note 17 of the Notes to the Unaudited Consolidated Financial Statements.

See accompanying Notes to the Unaudited Consolidated Financial Statements.

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CITY NATIONAL CORPORATION

NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Summary of Significant Accounting Policies

Organization

City National Corporation (the Corporation) is the holding company for City National Bank (the Bank). The Bank delivers banking, investment and trust services through 75 offices in Southern California, the San Francisco Bay area, Nevada, New York City, Nashville, Tennessee and Atlanta, Georgia. As of June 30, 2015, the Corporation had four consolidated investment advisory affiliates and one unconsolidated subsidiary, Business Bancorp Capital Trust I. Because the Bank comprises substantially all of the business of the Corporation, references to the Company mean the Corporation and the Bank together. The Corporation is approved as a financial holding company pursuant to the Gramm-Leach-Bliley Act of 1999.

Consolidation

The consolidated financial statements of the Company include the accounts of the Corporation, its non-bank subsidiaries, the Bank and the Bank s wholly owned subsidiaries, after the elimination of all material intercompany transactions. It also includes noncontrolling interest, which is the portion of equity in a subsidiary not attributable to a parent. Redeemable noncontrolling interests are noncontrolling ownership interests that are redeemable at the option of the holder or outside the control of the issuer. The redeemable noncontrolling interests of third parties in the Corporation s investment advisory affiliates are not considered to be permanent equity and are reflected in the mezzanine section between liabilities and equity in the consolidated balance sheets. Noncontrolling interests share of subsidiary earnings is reflected as Net income attributable to noncontrolling interest in the consolidated statements of income.

The Company s investment management and wealth advisory affiliates are organized as limited liability companies. The Corporation generally owns a majority position in each affiliate and certain management members of each affiliate own the remaining shares. The Corporation has contractual arrangements with its affiliates whereby a percentage of revenue is allocable to fund affiliate operating expenses (operating share) while the remaining portion of revenue (distributable revenue) is allocable to the Corporation and the noncontrolling owners. All majority-owned affiliates that meet the prescribed criteria for consolidation are consolidated. The Corporation s interests in investment management affiliates in which it holds a noncontrolling share are accounted for using the equity method. Additionally, the Company has various interests in variable interest entities (VIEs) that are not required to be consolidated. See Note 16 for a more detailed discussion on VIEs.

Use of Estimates

The Company s accounting and reporting policies conform to generally accepted accounting principles (GAAP) and practices in the financial services industry. To prepare the financial statements in conformity with GAAP, management must make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, and income and expenses during the reporting period. Circumstances and events that differ significantly from those underlying the Company s estimates and assumptions could cause actual financial results to differ from those estimates. The material estimates included in the financial statements relate to the allowance for loan and lease losses, the reserve for off-balance sheet credit commitments, other real estate owned (OREO), valuation of share-based compensation awards, income taxes, goodwill and intangible asset impairment, securities impairment, private equity and alternative investments impairment, valuation of assets and liabilities acquired in business combinations, including contingent consideration liabilities, subsequent valuations of acquired impaired loans, Federal Deposit Insurance Corporation (FDIC) indemnification asset, valuation of noncontrolling interest, and the valuation of financial assets and liabilities reported at fair value.

The Company has applied its critical accounting policies and estimation methods consistently in all periods presented in these financial statements. The Company s estimates and assumptions are expected to change as changes in market conditions and the Company s portfolio occur in subsequent periods.

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Note 1. Summary of Significant Accounting Policies (Continued)

Basis of Presentation

The Company is on the accrual basis of accounting for income and expenses. The results of operations reflect any adjustments, all of which are of a normal recurring nature, unless otherwise disclosed in this Form 10-Q, and which, in the opinion of management, are necessary for a fair presentation of the results for the periods presented. In accordance with the usual practice of banks, assets and liabilities of individual trust, agency and fiduciary funds have not been included in the financial statements. These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2014.

The results for the 2015 interim periods are not necessarily indicative of the results expected for the full year. The Company has not made any significant changes in its critical accounting policies or in its estimates and assumptions from those disclosed in its 2014 Annual Report other than the adoption of new accounting pronouncements and other authoritative guidance that became effective for the Company on or after January 1, 2015. Refer to *Accounting Pronouncements* for discussion of accounting pronouncements adopted in 2015.

Certain prior period amounts have been reclassified to conform to the current period presentation.

Accounting Pronouncements

The following is a summary of accounting pronouncements that became effective during the six months ended June 30, 2015:

- In January 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-01, *Investments Equity Method and Joint Ventures (Topic 323), Accounting for Investments in Qualified Affordable Housing Projects* (ASU 2014-01). ASU 2014-01 permits an entity to make an accounting policy election to apply a proportionate amortization method to its low income housing tax credit investments if certain conditions are met. Under the proportionate amortization method, an investor amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received, and recognizes the amortization in the income statement as a component of income taxes attributable to continuing operations. On January 1, 2015, the Company adopted ASU 2014-01 and elected to apply the proportionate amortization method to its low income housing tax credit investments. Following adoption, the Company recognizes amortization of its tax credit investments as a component of income taxes. The Company previously recognized amortization as a component of noninterest expense. Prior periods presented in the Company s consolidated financial statements have been adjusted to reflect retrospective adoption of ASU 2014-01 as follows:

(in thousands)	Consolidated Balance Sheet As of December 31, 2014 As Reported	As Adjusted (Unaudited)
Assets		
Deferred tax asset	$ 230,376	$ 233,811
Affordable housing investments	203,010	186,423
Other assets	537,826	537,847
Shareholders equity		
Retained earnings	2,084,361	2,071,230

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Note 1. Summary of Significant Accounting Policies (Continued)

(in thousands, except per share amounts)	Consolidated Statement of Income For the three months ended June 30, 2014 As Reported	As Adjusted	For the six months ended June 30, 2014 As Reported	As Adjusted
	(Unaudited)		(Unaudited)	
Noninterest expense				
Other operating	$ 13,567	$ 9,527	$ 26,413	$ 18,332
Income taxes	29,829	35,109	56,117	66,119
Net income	67,211	65,971	122,421	120,500
Net income per common share, basic	$ 1.13	$ 1.11	$ 2.04	$ 2.01
Net income per common share, diluted	$ 1.11	$ 1.09	$ 2.01	$ 1.98

(in thousands)	Consolidated Statement of Cash Flows For the six months ended June 30, 2014 As Reported	As Adjusted
	(Unaudited)	
Cash Flows From Operating Activities		
Net income	$ 122,421	$ 120,500
Adjustments to net income:		
Deferred income tax benefit	(2,934)	(3,492)
Other, net	14,926	17,383
Net change in:		
Other assets and other liabilities, net	(22,414)	(22,392)

• In January 2014, the FASB issued ASU 2014-04, *Receivables Troubled Debt Restructurings by Creditors (Subtopic 310-40), Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure* (ASU 2014-04). ASU 2014-04 requires entities to reclassify consumer mortgage loans collateralized by residential real estate to OREO when either (1) the creditor obtains legal title to the residential real estate property or (2) the borrower conveys all interest in the property to the creditor to satisfy the loan by completing a deed in lieu of foreclosure or similar agreement. The Company adopted ASU 2014-04 effective January 1, 2015 on a prospective basis. Adoption of the new guidance did not have a significant impact on the Company s consolidated financial statements.

• In April 2014, the FASB issued ASU 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity* (ASU 2014-08). ASU 2014-08 raises the threshold for a disposal to qualify as a discontinued operation and requires new disclosures of both discontinued operations and certain other disposals that do not meet the definition of a discontinued operation. The Company adopted ASU 2014-08 effective January 1, 2015 on a prospective basis. Adoption of the new guidance did not have a significant impact on the Company s consolidated financial statements.

- In June 2014, the FASB issued ASU 2014-11, *Transfers and Servicing (Topic 860), Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures* (ASU 2014-11). ASU 2014-11 aligns the accounting for repurchase-to-maturity transactions and repurchase agreements executed as a repurchase financing with the accounting for other repurchase agreements. Going forward, these transactions will all be accounted for as secured borrowings. Under the new guidance, parties to a repurchase financing transaction will be required to separately account for the initial transfer of the financial asset and the related repurchase agreement. The initial transfer of the financial asset would be accounted for as a sale by the transferor only if all criteria for derecognition have been met. ASU 2014-11 requires new or expanded disclosures for repurchase agreements and similar transactions accounted for as secured borrowings. The Company adopted ASU 2014-11 effective January 1, 2015. Adoption of the new guidance did not have a significant impact on the Company s consolidated financial statements.

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Note 1. Summary of Significant Accounting Policies (Continued)

The following is a summary of recently issued accounting pronouncements:

- In February 2015, the FASB issued ASU 2015-02, *Consolidation (Topic 810): Amendments to the Consolidation Analysis*, which significantly changes the consolidation analysis required under U.S. GAAP. The new consolidation guidance maintains two models: one for assessing most corporate entities based on the notion that majority voting rights indicate control (the voting model) and another for assessing entities that may be controlled through other means, such as management contracts or subordinated financial support (the variable interest model). Under the new guidance, limited partnerships will be VIEs, unless the limited partners have either substantive kick-out or participating rights. The ASU also changes the effect that fees paid to a decision maker or service provider have on the consolidation analysis. For entities other than limited partnerships, the ASU clarifies how to determine whether the equity holders (as a group) have power over the entity. The ASU is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2015. Early adoption is allowed for all entities, but the guidance must be applied as of the beginning of the annual period containing the adoption date. Entities have the option of using either a full or modified retrospective approach for adoption. The Company is assessing the impact of the new guidance on its consolidated financial statements.

- In April 2015, the FASB issued ASU 2015-03, *Interest Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*, which requires the debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The ASU is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2015. Early adoption is permitted. The amendments in this ASU are to be applied on a retrospective basis. Adoption of the new guidance is not expected to have a significant impact on the Company s consolidated financial statements.

- In April 2015, the FASB issued ASU 2015-05, *Intangibles Goodwill and Other Internal-Use Software (Subtopic 350-40): Customer s Accounting for Fees Paid in a Cloud Computing Arrangement*. Cloud computing arrangements include: (a) software as a service; (b) platform as a service; (c) infrastructure as a service; and (d) other similar hosting arrangements. Under the ASU, if a cloud computing arrangement contains a software license, the customer would account for the fees related to the software license element in a manner consistent with how the acquisition of other software licenses is accounted for under ASC 350-40. If the arrangement does not contain a software license, the customer would account for the arrangement as a service contract. The ASU is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2015. Early adoption is permitted. Entities may adopt the guidance either (1) prospectively to arrangements entered into or materially modified after the effective date, or (2) retrospectively. The Company is assessing the impact of the new guidance on its consolidated financial statements.

- In July 2015, the FASB approved to defer by one year the effective dates of its revenue recognition standard ASU 2014-09, *Revenue from Contracts with Customers: Topic 606.* As a result, the standard would be effective for public entities for annual reporting periods, and interim periods within those annual periods, beginning after December 15, 2017.

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Note 2. Fair Value Measurements

The following tables summarize assets and liabilities measured at fair value as of June 30, 2015 and December 31, 2014 by level in the fair value hierarchy:

		Fair Value Measurements at Reporting Date Using		
(in thousands)	Balance as of June 30, 2015	Quoted Prices in Active Markets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Measured on a Recurring Basis				
Assets				
Securities available-for-sale:				
U.S. Treasury	$ 148,308	$ 148,308	$	$
Federal agency - Debt	899,934		899,934	
Federal agency - MBS	96,878		96,878	
CMOs - Federal agency	3,286,076		3,286,076	
CMOs - Non-agency	21,731		21,731	
State and municipal	400,055		396,509	3,546
Other debt securities	87,395		87,395	
Equity securities and mutual funds	466	466		
Trading securities	110,136	103,999	6,137	
Derivative assets (1)	51,671	6,597	43,201	1,873
Contingent consideration asset (1)	2,605			2,605
Total assets at fair value	$ 5,105,255	$ 259,370	$ 4,837,861	$ 8,024
Liabilities				
Derivative liabilities	$ 49,587	$ 6,235	$ 43,352	$
Contingent consideration liability	36,573			36,573
FDIC clawback liability	16,289			16,289
Other liabilities	850		850	
Total liabilities at fair value (2)	$ 103,299	$ 6,235	$ 44,202	$ 52,862
Redeemable noncontrolling interest	$ 37,755	$	$	$ 37,755
Measured on a Nonrecurring Basis				
Assets				
Other real estate owned (3)	$ 5,577	$	$ 635	$ 4,942
Private equity and alternative investments	4,434			4,434
Total assets at fair value	$ 10,011	$	$ 635	$ 9,376

(1) Reported in Other assets in the consolidated balance sheets.

(2) Reported in Other liabilities in the consolidated balance sheets.

(3) Includes covered OREO.

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Note 2. Fair Value Measurements (Continued)

(in thousands)	Balance as of December 31, 2014	Fair Value Measurements at Reporting Date Using Quoted Prices in Active Markets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Measured on a Recurring Basis				
Assets				
Securities available-for-sale:				
U.S. Treasury	$ 116,926	$ 116,926	$	$
Federal agency - Debt	1,398,581		1,398,581	
Federal agency - MBS	104,526		104,526	
CMOs - Federal agency	3,580,590		3,580,590	
CMOs - Non-agency	24,014		24,014	
State and municipal	479,031		475,484	3,547
Other debt securities	176,169		176,169	
Equity securities and mutual funds	3,146	3,146		
Trading securities	173,188	171,778	1,410	
Derivative assets (1)	51,586	6,106	44,598	882
Contingent consideration asset (1)	2,930			2,930
Total assets at fair value	$ 6,110,687	$ 297,956	$ 5,805,372	$ 7,359
Liabilities				
Derivative liabilities	$ 51,309	$ 6,623	$ 44,686	$
Contingent consideration liability	34,983			34,983
FDIC clawback liability	15,106			15,106
Other liabilities	946		946	
Total liabilities at fair value (2)	$ 102,344	$ 6,623	$ 45,632	$ 50,089
Redeemable noncontrolling interest	$ 39,978	$	$	$ 39,978
Measured on a Nonrecurring Basis				
Assets				
Other real estate owned (3)	$ 5,644	$	$	$ 5,644
Total assets at fair value	$ 5,644	$	$	$ 5,644

(1) Reported in Other assets in the consolidated balance sheets.

(2) Reported in Other liabilities in the consolidated balance sheets.

(3) Includes covered OREO.

At June 30, 2015, $5.11 billion, or approximately 15 percent, of the Company s total assets were recorded at fair value on a recurring basis, compared with $6.11 billion, or 19 percent, at December 31, 2014. The majority of these financial assets were valued using Level 1 or Level 2 inputs. Less than one percent of total assets were measured using Level 3 inputs. At June 30, 2015, $103.3 million of the Company s total liabilities were recorded at fair value using mostly Level 2 or Level 3 inputs, compared with $102.3 million at December 31, 2014. There were no transfers between Level 1 and Level 2 of the fair value hierarchy for assets or liabilities measured on a recurring basis during the six months ended June 30, 2015. At June 30, 2015, $10.0 million of the Company s total assets were recorded at fair value on a nonrecurring basis, compared with $5.6 million at December 31, 2014. These assets represent less than one percent of total assets and were measured using Level 2 or Level 3 inputs.

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Note 2. Fair Value Measurements (Continued)

Recurring Fair Value Measurements

Assets and liabilities for which fair value measurement is based on significant unobservable inputs are classified as Level 3 in the fair value hierarchy. The following table provides a reconciliation of the beginning and ending balances for Level 3 assets and liabilities measured at fair value on a recurring basis for the six months ended June 30, 2015 and 2014.

Level 3 Assets and Liabilities Measured on a Recurring Basis

	For the six months ended June 30, 2015				
(in thousands)	**Securities Available-for-Sale**	**Equity Warrants**	**Contingent Consideration Asset**	**Contingent Consideration Liability**	**FDIC Clawback Liability**
Balance, beginning of period	$ 3,547	$ 882	$ 2,930	$ (34,983)	$ (15,106)
Total realized/unrealized gains (losses):					
Included in earnings		103	(325)	(754)	(1,183)
Included in other comprehensive income	(1)				
Additions		888			
Other (1)				(836)	
Balance, end of period	$ 3,546	$ 1,873	$ 2,605	$ (36,573)	$ (16,289)

	For the six months ended June 30, 2014			
(in thousands)	**Securities Available-for-Sale**	**Equity Warrants**	**Contingent Consideration Liability**	**FDIC Clawback Liability**
Balance, beginning of period	$ 3,633	$	$ (49,900)	$ (11,967)
Total realized/unrealized gains (losses):				
Included in earnings		78		(2,112)
Included in other comprehensive income	(16)			
Additions		489		
Settlements		(2)	16,250	
Other (1)			(813)	
Balance, end of period	$ 3,617	$ 565	$ (34,463)	$ (14,079)

(1) Other rollforward activity consists of accretion of discount related to the contingent consideration liability.

Redeemable noncontrolling interest is classified as Level 3 in the fair value hierarchy and measured on a recurring basis. Redeemable noncontrolling interest is valued based on a combination of factors, including but not limited to, observable valuation of firms similar to the affiliates, multiples of revenue or profit, unique investment products or performance track records, strength in the marketplace, projected discounted cash flow scenarios, strategic value of affiliates to other entities, as well as unique sources of value specific to an individual firm. The methodology used to fair value these interests is consistent with the industry practice of valuing similar types of instruments. Refer to Note 17, *Noncontrolling Interest*, for a rollforward of activity for the six months ended June 30, 2015 and 2014.

Level 3 assets measured at fair value on a recurring basis include municipal auction rate securities that are classified in securities available-for-sale, a contingent consideration asset and equity warrants classified as derivative assets. Municipal auction rate securities were valued using an average yield on California variable rate notes that were comparable in credit rating and maturity to the securities held, plus a liquidity premium. The contingent consideration asset represents the fair value of future payments to be received on the sale of the Company s retirement services recordkeeping business. The fair value of contingent consideration was determined by discounting the expected future cash flows using a bond rate for an investment grade finance company. Equity warrants in private companies obtained in association with certain loan transactions are measured at fair value on a recurring basis using the Black-Scholes option pricing model. Key inputs to the valuation model include current share estimated fair value, strike price, volatility, expected life, risk-free interest rate, and market and liquidity discounts. Several of the inputs to the valuation model incorporate assumptions by management that are not observable in the market; consequently, the valuation of warrants is classified in Level 3 of the fair value hierarchy. Refer to Note 11, *Derivative Instruments,* for additional discussion of equity warrants.

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Note 2. Fair Value Measurements (Continued)

Level 3 liabilities measured at fair value on a recurring basis consist of contingent consideration and an FDIC clawback liability that are included in other liabilities. As part of its acquisition of Rochdale Investment Management, LLC and associated entities (collectively, Rochdale), the Company entered into a contingent consideration arrangement that requires the Company to pay additional cash consideration to Rochdale s former shareholders at certain points in time over the six years after the date of acquisition if certain criteria, such as revenue growth and pre-tax margin, are met. In 2014, the Company made total contingent consideration payments to Rochdale s former shareholders of approximately $17.4 million. The fair value of the remaining contingent consideration was estimated using a probability-weighted discounted cash flow model. Although the acquisition agreement does not set a limit on the total payment, the Company estimates that the remaining consideration payment could be in the range of $16 million to $47 million, but will ultimately be determined based on actual future results. The contingent consideration liability is remeasured to fair value at each reporting date until its settlement.

The FDIC clawback liability was valued using the discounted cash flow method based on the terms specified in loss-sharing agreements with the FDIC, the actual FDIC payments collected, and the following unobservable inputs: (1) risk-adjusted discount rate reflecting the Bank s credit risk, plus a liquidity premium, and (2) loan performance assumptions such as prepayments and losses.

There were no transfers into or out of Level 3 assets or liabilities measured on a recurring basis during the six months ended June 30, 2015 and 2014.

Nonrecurring Fair Value Measurements

Assets measured at fair value on a nonrecurring basis using significant unobservable inputs include certain collateral dependent impaired loans, OREO for which fair value is not solely based on market observable inputs, and certain private equity and alternative investments. Private equity and alternative investments do not have readily determinable fair values. These investments are carried at cost and evaluated for impairment on a quarterly basis. Due to the lack of readily determinable fair values for these investments, the impairment assessment is based primarily on a review of investment performance and whether the Company expects to recover the cost of an investment.

The table below provides information about valuation method, inputs and assumptions for nonrecurring Level 3 fair value measurements. The weight assigned to each input is based on the facts and circumstances that exist at the date of measurement.

Information About Nonrecurring Level 3 Fair Value Measurements

(in thousands)		Fair Value at June 30, 2015	Valuation Method	Unobservable Inputs
Other real estate owned	$	4,942	Third-party appraisal	- Fair values are primarily based on unadjusted appraised values.

				- One property is valued using comparable sales values resulting in discount to appraised value of 12%.
Private equity and alternative investments	$	4,434	See note (1)	- See note (1) - Fair values reflect discounts to investment carrying amounts ranging from 14% to 50%.

(1) Fair values are based on management s assumptions regarding recoverability of an investment based on a range of factors including, but not limited to, nature and age of the investment, actual and forecasted investment performance, fund operating results, recent and planned transactions, general and industry specific market conditions, performance of comparable companies and investment exit strategies.

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Note 2. Fair Value Measurements (Continued)

For assets measured at fair value on a nonrecurring basis, the following table presents the total net gains and losses, which include charge-offs, recoveries, specific reserves, OREO valuation write-downs and write-ups, gains and losses on sales of OREO, and impairment write-downs on private equity investments, recognized in the three and six months ended June 30, 2015 and 2014:

	For the three months ended June 30,		For the six months ended June 30,	
(in thousands)	**2015**	**2014**	**2015**	**2014**
Collateral dependent impaired loans:				
Commercial real estate mortgages	$	$	$	$ (5)
Residential mortgages		74		74
Other real estate owned (1)	318	1,006	(1,319)	1,067
Private equity and alternative investments	(1,230)		(1,630)	
Total net (losses) gains recognized	$ (912)	$ 1,080	$ (2,949)	$ 1,136

(1) Net gains and losses on OREO include amounts related to covered OREO, a significant portion of which is payable to or reimbursable by the FDIC.

Fair Value of Financial Instruments

A financial instrument is broadly defined as cash, evidence of an ownership interest in another entity, or a contract that imposes a contractual obligation on one entity and conveys a corresponding right to a second entity to require delivery or exchange of financial assets or liabilities. Refer to Note 1, *Summary of Significant Accounting Policies,* in the Company s 2014 Form 10-K for additional information on fair value measurements.

The disclosure does not include estimated fair value amounts for assets and liabilities which are not defined as financial instruments but which have significant value. These assets and liabilities include the value of customer-relationship intangibles, goodwill, affordable housing investments carried at cost, other assets, deferred taxes and other liabilities. Accordingly, the total of the fair values presented does not represent the underlying value of the Company.

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Note 2. Fair Value Measurements (Continued)

The following tables summarize the carrying amounts and estimated fair values of those financial instruments that are reported at amortized cost in the Company s consolidated balance sheets. The tables also provide information on the level in the fair value hierarchy for inputs used in determining the fair value of those financial instruments. Most financial assets and financial liabilities for which carrying amount equals fair value are considered by the Company to be Level 1 measurements in the fair value hierarchy.

	June 30, 2015				
	Carrying	Total	Fair Value Measurements Using		
(in millions)	Amount	Fair Value	Level 1	Level 2	Level 3