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Elan Corporation, plc

Half-Year Financial Report

Six Months Ended 30 June 2011

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CHIEF EXECUTIVE OFFICER S STATEMENT

To Our Shareholders:

During the first half of 2011, Elan delivered significant financial advancement, announced a strategic transaction that will lay the foundation for the Company in the years to come and added to the depth and breadth of our discovery/research activities. Adjusted Earnings Before Interest Tax Depreciation and Amortisation (EBITDA) increased by 49% over the same period in 2010 as overall financial results continue to improve (see page 13 for a reconciliation of Adjusted EBITDA to IFRS net income/(loss)). The significant increase in Adjusted EBITDA principally reflects a continuation in revenue growth coupled with an increase in operating margins being driven by a business structure that allows a portfolio approach to costs and investments against expected timelines, results and overall performance.

Revenue increases for the BioNeurology business were driven by growth of *Tysabri*®, which recorded in-market sales of $738.4 million in the first half of 2011, an increase of 25% over the $589.4 million recorded in the same period of 2010. At the end of June 2011, approximately 61,500 patients were on therapy worldwide, an increase of 15% over the 53,300 (revised) who were on therapy at the end of June 2010.

We continue to work closely with our collaborator on *Tysabri*, Biogen Idec, Inc. (Biogen Idec), as well as the clinical and scientific communities, to create significant understanding in both efficacy and safety of the therapy so it may be best positioned to the maximum clinical benefit of patients. Importantly, in June 2011, the European Commission (EC) approved the inclusion of the anti-JC virus (JCV) antibody status as an additional factor in stratifying patients at risk for developing progressive multifocal leukoencephalopathy (PML) in the survey of Product Characteristics for *Tysabri* in the European Union. In addition, as part of a standard review process, the EC concluded the quality, safety and efficacy of *Tysabri* continue to be adequately demonstrated, and renewed *Tysabri s* five year marketing authorization in the EU. Elan and Biogen have filed for a similar label update with the U.S. Food and Drug Administration (FDA) and expect to hear a response in the second half of 2011.

In May 2011, we announced the signing of an agreement to merge our Elan Drug Technologies (EDT) business with Alkermes, Inc. (Alkermes), a transaction that we believe provides a clear strategic pathway for Elan while, at the same time, providing significant benefit to our shareholders. The newly formed Alkermes plc will have a diversity of assets, a balance of expertise and will be cash flow positive from an operating point of view upon the closing of the transaction. In consideration for this transaction, we will receive $500 million in cash and 31.9 million shares of Alkermes plc common stock upon closing of the transaction. We intend to use the proceeds to further reduce our debt and continue to strengthen our balance sheet and overall capital structure. We expect the EDT transaction to close in the third quarter of 2011.

Also in May 2011, we entered a strategic business relationship with Proteostasis Therapeutics, Inc. (Proteostasis) to advance the discovery and development of disease modifying small molecule drugs and diagnostics for the treatment of neurodegenerative disorders and a broad array of dementia related diseases including Alzheimer s disease. This innovative initiative will combine Proteostasis unique discovery technology, novel targets and compounds that modulate key Proteostasis network pathways with our longstanding strength in proprietary animal models, biology, medicinal chemistry and clinical development. We invested $20 million into the equity capital of Proteostasis and became a 24% shareholder. We will have the opportunity to invest an additional $30 million in collaboration funding over five years and retain the right of first negotiation to exclusively license potential compounds.

As part of our on-going effort to engage best in class business partners, we announced a global technical development and manufacturing agreement for antibody based therapeutics with Boehringer Ingelheim. In addition, we formed a global business collaboration with Pharmaceutical Product Development, Inc. (PPD) to focus the advancement and execution of our clinical development portfolio. Both of these important initiatives will allow us to advance our science and therapeutics in a flexible, cost efficient manner and further combine outstanding science with a business model that allows for flexibility, scale and operating leverage.

We look forward to and expect to make continued progress on all aspects of our business. Elan will remain a company that has as its core distinctive science and an ability to translate that science into possible therapies that may offer the opportunity to help millions of patients around the world. In doing so, we expect to create shareholder value over time and through cycles as we dynamically manage a portfolio of science, clinical assets, cash flows, timelines, risks and capital structure to achieve our goal of attaining clear leadership within the industry.

G. Kelly Martin

Chief Executive Officer

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HALF-YEAR MANAGEMENT REPORT

In connection with the proposed merger, Alkermes plc has filed with the Securities and Exchange Commission (SEC) a registration statement that includes a preliminary prospectus regarding the proposed merger and Alkermes, Inc. has filed with the SEC a proxy statement in respect of the proposed merger. The definitive proxy statement/prospectus will be mailed to the stockholders of Alkermes, Inc. INVESTORS ARE URGED TO CAREFULLY READ THE REGISTRATION STATEMENT AND THE PROXY STATEMENT/PROSPECTUS AND OTHER MATERIALS REGARDING THE PROPOSED MERGER BECAUSE THEY WILL CONTAIN IMPORTANT INFORMATION ABOUT ALKERMES, INC. AND EDT AND THE PROPOSED TRANSACTION. Investors may obtain a free copy of the registration statement and the proxy statement/prospectus and other documents containing information about EDT and Alkermes, Inc., without charge, at the SEC s website at www.sec.gov. Copies of the proxy statement/prospectus and the filings with the SEC that will be incorporated by reference in the proxy statement/prospectus can also be obtained, without charge, from Elan s website www.elan.com.

This communication does not constitute an offer to sell, or the solicitation of an offer to sell, or the solicitation of an offer to subscribe for, or buy, any securities, nor shall there be any sale, issuance or transfer of securities in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such jurisdiction.

Introduction

This Half-Year Financial Report for the six months ended 30 June 2011 meets the reporting requirements pursuant to the Transparency (Directive 2004/109/EC) Regulations 2007 and the related Transparency Rules of the Republic of Ireland s Financial Regulator.

This half-year management report includes the following:

- Business overview, including important events that have occurred during the half-year;
- Selected financial data;
- Principal risks and uncertainties relating to the remaining six months of the year;
- Results of operations for continuing and discontinued operations for the first half 2011, compared to the first half of 2010;
- Reconciliation of net income/(loss) to Adjusted EBITDA non-GAAP financial information;
- Liquid resources and shareholders equity;
- Cash flows summary;
- Debt facilities;
- Related party transactions; and

Directors.

Business Overview

Elan Corporation, plc, an Irish public limited company (also referred to hereafter as we , our , us , Elan and the Company), is a neuroscience-b biotechnology company, listed on the Irish and New York Stock Exchanges, and headquartered in Dublin, Ireland. We were incorporated as a private limited company in Ireland in December 1969 and became a public limited company in January 1984. Our registered office and principal executive offices are located at Treasury Building, Lower Grand Canal Street, Dublin 2, Ireland and our telephone number is +353-1-709-4000. As of 30 June 2011, we employed over 1,000 people and our principal research and development (R&D), manufacturing and marketing facilities are located in Ireland and the United States.

Our operations are organised into two business units; BioNeurology and EDT. BioNeurology engages in research, development and commercial activities primarily in the areas of Alzheimer s disease, Parkinson s disease and multiple sclerosis (MS). EDT is an established, profitable, integrated drug delivery business unit of Elan, which has been applying its skills and knowledge in product development and drug delivery technologies to enhance the performance of dozens of drugs that have been marketed worldwide.

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EDT Transaction

On 9 May 2011, Alkermes and Elan announced the execution of a definitive agreement under which Alkermes will merge with EDT in a cash and stock transaction valued at approximately $960 million as of the date of announcement. Alkermes and EDT will be combined under a new holding company incorporated in Ireland. This newly created company will be named Alkermes plc.

In connection with the transaction, at closing, we will receive $500 million in cash and 31.9 million ordinary shares of Alkermes plc common stock. Existing shareholders of Alkermes will receive one ordinary share of Alkermes plc in exchange for each share of Alkermes they own at the time of the merger. Alkermes plc shares will be registered in the United States and are expected to trade on the NASDAQ exchange.

On the closing of the transaction, we will hold approximately 25% of the equity of Alkermes plc, with the existing shareholders of Alkermes holding the remaining 75% of the equity. We will account for our equity investment in Alkermes plc as an investment in an associate and expect to record a substantial gain on the disposal of EDT when the transaction closes. We intend to use the net cash proceeds from the transaction to retire debt.

The transaction is subject to approval by Alkermes stockholders and the satisfaction of customary closing conditions and regulatory approvals. The transaction is expected to close during the third quarter of 2011. We refer to this transaction as the EDT Transaction in this Half-Year Financial Report.

Following the approval of the EDT Transaction by the Board of Elan on 8 May 2011, the EDT business met the criteria to be classified as held for sale and the assets and liabilities of EDT have been classified as held for sale on the half-year balance sheet at 30 June 2011. The results of EDT are presented as a discontinued operation in the half-year income statement for the first half of 2011 and the comparative amounts have been restated to reflect this classification.

Summary of Operating Performance

Our continuing operations solely relate to the BioNeurology business. Total revenue for the BioNeurology business increased by 12% to $324.9 million in the first half of 2011, compared to the same period in 2010. The increase was driven by the growth of *Tysabri* revenue where total in-market sales were $738.4 million in the first half of 2011, an increase of 25% over the $589.4 million recorded in the same period of 2010, and resulted in recorded *Tysabri* revenue of $321.7 million (2010: $250.3 million). The growth in in-market sales reflects increased patient demand across global markets and a higher price in the United States, along with favourable foreign currency movements in the rest of world (ROW). At the end of June 2011, approximately 61,500 patients were on therapy worldwide, including approximately 28,500 commercial patients in the United States and approximately 32,300 commercial patients in ROW, representing an increase of 15% over the 53,300 patients (revised) who were on therapy at the end of June 2010.

For a reconciliation of operating profit/(loss) before other charges to operating profit/(loss), refer to page 8. We believe this reconciliation is meaningful because it provides additional information when analysing certain items. The principal items classified as other charges include transaction costs, severance, restructuring and other costs, facilities charges and net loss on divestment of business.

In July 2010, we announced that we reached an agreement in principle with the U.S. Attorney s Office for the District of Massachusetts with respect to the previously disclosed U.S. Department of Justice s investigation of sales and marketing practices for Zonegran®, which we divested in 2004. During the first half of 2010, we recorded a $206.3 million provision charge for the settlement, interest and related costs. The agreement was finalised in December 2010. Consistent with the terms of the agreement-in-principle announced in July 2010, we paid $203.5 million pursuant to the terms of a global settlement resolving all U.S. federal and related state Medicaid claims. The resolution of the Zonegran investigation could give rise to other investigations of litigation by state government entities or private parties.

Excluding other charges, the BioNeurology business recorded an operating profit for the first half of 2011 of $44.0 million compared to an operating profit, excluding the settlement provision and other charges, of $7.1 million recorded in the first half of 2010. This improvement reflects the 12% increase in revenue, improved operating margins and a 11% reduction in combined SG&A and R&D expenses (excluding other charges).

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The net income from discontinued operations of $103.1 million in the first half of 2011 as compared to $21.1 million in the first half of 2010 relates to the EDT business. The net income from discontinued operations in the first half of 2011 includes legal settlement gains of $84.5 million, which are further discussed on page 12. Including the net income from continuing and discontinued operations, total net income for the first half of 2011 was $50.1 million compared to a net loss of $219.8 million in the same period of 2010.

In the first half of 2011, BioNeurology Adjusted EBITDA increased to $73.2 million from $35.9 million for the same period in 2010. The increase principally reflects the increase in revenue, improved operating margins and the reduction in combined SG&A and R&D expenses (excluding other charges). For a reconciliation of net loss to Adjusted EBITDA, refer to page 13.

For additional discussion of the results of operations for the first half of 2011, refer to pages 6 to 12 of this half-year management report.

BioNeurology R&D Update

In June 2011, the EC approved the inclusion of anti-JCV antibody status as an additional factor to aid in stratifying patients at risk for developing PML in the Summary of Product Characteristics (SmPC) for *Tysabri* in the European Union. In addition, as part of a standard review process, the EC concluded the quality, safety and efficacy of *Tysabri* continue to be adequately demonstrated and renewed the EU five-year Marketing Authorisation.

The new SmPC language states that patients who are anti-JCV antibody positive are at an increased risk of developing PML compared to patients who are anti-JCV antibody negative. Recent studies suggest that irrespective of MS treatment, approximately 55% of MS patients are anti-JCV antibody positive. The SmPC language also states that patients who are anti-JCV antibody positive, have received prior immunosuppressant (IS) therapy, and received treatment with *Tysabri* for more than two years have the highest risk of developing PML.

This update to the SmPC was based on analysis of data from Biogen and Elan s quantitative risk stratification algorithm, which was presented at a number of recent major, international medical meetings. In the analysis, patients who were anti-JCV antibody negative were at a lower risk for developing PML. Patients who were anti-JCV antibody positive had varying degrees of risk for developing PML depending on prior IS use and *Tysabri* treatment duration.

In May 2011, we announced a strategic business relationship with Proteostasis to leverage Proteostasis platform for the discovery and development of disease-modifying, small molecule drugs and diagnostics for the treatment of neurodegenerative disorders such as Parkinson s, Huntington s, MS and amyotrophic lateral sclerosis (ALS), and a broad array of dementia-related diseases including Alzheimer s. This innovative initiative will bring together Proteostasis unique discovery technology, novel targets and compounds that modulate key Proteostasis Network pathways with our recent scientific advances in Parkinson s disease and long-standing strength in proprietary animal models, biology and medicinal chemistry as well as our current development expertise.

Under the terms of the agreement, we invested $20 million into the equity capital of Proteostasis and will have an opportunity to provide an additional $30 million in collaboration funding over five years. As part of the agreement, we became an approximate 24% shareholder in Proteostasis, obtained a right of first negotiation to exclusively license compounds emerging from the combined initiative, and have the right to a seat on the Proteostasis board of directors as well as its scientific advisory board. By mutual agreement, the relationship can be extended for a further five years. Elan s CEO, Kelly Martin, has joined the board of directors of Proteostasis and Elan s chief scientific officer, Dale Schenk, has joined its Scientific Advisory Board.

Neotope Biosciences Limited (Neotope Biosciences) is a wholly owned subsidiary of Elan that was created in 2010. Its focus is on creating novel monoclonal antibodies to neo-epitope amyloid related targets for the treatment of a broad range of therapeutic indications. These indications cover many different diseases from neurodegeneration to cancer to diabetes.

With progress being made in our lead programme against AL amyloidosis, we will begin the process of forming a separate and initially wholly owned subsidiary dedicated to advancing oncology related therapeutics. This business structure enables Neotope Biosciences and our Parkinson s Disease Genetics (PDG) group to continue to follow the science, reinforcing our focus, expertise and operating discipline in the broad field of neurology while simultaneously benefiting from possible therapeutic advancements in non-neurology fields.

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During the second quarter of 2011, we discontinued our ELND007 gamma secretase programme.

In July 2011, we presented data from the Phase 2 clinical trial of ELND005 (Scyllo-inositol) in mild to moderate Alzheimer s disease patients, at the Alzheimher s Association International Conference 2011.

Poster presentations on the safety and efficacy results of the Phase 2 randomised, placebo-controlled, dose-ranging study of ELND005 in mild to moderate Alzheimer s disease and on the population pharmacokinetic analysis of plasma, cerebrospinal fluid, and brain ELND005 in patients with mild to moderate Alzheimer s disease were presented. An oral presentation on imaging and cerebrospinal fluid biomarker results of a Phase 2 dose-ranging study of ELND005 in mild to moderate Alzheimer s disease was also presented.

Selected Financial Data

The selected financial data set forth below is derived from our unaudited condensed consolidated half-year financial statements (half-year financial statements) in this Half-Year Financial Report and our 2010 Annual Report, and should be read in conjunction with, and is qualified by reference to, our half-year financial statements and related notes thereto.

Six Months Ended 30 June,	2011	2010
Income Statement Data (in $m, except for per share and number of shares data):		
Continuing operations		
Total revenue	324.9	291.1
Settlement provision charge		206.3
Operating profit/(loss)	32.5	(203.1)
Net loss from continuing operations	(53.0)	(240.9)
Adjusted EBITDA continuing operations[1]	73.2	35.9
Discontinued operations		
Net income from discontinued operations	103.1	21.1
Adjusted EBITDA discontinued operations[1]	49.8	46.5
Net income/(loss)	50.1	(219.8)
Adjusted EBITDA[1]	123.0	82.4
Basic earnings/(loss) per Ordinary Share		
From continuing operations	(0.09)	(0.41)
From discontinued operations	0.18	0.04
Basic weighted-average shares outstanding (in millions) continuing and discontinued operations	586.4	584.6
Diluted earnings/(loss) per Ordinary Share		
From continuing operations	(0.09)	(0.41)
From discontinued operations	0.17	0.04
Diluted weighted-average shares outstanding (in millions) continuing operations	586.4	584.6
Diluted weighted-average shares outstanding (in millions) discontinued operations	591.4	587.3

	30 June 2011	31 December 2010
Balance Sheet Data (in $m):		
Cash and cash equivalents	491.9	422.5
Restricted cash and cash equivalents current and non-current	17.6	223.1
Available-for-sale investments current	1.2	2.0
Assets held for sale	349.4	
Total assets	1,881.3	1,999.1
Liabilities held for sale	23.4	
Long-term debt	1,251.8	1,249.1
Total shareholders equity	295.4	214.0

Refer to page 13 for a reconciliation of Adjusted EBITDA to net income/(loss) and our reasons for presenting this non-GAAP measure.

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Principal Risks and Uncertainties

Our operating performance in the second half of 2011 is subject to risks and uncertainties. These include, but are not limited to, the following principal items:

In respect of *Tysabri*, at the end of June 2011, approximately 61,500 patients were on therapy worldwide, including approximately 28,500 commercial patients in the United States and approximately 32,300 commercial patients in the ROW, representing an increase of 15% over the 53,300 patients (revised) who were on therapy at the end of June 2010. While we expect sales of *Tysabri* to continue to grow in the second half of 2011, the potential of *Tysabri* may be severely constrained by increases in the incidence of serious adverse events (including deaths) associated with *Tysabri* (in particular, if there are increases in the incidence rate for cases of PML, or by competition from existing or new therapies (in particular, oral therapies approved or filed for U.S. and European approvals);

In May 2011, we announced that we had entered into an agreement with Alkermes to sell our EDT business unit in a cash and stock transaction valued at approximately $960 million, as of the date of announcement. While we expect the transaction to close in the third quarter of 2011, there are conditions to closing that must be satisfied or waived before the deal can close. There can be no assurance that such conditions will be satisfied or waived and thus there can be no assurance that the transaction will be consummated in the third quarter of 2011 or at all; and

Johnson & Johnson is our largest shareholder with an 18.4% interest in our outstanding Ordinary Shares and is in control of our remaining interest in the Alzheimer s Immunotherapy Program (AIP). Johnson & Johnson s interest in Elan and the AIP may discourage others from seeking to work with or acquire us.

Additionally, the pharmaceutical industry is highly competitive and subject to significant and changing regulation by international, national, state and local government entities; thus we face a number of other risks and uncertainties, which are discussed in more detail in our 2010 Annual Report.

Results of Operations for the Six Months Ended 30 June 2011 and 2010

	2011 $m	2010 $m	% increase/ (decrease)
Continuing Operations			
Product revenue	324.9	290.1	12%
Contract revenue		1.0	(100%)
Total revenue	324.9	291.1	12%
Cost of sales	121.8	105.1	16%
Gross profit	203.1	186.0	9%
Selling, general and administrative expenses	73.0	79.4	(8%)
Research and development expenses	97.6	103.4	(6%)
Settlement provision charge		206.3	(100%)
Operating profit/(loss)	32.5	(203.1)	(116%)
Interest expense	59.5	60.7	(2%)
Interest income	(1.4)	(1.7)	(18%)
Investment gains	(2.3)	(13.9)	(83%)
Net loss on investments in associates	25.9		100%

Net interest and investment gains and losses	81.7	45.1	81%
Loss before tax	(49.2)	(248.2)	(80%)
Income tax expense/(benefit)	3.8	(7.3)	(152%)
Net loss from continuing operations	(53.0)	(240.9)	(78%)
Discontinued Operations			
Net income from discontinued operations	103.1	21.1	389%
Net income/(loss)	50.1	(219.8)	(123%)

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Results of Continuing and Discontinued Operations

The results of our continuing operations exclude the EDT business and relate to the operations of BioNeurology only. The EDT business is presented as a discontinued operation in the half-year income statement for the first half of 2011 and the comparative amounts have been restated to reflect this classification. A discussion of the results of the BioNeurology and EDT businesses in the first half of 2011 is set out below.

Operating Review of Continuing Operations   BioNeurology

Revenue

Total revenue from BioNeurology increased 12% to $324.9 million in the first half of 2011 from $291.1 million in the same period of 2010. The increase was driven by growth in *Tysabri* sales.

	Six Months Ended 30 June	
	2011 $m	2010 $m
Product revenue:		
Tysabri	321.7	250.3
Maxipime®	0.7	5.4
Azactam®	0.4	27.4
Prialt®		6.2
Royalties	2.1	0.8
Total product revenue	324.9	290.1
Contract revenue		1.0
Total revenue from BioNeurology	324.9	291.1

Tysabri

The *Tysabri* collaboration is a jointly controlled operation in accordance with International Accounting Standards (IAS) 31, *Financial Reporting of Interests in Joint Ventures* , (IAS 31). A jointly controlled operation is an operation of a joint venture (as defined by IAS 31) that involves the use of the assets and other resources of the venturers rather than establishing a corporation, partnership or other entity, or a financial structure that is separate from the venturers themselves. Each venturer uses its own property, plant and equipment and carries its own inventories. It also incurs its own expenses and liabilities and raises its own finance, which represent its own obligations.

The *Tysabri* collaboration operating profit or loss is calculated excluding R&D expenses (we record our share of the total *Tysabri* collaboration R&D expenses within our R&D expenses). In accordance with IAS 31, we recognise as revenue our share of the collaboration profit from the sale of *Tysabri*, plus our directly-incurred collaboration expenses on these sales. Our actual operating profit or loss on *Tysabri* differs from our share of the collaboration operating profit or loss because certain *Tysabri*-related expenses are not shared through the collaboration, and certain unique risks are retained by each party.

Global in-market net sales of *Tysabri* for MS, which we market in collaboration with Biogen Idec, were as follows:

	Six Months Ended 30 June	
	2011 $m	2010 $m
United States	353.0	280.1
ROW	385.4	309.3

Total *Tysabri* in-market net sales	738.4	589.4

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Tysabri in-market net sales increased 25% to $738.4 million in the first half of 2011 from $589.4 million in the same period of 2010. The increase reflects increased patient demand across global markets and a higher price in the United States, along with favourable foreign currency movements in ROW.

The *Tysabri* revenue of $321.7 million in the first half of 2011 (2010: $250.3 million) was calculated as follows:

	Six Months Ended 30 June	
	2011	**2010**
	$m	**$m**
Tysabri in-market sales	738.4	589.4
Operating expenses incurred by Elan and Biogen Idec (excluding R&D expenses)	(336.9)	(283.1)
Tysabri collaboration operating profit	401.5	306.3
Elan s 50% share of *Tysabri* collaboration operating profit	200.8	153.2
Elan s directly incurred costs	120.9	97.1
Net *Tysabri* revenue	321.7	250.3

Other BioNeurology Products

Elan ceased distributing Azactam as of 31 March 2010 and Maxipime as of 30 September 2010. Revenue for Maxipime and Azactam for the first half of 2011 was $0.7 million and $0.4 million, respectively, and relates to adjustments to discounts and allowances associated with sales prior to the cessation of distribution. Elan divested its Prialt assets and rights in May 2010 and revenue for the first half of 2010 was $6.2 million.

Other Charges Reconciliation

The following table shows a reconciliation of BioNeurology operating profit/(loss) before other charges to operating profit/(loss):

	Six Months Ended 30 June 2011			Six Months Ended 30 June 2010		
	Before Other Charges $m	**Other Charges $m**	**IFRS $m**	**Before Other Charges $m**	**Other Charges $m**	**IFRS $m**
Product revenue	324.9		324.9	290.1		290.1
Contract revenue				1.0		1.0
Total revenue	324.9		324.9	291.1		291.1
Cost of sales	122.1	(0.3)	121.8	104.8	0.3	105.1
Gross margin	202.8	0.3	203.1	186.3	(0.3)	186.0
Selling, general and administrative expenses	62.0	11.0	73.0	75.9	3.5	79.4
Research and development expenses	96.8	0.8	97.6	103.3	0.1	103.4
Settlement provision charge				206.3		206.3
Operating profit/(loss)	44.0	(11.5)	32.5	(199.2)	(3.9)	(203.1)

Cost of Sales

BioNeurology cost of sales decreased to $121.8 million in the first half of 2011 from $105.1 million in the first half of 2010. Included within cost of sales was an other charges credit of $0.3 million (2010: $0.3 million expense), as described in Note 5 to the half-year financial statements. Excluding other charges, the BioNeurology gross margin on revenue was 62% in 2011 and 64% in 2010.

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Included within total cost of sales is $115.2 million of directly incurred collaboration expenses related to *Tysabri* for 2011 (2010: $88.4 million), resulting in a reported *Tysabri* gross margin of 64% in 2011 (2010: 65%). The reported *Tysabri* gross margin is impacted by the collaboration profit-sharing, commercial spend and operational arrangements.

Selling, General and Administrative Expenses

BioNeurology selling, general and administrative (SG&A) expenses decreased to $73.0 million in the first half of 2011 from $79.4 million in the first half of 2010. Included within SG&A expenses were other charges of $11.0 million (2010: $3.5 million), as described in Note 5 to the half-year financial statements. Excluding other charges, SG&A expenses decreased 18% to $62.0 million in 2011 from $75.9 million in 2010. The decrease principally reflects lower support costs in the first half of 2011 as a result of the realignment and restructuring of the R&D organisation within BioNeurology in 2010, partially offset by increased commercial spending for *Tysabri*.

Research and Development Expenses

BioNeurology R&D expenses decreased to $97.6 million in the first half of 2011 from $103.4 million in the first half of 2010. Included within R&D expenses were other charges of $0.8 million (2010: $0.1 million), as described in Note 5 to the half-year financial statements. Excluding other charges, R&D expenses decreased 6% to $96.8 million in 2011, compared to $103.3 million in 2010. The decrease primarily relates to the realignment and restructuring of the R&D organisation within Elan s BioNeurology business in 2010, partially offset by increased investment in development activities related to *Tysabri*.

Settlement Provision Charge

In July 2010, we announced that we reached an agreement in principle with the U.S. Attorney s Office for the District of Massachusetts with respect to the previously disclosed U.S. Department of Justice s investigation of sales and marketing practices for Zonegran, which we divested in 2004. During the first half of 2010, we recorded a $206.3 million provision charge for the settlement, interest and related costs. The agreement was finalised in December 2010. Consistent with the terms of the agreement-in-principle announced in July 2010, we paid $203.5 million pursuant to the terms of a global settlement resolving all U.S. federal and related state Medicaid claims. The resolution of the Zonegran investigation could give rise to other investigations of litigation by state government entities or private parties.

Net Interest and Investment Gains and Losses

Net interest and investment gains and losses amounted to a net expense of $81.7 million for the first half of 2011, compared to a net expense of $45.1 million for the same period of 2010. The increase in net interest and investment gains and losses is primarily attributable to the net loss on investment in associates of $25.9 million (2010: $Nil) in the first half of 2011. For further discussion of investments in associates, refer to Note 8 to the half-year financial statements. In addition, we recorded net investment gains of $2.3 million in the first half of 2011 (2010: $13.9 million), relating to the disposal of non-current investments.

Taxation

The income tax expense was $3.8 million in the first half of 2011, compared to a $7.3 million benefit in the first half of 2010. The income tax expense for the first half of 2011 includes deferred expense of $2.1 million (2010: $8.1 million benefit) primarily related to the deferred tax asset (DTA) recognised in 2008, as the underlying loss carryforwards and other DTAs are utilised to shelter taxable income in the United States.

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Operating Review of Discontinued Operations EDT

	Six Months Ended 30 June	
	2011 $m	2010 $m
Product revenue	124.4	124.3
Contract revenue	4.4	8.1
Total revenue	128.8	132.4
Cost of sales	49.6	58.9
Gross margin	79.2	73.5
Operating expenses:		
Selling, general and administrative expenses	19.8	20.6
Research and development expenses	37.8	27.1
Gain on legal settlements	(84.5)	
Operating profit	106.1	25.8
Net interest expense	0.4	0.2
Net income before tax	105.7	25.6
Income tax expense	2.6	4.5
Net income from discontinued operations	103.1	21.1

Revenue

Revenue from the EDT business unit decreased to $128.8 million in 2011 from $132.4 million in the first half of 2010.

	Six Months Ended 30 June	
	2011 $m	2010 $m
Product revenue:		
Manufacturing revenue and royalties:		
TriCor® 145	24.0	25.0
Ampyra®	22.4	20.8
Focalin XR®/Ritalin LA®	18.2	16.6
Verelan®	13.2	11.9
Skelaxin®		5.2
Other	46.6	44.8
Total product revenue manufacturing revenue and royalties	124.4	124.3
Contract revenue:		
Research revenue	3.9	3.7
Milestone payments	0.5	4.4
Total contract revenue from EDT	4.4	8.1

Total revenue from EDT	128.8	132.4

Manufacturing revenue and royalties comprise revenue earned from products we manufacture for clients and royalties earned principally on sales by clients of products that incorporate our technologies. Except as noted above, no other product accounted for more than 10% of total manufacturing revenue and royalties in the first half of 2011 or the first half of 2010.

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Manufacturing revenue and royalties increased slightly to $124.4 million in the first half of 2011 from $124.3 in the first half of 2010.

The increase in manufacturing revenue and royalties in the first half of 2011, compared to the first half 2010, is primarily attributable to increased revenue from Ampyra, Rapamune®, Invega®Sustenna® and Focalin XR/Ritalin LA, partially offset by decreased revenue from *Naprelan®,* Diltiazem and Skelaxin.

The manufacturing and royalty revenue recorded for Ampyra in the first half of 2010 of $20.8 million principally reflected shipments to Acorda Therapeutics, Inc. (Acorda) of $18.9 million in the first quarter of 2010 to satisfy Acorda s initial stocking requirements for the launch of the product as well as build-up of safety stock supply. Elan records revenue upon shipment of Ampyra to Acorda, as this revenue is not contingent upon ultimate sale of the shipped product by Acorda or its customers. Consequently, revenue varies with shipments and is not based directly on in-market sales.

Potential generic competitors have challenged the existing patent protection for several of the products from which we earn manufacturing revenue and royalties. We and our clients defend the parties intellectual property rights vigorously. However, if these challenges are successful, EDT s manufacturing revenue and royalties will be materially and adversely affected. As a result of the approval and launch of a generic form of Skelaxin in April 2010, EDT s royalty revenue from this product has ended.

Contract Revenue

Contract revenue decreased to $4.4 million in the first half of 2011 from $8.1 million for the same period in 2010. The decrease in contract revenue in the first half of 2011 compared to the first half of 2010 was primarily due to the timing of recognition of milestones, partially offset by development fees from clients.

Other Charges Reconciliation

The following table shows a reconciliation of the EDT operating profit before other charges to operating profit:

	Six Months Ended 30 June 2011			Six Months Ended 30 June 2010		
	Before Other Charges $m	Other Charges $m	IFRS $m	Before Other Charges $m	Other Charges $m	IFRS $m
Product revenue	124.4		124.4	124.3		124.3
Contract revenue	4.4		4.4	8.1		8.1
Total revenue	128.8		128.8	132.4		132.4
Cost of sales	49.4	0.2	49.6	58.5	0.4	58.9
Gross margin	79.4	(0.2)	79.2	73.9	(0.4)	73.5
Selling, general and administrative expenses	18.1	1.7	19.8	20.6		20.6
Research and development expenses	24.6	13.2	37.8	27.1		27.1
Gain on legal settlements	(84.5)		(84.5)			
Operating profit	121.2	(15.1)	106.1	26.2	(0.4)	25.8

Cost of Sales

Total EDT cost of sales decreased to $49.6 million in the first half of 2011 from $58.9 million in the first half of 2010. Included within cost of sales were other charges of $0.2 million (2010: $0.4 million), as described in Note 10 to the half-year financial statements. Excluding other charges, the EDT gross margin on revenue was 62% in 2011 and 56% in 2010. The decrease in cost of sales in the first half of 2011 is primarily due to decreased amortisation expense on the *Verelan* intangible asset, which was fully amortised in December 2010.

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Selling, General and Administrative Expenses

Total EDT SG&A expenses were $19.8 million in the first half of 2011 from $20.6 million in the first half of 2010. Included within SG&A expenses were other charges of $1.7 million (2010: $Nil), as described in Note 10 to the half-year financial statements. Excluding other charges, SG&A expenses decreased 12% to $18.1 million in 2011 from $20.6 million in 2010. The decrease primarily relates to lower legal costs.

Research and Development Expenses

Total EDT R&D expenses were $37.8 million in the first half of 2011 from $27.1 million in the first half of 2010. Included within R&D expenses were other charges of $13.2 million (2010: $Nil), as described in Note 10 to the half-year financial statements. Excluding other charges, R&D expenses decreased 9% to $24.6 million in 2011, compared to $27.1 million in 2010. The decrease is primarily due to timing of R&D spending on proprietary projects.

Gain on Legal Settlements

In May 2011, we entered into an agreement with Alcon Laboratories, Inc. (Alcon) to settle litigation in relation to the application of its *NanoCrystal*® technology. As part of the settlement agreement with Alcon, we received $6.5 million in May 2011 in full and final settlement.

In June 2008, a jury ruled in the U.S. District Court for the District of Delaware that Abraxis (since acquired by Celgene Corporation) had infringed a patent owned by Elan in relation to the application of its *NanoCrystal* technology to Abraxane®. We were awarded $55 million, applying a royalty rate of 6% to sales of Abraxane from 1 January 2005 through 13 June 2008 (the date of the verdict). This award and damages associated with the continuing sales of the Abraxane product were subject to interest. In February 2011, we entered into an agreement with Abraxis to settle this litigation. As part of the settlement agreement with Abraxis, we received $78.0 million in full and final settlement of the litigation in March 2011. We will not receive future royalties in respect of Abraxane.

Net Interest

Net interest expense of $0.4 million (2010: $0.2 million) for the first half of 2011 is primarily related to foreign exchange losses.

Taxation

The income tax expense was $2.6 million in the first half of 2011, compared to a $4.5 million expense in the first half of 2010. The income tax expense in the first half of 2011 includes a deferred tax expense of $2.0 million (2010: $3.9 million) primarily related to the DTA recognised in 2008, as the underlying loss carryforwards and other DTAs are utilised to shelter taxable income in the United States.

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Reconciliation of Net Income/(Loss) to Adjusted EBITDA Non-GAAP Financial Information

	Continuing Operations Six Months Ended 30 June		Discontinued Operations Six Months Ended 30 June		Total Six Months Ended 30 June	
	2011 $m	2010 $m	2011 $m	2010 $m	2011 $m	2010 $m
Net income/(loss)	(53.0)	(240.9)	103.1	21.1	50.1	(219.8)
Adjustments:						
Interest expense	59.5	60.7	0.4	0.2	59.9	60.9
Interest income	(1.4)	(1.7)			(1.4)	(1.7)
Income tax expense/(benefit)	3.8	(7.3)	2.6	4.5	6.4	(2.8)
Depreciation and amortisation	15.3	15.9	8.6	16.3	23.9	32.2
Amortised fees	(0.3)	(0.2)	(0.2)	(0.2)	(0.5)	(0.4)
EBITDA	23.9	(173.5)	114.5	41.9	138.4	(131.6)
Share-based compensation expense[(1)]	14.2	13.1	4.7	4.2	18.9	17.3
Gain on legal settlement			(84.5)		(84.5)	
Settlement provision charge		206.3				206.3
Other charges	11.5	3.9	15.1	0.4	26.6	4.3
Net losses on investments in associates	25.9				25.9	
Net investment gains	(2.3)	(13.9)			(2.3)	(13.9)
Adjusted EBITDA	73.2	35.9	49.8	46.5	123.0	82.4

(1) *Share-based compensation expense excludes $0.6 million included in other charges in the first half of 2011 (2010: $0.2 million credit).*

Adjusted EBITDA is a non-GAAP measure of operating results. Elan s management uses this measure to evaluate our operating performance and it is among the factors considered as a basis for our planning and forecasting for future periods. We believe that Adjusted EBITDA is a measure of performance used by some investors, equity analysts and others to make informed investment decisions.

Adjusted EBITDA is defined as net income or loss plus or minus net interest expense, income tax expense, depreciation and amortisation of costs and revenue, share-based compensation, gain on legal settlements, settlement provision charge, other charges or gains, net losses on investments in associates and net investment gains and losses. Adjusted EBITDA is not presented as, and should not be considered an alternative measure of, operating results or cash flows from operations, as determined in accordance with International Financial Reporting Standards (IFRS). A reconciliation of Adjusted EBITDA to net income/(loss) is set out in the table above.

In the first half of 2011, we reported Adjusted EBITDA of $123.0 million, compared to Adjusted EBITDA of $82.4 million in the first half of 2010. The improvement reflects the 12% increase in revenue, improved operating margins and the 11% decrease in combined SG&A and R&D expenses (excluding other charges).

Liquid Resources and Shareholders Equity

Our liquid resources and shareholders equity were as follows:

	30 June 2011 $m	31 December 2010 $m	% increase /(decrease)
Cash and cash equivalents	491.9	422.5	16%
Restricted cash and cash equivalents current	2.6	208.2[(1)]	(99%)

Available-for-sale investments current	1.2	2.0	(40%)
Total liquid resources	495.7	632.7	(22%)
Shareholders equity	295.4	214.0	38%

(1) *Current restricted cash included $203.7 million held in an escrow account in relation to the Zonegran settlement, which was subsequently paid in March 2011.*

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We have historically financed our operating and capital resource requirements through cash flows from operations, sales of investment securities and borrowings. We consider all highly liquid deposits with a maturity on acquisition of three months or less to be cash equivalents. Our primary source of funds as at 30 June 2011 consisted of cash and cash equivalents of $491.9 million, which excludes current restricted cash of $2.6 million, and current investment securities of $1.2 million. Cash and cash equivalents primarily consist of bank deposits and holdings in U.S. Treasuries funds.

At 30 June 2011, our shareholders equity was $295.4 million, compared to $214.0 million at 31 December 2010. The increase is primarily due to the net income in the first half of 2011 of $50.1 million. The net income in the first half of 2011 includes legal settlement gains of $84.5 million.

Cash Flows Summary

Continuing and Discontinued Operations:

	Six Months Ended 30 June	
	2011 $m	2010 $m
Net cash provided by/(used in) operating activities	(100.5)	46.1
Net cash provided by investing activities	167.5	0.1
Net cash provided by financing activities	2.3	0.8
Effect of foreign exchange rate changes on cash	0.1	(0.3)
Net increase in cash and cash equivalents	69.4	46.7
Cash and cash equivalents at beginning of period	422.5	836.5
Cash and cash equivalents at end of period	491.9	883.2

Operating Activities

The components of net cash used in operating activities were as follows:

	Six Months Ended 30 June	
	2011 $m	2010 $m
Adjusted EBITDA	123.0	82.4
Net interest and tax	(58.1)	(56.8)
Gain on legal settlements	84.5	
Other charges	(20.9)	(3.7)
Working capital decrease/(increase)	(22.7)	24.2
Decrease in other liabilities relating to Zonegran settlement	(206.3)	
Net cash provided by/(used in) operating activities	(100.5)	46.1

Net cash used in operating activities was $100.5 million in the first half of 2011 (2010: $46.1 million).

The improvement in net cash inflow from Adjusted EBITDA from $82.4 million in 2010 to $123.0 million in the first half of 2011 is discussed on page 13.

Net interest and tax of $58.1 million in the first half of 2011, was primarily comprised of debt interest expense and was higher than the $56.8 million incurred in the first half of 2010, as further discussed on page 9 and page 12. The legal settlement gains of $84.5 million in the first half of 2011 is discussed in Note 10 to the half-year financial statements. The settlement provision charge of $206.3 million which was paid in the first half of 2011, is discussed in Note 6 to the half-year financial statements. The other net charges of $20.9 million in the

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first half of 2011 (adjusted to exclude net non-cash other charges of $5.7 million) was primarily comprised of severance, restructuring charges, and EDT Transaction costs. The other charges of $3.7 million in the first half of 2010 (adjusted to exclude non-cash other charges of $0.6 million) was also primarily comprised of severance and restructuring charges.

The working capital increase of $22.7 million in the first half of 2011 was primarily driven by the increase in trade receivables. This is mainly due to higher revenues from *Tysabri* in the first half of 2011 compared to the first half of 2010.

The working capital decrease of $24.2 million was primarily due to the reduction in revenues from Azactam and Skelaxin following the launch of generic competitors during the first half of 2010, offset by increased revenues from *Tysabri*.

Investing Activities

Net cash provided by investing activities was $167.5 million in the first half of 2011. The primary component of cash provided by investing activities is the decrease in restricted cash. The restricted cash and cash equivalents movement includes the $203.7 million that was held in escrow in relation to the Zonegran settlement. This settlement amount was paid in March 2011. The cash provided by investing activities was partially offset by the purchase of an equity method investment in Proteostasis in the first half of 2011 and the payment of $9.0 million to Transition Therapeutics, Inc. (Transition) in January 2011 in relation to the modification of our Collaboration Agreement with Transition in December 2010. In connection with this modification, Transition elected to exercise its opt-out right under the original agreement. Under this amendment, we agreed to pay Transition $9.0 million, which has been capitalised in acquired in process research and development (IPR&D).

Net cash provided by investing activities was $0.1 million in the first half of 2010. The primary components of cash provided by investing activities were capital expenditures of $23.8 million offset by investment and business disposal proceeds of $21.0 million.

Financing Activities

Net cash provided by financing activities totaled $2.3 million in the first half of 2011 (2010: $0.8 million), primarily reflecting the net proceeds from employee share issuances.

Discontinued Operations

The operating and investing net cash flows for the first half of 2011 and the first half of 2010 discussed above include the discontinued operations of the EDT business. There were no cash flows from financing activities attributable to EDT in the first half of 2011 or 2010. The net cash flows attributable to EDT are set out below:

	Six Months Ended 30 June	
	2011	2010
	$m	$m
Net operating cash inflows	133.4	56.9
Net investing cash outflows	(5.1)	(6.5)
Total net cash inflows	128.3	50.4

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Debt Facilities

At 30 June 2011, we had outstanding debt of $1,285.0 million in aggregate principal amount (excluding unamortised financing costs and original issue discount), which consisted of the following:

	Original Maturity	$m
8.875% Notes	December 2013	449.5
Floating Rate Notes due 2013	December 2013	10.5
8.75% Notes issued October 2009	October 2016	625.0
8.75% Notes issued August 2010	October 2016	200.0
Total		1,285.0

As at 30 June 2011, and as of the date of filing of this Half-Year Financial Report, we were not in violation of any of our debt covenants. For additional information regarding our outstanding debt, please refer to Note 15 to the half-year financial statements.

Related Party Transactions

We have related party relationships with our subsidiaries, associates, directors and executive officers. All transactions with subsidiaries eliminate on consolidation and are not presented in accordance with revised IAS 24, *Related Party Disclosures* (IAS 24).

There were no related party transactions that have taken place in the six months ended 30 June 2011 that materially affected the financial position or the performance of the Company during that period and there were no changes in the related party transactions described in the 2010 Annual Report that could have a material effect on the financial position or performance of the Company in the same period.

Directors

The names and functions of the directors are shown on pages 62 to 65 of our 2010 Annual Report. On 26 May 2011, Jonas Frick retired from the Board.

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UNAUDITED CONDENSED CONSOLIDATED HALF-YEAR INCOME STATEMENT

For the Six Months Ended 30 June

	Notes	2011 $m	2010 $m
Continuing operations			
Product revenue		324.9	290.1
Contract revenue			1.0
Total revenue	**3**	324.9	291.1
Cost of sales	**5**	121.8	105.1
Gross profit		203.1	186.0
Selling, general and administrative expenses	**5**	73.0	79.4
Research and development expenses	**5**	97.6	103.4
Settlement provision charge	**6**		206.3
Operating profit/(loss)		32.5	(203.1)
Interest expense	**7**	59.5	60.7
Interest income	**7**	(1.4)	(1.7)
Investment gains	**7**	(2.3)	(13.9)
Net loss on investments in associates	**8**	25.9	
Net interest and investment gains and losses		81.7	45.1
Net loss before tax		(49.2)	(248.2)
Income tax expense/(benefit)	**9**	3.8	(7.3)
Net loss from continuing operations		(53.0)	(240.9)
Discontinued operations			
Net income from discontinued operations (net of tax)	**10**	103.1	21.1
Net income/(loss)		50.1	(219.8)
Basic earnings/(loss) per Ordinary Share			
From continuing operations	**11**	$ (0.09)	$ (0.41)
From discontinued operations	**11**	$ 0.18	$ 0.04
Basic weighted-average shares outstanding (in millions) continuing and discontinued operations	**11**	586.4	584.6
Diluted earnings/(loss) per Ordinary Share			
From continuing operations	**11**	$ (0.09)	$ (0.41)
From discontinued operations	**11**	$ 0.17	$ 0.04
Diluted weighted-average shares outstanding (in millions) continuing operations	**11**	586.4	584.6
Diluted weighted-average shares outstanding (in millions) discontinued operations	**11**	591.4	587.3

The net income/(loss) for the six months ended 30 June 2011 and 30 June 2010 are wholly attributable to the owners of the Parent Company.

The accompanying notes are an integral part of these unaudited condensed consolidated half-year financial statements.

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UNAUDITED CONDENSED CONSOLIDATED HALF-YEAR

STATEMENT OF COMPREHENSIVE INCOME

For the Six Months Ended 30 June

	2011 $m	2010 $m
Net income/(loss) for the period	50.1	(219.8)
Other comprehensive income:		
Foreign currency translation		(0.2)
Available-for-sale investments	(0.1)	2.2
Net gain on available-for-sale investments transferred to the income statement		(4.8)
Other comprehensive loss for the period	(0.1)	(2.8)
Total comprehensive income/(loss) for the period	50.0	(222.6)

The total comprehensive income/(losses) for the six months ended 30 June 2011 and 30 June 2010 are wholly attributable to the owners of the Parent Company.

Total comprehensive income/(loss) arises from:		
Continuing operations	(53.1)	(243.7)
Discontinued operations	103.1	21.1
Total comprehensive income/(loss) for the period	50.0	(222.6)

The accompanying notes are an integral part of these unaudited condensed consolidated half-year financial statements.

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UNAUDITED CONDENSED CONSOLIDATED HALF-YEAR BALANCE SHEET

	Notes	30 June 2011 $m	31 December 2010[1] $m
Non-Current Assets			
Goodwill and other intangible assets	**13**	147.9	225.7
Property, plant and equipment		77.9	287.5
Investments in associates	**8**	203.1	209.0
Available-for-sale investments		9.8	8.9
Deferred tax asset	**9**	345.3	336.7
Restricted cash and cash equivalents		15.0	14.9
Other non-current assets		29.3	34.6
Total Non-Current Assets		828.3	1,117.3
Current Assets			
Inventory	**14**	20.1	39.0
Accounts receivable		171.4	191.6
Other current assets		13.5	15.4
Income tax prepayment		2.9	3.1
Available-for-sale investments		1.2	2.0
Restricted cash and cash equivalents		2.6	208.2
Cash and cash equivalents		491.9	422.5
Assets held for sale	**10**	349.4	
Total Current Assets		1,053.0	881.8
Total Assets		1,881.3	1,999.1
Non-Current Liabilities			
Long-term debt	**15**	1,251.8	1,249.1
Other liabilities	**16**	35.8	40.1
Income tax payable		14.4	14.2
Total Non-Current Liabilities		1,302.0	1,303.4
Current Liabilities			
Accounts payable		38.5	39.2
Accrued and other liabilities	**16**	220.3	235.5
Provisions	**17**	0.7	207.0
Income tax payable		1.0	
Liabilities held for sale	**10**	23.4	
Total Current Liabilities		283.9	481.7
Total Liabilities		1,585.9	1,785.1
Shareholders Equity			
Share capital		36.0	35.9
Share premium		7,089.5	7,087.3
Share-based compensation reserve		235.8	235.0
Foreign currency translation reserve		(11.2)	(11.2)

Available-for-sale investment reserve	0.8	0.9
Retained loss	(7,055.5)	(7,133.9)
Total Shareholders Equity	295.4	214.0
Total Shareholders Equity and Liabilities	1,881.3	1,999.1

(1) *Amounts as at 31 December 2010 are derived from the 31 December 2010 audited financial statements.*

The accompanying notes are an integral part of these unaudited condensed consolidated half-year financial statements.

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UNAUDITED CONDENSED CONSOLIDATED HALF-YEAR

STATEMENT OF CASH FLOWS

For the Six Months Ended 30 June

	2011 $m	2010 $m
Net income/(loss)	50.1	(219.8)
Adjustments to reconcile net income/(loss) to net cash provided by/(used in) operating activities:		
Depreciation and amortisation	23.9	32.2
Gain on sale of investments	(2.3)	(12.7)
Impairment of property, plant and equipment and intangible assets	5.1	
Settlement provision charge		206.3
Share-based compensation expense	19.5	17.1
Net loss on investments in associates	25.9	
Net loss on divestment of business		0.8
Debt interest expense	59.0	60.2
Interest income	(0.3)	(0.5)
Income tax expense	6.4	(2.8)
Other	(0.5)	(3.0)
	186.8	77.8
Decrease/(increase) in accounts receivable	(32.4)	15.3
Decrease/(increase) in prepayments and other assets	(1.5)	3.0
Decrease in inventory	0.8	17.2
Increase/(decrease) in accounts payable and accrued and other liabilities	8.8	(6.7)
Decrease in other liabilities relating to Zonegran settlement	(206.3)	
Cash provided by operations	(43.8)	106.6
Interest received	0.3	0.7
Interest paid	(56.2)	(59.7)
Income taxes paid	(0.8)	(1.5)
Net cash provided by/(used in) operating activities	(100.5)	46.1
Investing activities		
Decrease in restricted cash	205.5	3.2
Purchase of property, plant and equipment	(10.0)	(22.4)
Purchase of intangible and other assets	(10.1)	(1.4)
Purchase of available-for-sale investments	(0.5)	(0.3)
Proceeds from disposal of current available-for-sale investments		8.3
Proceeds from disposal of non-current available-for-sale investments	2.6	8.0
Purchase of investment in associate	(20.0)	
Proceeds from divestment of business		4.7
Net cash provided by investing activities	167.5	0.1
Financing activities		
Proceeds from issue of share capital	2.3	0.8
Net cash provided by financing activities	2.3	0.8
Effect of foreign exchange rate changes	0.1	(0.3)
Net increase in cash and cash equivalents	69.4	46.7

Cash and cash equivalents at the beginning of the period	422.5	836.5
Cash and cash equivalents at the end of the period	491.9	883.2

The accompanying notes are an integral part of these unaudited condensed consolidated half-year financial statements.

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UNAUDITED CONDENSED CONSOLIDATED HALF-YEAR STATEMENT

OF CHANGES IN SHAREHOLDERS EQUITY

	Number of Shares m	Share Capital $m	Share Premium $m	Share-Based Compensation Reserve $m	Foreign Currency Translation Reserve $m	Available-for-sale Investment Reserve $m	Retained Loss $m	Total Amount $m
Balances at 1 January 2010	583.9	35.8	7,085.6	237.2	(11.1)	5.1	(6,838.2)	514.4
Comprehensive income:								
Net loss							(219.8)	(219.8)
Other comprehensive income/(loss):								
Foreign currency translation					(0.2)			(0.2)
Available-for-sale investments						(2.6)		(2.6)
Total other comprehensive loss								(2.8)
Total comprehensive loss								(222.6)
Transactions with owners of the Company, recognised directly in equity:								
Issue of share capital, net of issue costs	0.9		0.8					0.8
Share-based compensation cost				17.1				17.1
Share-based compensation deferred tax				(7.1)				(7.1)
Transfer of exercised and expired share-based awards				(16.6)			16.6	
Balances at 30 June 2010	584.8	35.8	7,086.4	230.6	(11.3)	2.5	(7,041.4)	302.6
Comprehensive income:								
Net loss							(102.8)	(102.8)
Other comprehensive income/(loss):								
Foreign currency translation					0.1			0.1
Available-for-sale investments						(1.6)		(1.6)
Total other comprehensive loss								(1.5)
Total comprehensive loss								(104.3)
Transactions with owners of the Company, recognised directly in equity:								
Issue of share capital, net of issue costs	0.4	0.1	0.9					1.0
Share-based compensation cost				14.3				14.3
Share-based compensation deferred tax				0.4				0.4
Transfer of exercised and expired share-based awards				(10.3)			10.3	
Balances at 1 January 2011	585.2	35.9	7,087.3	235.0	(11.2)	0.9	(7,133.9)	214.0
Comprehensive income:								
Net income							50.1	50.1
Other comprehensive income/(loss):								
Available-for-sale investments						(0.1)		(0.1)
Total other comprehensive loss								(0.1)
Total comprehensive income								50.0

Transactions with owners of the Company, recognised directly in equity:								
Issue of share capital, net of issue costs	1.8	0.1	2.2					2.3
Share-based compensation cost				19.5				19.5
Share-based compensation deferred tax				9.6				9.6
Transfer of exercised and expired share-based awards				(28.3)			28.3	
Balance at 30 June 2011	587.0	36.0	7,089.5	235.8	(11.2)	0.8	(7,055.5)	295.4

The accompanying notes are an integral part of these unaudited condensed consolidated half-year financial statements.

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NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED

HALF-YEAR FINANCIAL STATEMENTS

1. BASIS OF PREPARATION

These unaudited half-year financial statements, which should be read in conjunction with our 2010 Annual Report, have been prepared by Elan Corporation, plc in accordance with IAS 34, *Interim Financial Reporting* (IAS 34), as adopted by the European Union. In addition, these half-year financial statements have been prepared in accordance with the Transparency (Directive 2004/109/EC) Regulations 2007 and the related Transparency Rules of the Republic of Ireland s Financial Regulator. They do not include all of the information required for full annual financial statements, and should be read in conjunction with our 2010 Annual Report.

These half-year financial statements are presented in U.S. dollars, which is the functional currency of the parent company and the majority of the group companies. They are prepared on the historical cost basis, except for certain financial assets and derivative financial instruments, which are stated at fair value.

The half-year financial statements include the accounts of Elan and all of our subsidiary undertakings. All significant intercompany account balances, transactions, and any unrealised gains and losses or income and expenses arising from intercompany transactions have been eliminated in preparing the half-year financial statements.

Following the approval of the EDT Transaction by the Board of Elan on 8 May 2011, the EDT business met the criteria to be classified as held for sale and the assets and liabilities of the EDT business have been classified as held for sale on the half-year balance sheet at 30 June 2011. The results of EDT are presented as a discontinued operation in the half-year income statement for the first half of 2011 and the comparative amounts have been restated to reflect this classification.

The preparation of half-year financial statements requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. Actual results could differ materially from these estimates. In preparing these half-year financial statements, the critical judgements made by management in applying the Company s accounting policies and the key sources of estimation uncertainty were the same as those that applied to the Consolidated Financial Statements as at and for the year ended 31 December 2010, and described on pages 114 to 119 of the 2010 Annual Report.

The comparative amounts included for the year ended 31 December 2010 do not constitute statutory financial statements of Elan within the meaning of Regulation 40 of the European Communities (Companies; Group accounts) Regulations, 1992. Statutory financial statements for the year ended 31 December 2010 have been filed with the Companies Office. The auditor s report on those financial statements was unqualified and did not contain an emphasis of matter paragraph.

Although profitable in the current half-year, we have incurred significant losses during the last number of fiscal years. However, our directors believe that we have adequate resources to continue in operational existence for the foreseeable future and that it is appropriate to continue to prepare our condensed consolidated half-year financial statements on a going concern basis.

These half-year financial statements were approved by the directors on 25 July 2011.

2. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies applied in these half-year financial statements are consistent with those applied in our Consolidated Financial Statements as at and for the year ended 31 December 2010, as set out on pages 106 to 114 of the 2010 Annual Report, except for the impact of the standards described below.

The following new interpretations and amendments to standards are mandatory for the first time for the financial year beginning 1 January 2011.

Revised IAS 24, *Related Party Disclosures* ;

IFRIC 19, *Extinguishing Financial Liabilities with Equity Instruments* ;

IFRIC 14 (Amendment), *Prepayments of a Minimum Funding Requirement ;*

Amendment to IAS 32, *Financial instruments: Presentation* , on classification of rights issues.

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The adoption of these amendments to standards and interpretations did not impact on our financial position or results from operations.

3. REVENUE

Revenue from continuing operations for the six months ended 30 June 2011 and 2010 is comprised of BioNeurology revenue only, as the results of the EDT business are presented as a discontinued operation in the half-year financial statements for the first half of 2011 and 2010.

Revenue from the BioNeurology business can be further analysed as follows:

	Six Months Ended 30 June	
	2011 $m	2010 $m
Product revenue:		
Tysabri	321.7	250.3
Maxipime	0.7	5.4
Azactam	0.4	27.4
Prialt		6.2
Royalties	2.1	0.8
Total product revenue	324.9	290.1
Contract Revenue		1.0
Total revenue from BioNeurology	324.9	291.1

The *Tysabri* collaboration is a jointly controlled operation in accordance with IAS 31. A jointly controlled operation is an operation of a joint venture (as defined by IAS 31) that involves the use of the assets and other resources of the venturers rather than establishing a corporation, partnership or other entity, or a financial structure that is separate from the venturers themselves. Each venturer uses its own property, plant and equipment and carries its own inventories. It also incurs its own expenses and liabilities and raises its own finance, which represent its own obligations.

The *Tysabri* collaboration operating profit or loss is calculated excluding R&D expenses (we record our share of the total *Tysabri* collaboration R&D expenses within our R&D expenses). In accordance with IAS 31, we recognise as revenue our share of the collaboration profit from the sale of *Tysabri* plus our directly incurred collaboration expenses on these sales, which are primarily comprised of royalties, that we incur and are payable by us to third parties and are reimbursed by the collaboration. Our actual operating profit on *Tysabri* differs from our share of the collaboration operating profit because certain *Tysabri*-related expenses are not shared through the collaboration, and certain unique risks are retained by each party.

Global in-market net sales of *Tysabri* were as follows:

	Six Months Ended 30 June	
	2011 $m	2010 $m
United States	353.0	280.1
ROW	385.4	309.3
Total *Tysabri* global in-market net sales	738.4	589.4

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For the first half of 2011, we recorded net *Tysabri* revenue of $321.7 million which was calculated as follows:

	Six Months Ended 30 June 2011		
	U.S. $m	ROW $m	Total $m
Tysabri in-market sales	353.0	385.4	738.4
Operating expenses incurred by Elan and Biogen Idec (excluding R&D expenses)	(160.5)	(176.4)	(336.9)
Tysabri collaboration operating profit	192.5	209.0	401.5
Elan s 50% share of *Tysabri* collaboration operating profit	96.3	104.5	200.8
Elan s directly incurred costs	63.9	57.0	120.9
Net *Tysabri* revenue	160.2	161.5	321.7

For the first half of 2010, we recorded net *Tysabri* revenue of $250.3 million which was calculated as follows:

	Six Months Ended 30 June 2010		
	U.S. $m	ROW $m	Total $m
Tysabri in-market sales	280.1	309.3	589.4
Operating expenses incurred by Elan and Biogen Idec (excluding R&D expenses)	(138.7)	(144.4)	(283.1)
Tysabri collaboration operating profit	141.4	164.9	306.3
Elan s 50% share of *Tysabri* collaboration operating profit	70.7	82.5	153.2
Elan s directly incurred costs	53.5	43.6	97.1
Net *Tysabri* revenue	124.2	126.1	250.3

Please refer to Note 10 for an analysis of revenue from the EDT business for the first half of 2011 and 2010.

4. SEGMENT INFORMATION

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision maker (CODM). Our CODM has been identified as Mr. G. Kelly Martin, chief executive officer. Our business is organised into two business units: BioNeurology and EDT, and our chief executive officer reviews the business from this perspective.

Following the approval of the EDT Transaction by the Board of Elan on 8 May 2011, the assets and liabilities of the EDT business are classified as held for sale on the Elan half-year balance sheet and the results of EDT are presented as a discontinued operation in the half-year income statement for the first half of 2011 and the comparative amounts have been restated to reflect this classification. The EDT Transaction is expected to close in the third quarter of 2011. Until the close of this transaction, our CODM will continue to review the performance of the business by evaluating the performance of the BioNeurology and EDT business units.

Segment performance is evaluated based on operating profit/(loss) and Adjusted EBITDA. Interest income, interest expense, investments and income tax expense are managed on a group basis. Therefore, these items are not allocated between operating segments for the purposes of the information presented to the CODM, and are accordingly omitted from the measure of segment profit or loss and Adjusted EBITDA.

BioNeurology engages in research, development and commercial activities primarily in Alzheimer s disease, Parkinson s disease and MS. EDT is an established, profitable, integrated drug delivery business unit of Elan, which has been applying its skills and knowledge in product development and drug delivery technologies to enhance the performance of dozens of drugs that have been marketed worldwide.

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The same accounting principles used for the group as a whole are applied to segment reporting. There has been no change in the basis of segmentation or in the basis of measurement of segment profit or loss in the period. Inter-segment pricing is determined on an arm s length basis.

	BioNeurology Six Months Ended 30 June		EDT Six Months Ended 30 June		Total Six Months Ended 30 June	
	2011 $m	2010 $m	2011 $m	2010 $m	2011 $m	2010 $m
Segment revenue						
Segment revenue	324.9	291.1	128.9	133.0	453.8	424.1
Less intersegment sales			(0.1)	(0.6)	(0.1)	(0.6)
Total revenue from external customers	324.9	291.1	128.8	132.4	453.7	423.5
Cost of sales	121.8	105.1	49.6	58.9	171.4	164.0
Gross margin	203.1	186.0	79.2	73.5	282.3	259.5
Operating expenses:						
Selling, general and administrative expenses	73.0	79.4	19.8	20.6	92.8	100.0
Research and development expenses	97.6	103.4	37.8	27.1	135.4	130.5
Gain on legal settlements			(84.5)		(84.5)	
Settlement provision charge		206.3				206.3
Total operating expenses	170.6	389.1	(26.9)	47.7	143.7	436.8
Segment operating profit/(loss)	32.5	(203.1)	106.1	25.8	138.6	(177.3)
Segment Adjusted EBITDA	73.2	35.9	49.8	46.5	123.0	82.4

Reconciliation of segment results to net income/(loss):

	BioNeurology Six Months Ended 30 June		EDT Six Months Ended 30 June		Total Six Months Ended 30 June	
	2011 $m	2010 $m	2011 $m	2010 $m	2011 $m	2010 $m
Segment Adjusted EBITDA	73.2	35.9	49.8	46.5	123.0	82.4
Depreciation and amortisation	(15.3)	(15.9)	(8.6)	(16.3)	(23.9)	(32.2)
Amortised fees	0.3	0.2	0.2	0.2	0.5	0.4
Share-based compensation expense[1]	(14.2)	(13.1)	(4.7)	(4.2)	(18.9)	(17.3)
Gain on legal settlements			84.5		84.5	
Settlement provision charge		(206.3)				(206.3)
Other charges	(11.5)	(3.9)	(15.1)	(0.4)	(26.6)	(4.3)
Segment operating profit/(loss)	32.5	(203.1)	106.1	25.8	138.6	(177.3)
Net interest and investment gains and losses					82.1	45.3
Income tax expense/(benefit)					6.4	(2.8)
Net income/(loss)					50.1	(219.8)

[(1)] *Share-based compensation expense excludes $0.6 million included in other charges in the first half of 2011 (2010: $0.2 million credit).*

The segment total assets for BioNeurology and EDT as at 31 December 2010 of $1,549.2 million and $449.9 million, respectively, did not materially change as at 30 June 2011, therefore this segmental disclosure has been omitted in accordance with IAS 34.

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5. OTHER CHARGES

The principal items classified as other charges include transaction costs, severance, restructuring and other costs, facilities charges and a net loss on divestment of business. We believe that disclosure of significant other charges is meaningful because it provides additional information when analysing certain items.

For the first half of 2011, included within cost of sales, SG&A expenses, and R&D expenses for our continuing operations were total other charges of $11.5 million (2010: $3.9 million) consisting of the following:

2011

	Cost of Sales $m	SG&A $m	R&D $m	Total $m
EDT Transaction costs		6.9		6.9
Severance, restructuring and other costs	(0.3)	1.4	0.8	1.9
Facilities charges		2.7		2.7
Total other charges from continuing operations	(0.3)	11.0	0.8	11.5

2010

	Cost of Sales $m	SG&A $m	R&D $m	Total $m
Severance, restructuring and other costs	0.3	2.7	0.1	3.1
Net loss on divestment of business		0.8		0.8
Total other charges from continuing operations	0.3	3.5	0.1	3.9

Transaction costs of $6.9 million were incurred during the first half of 2011 relating to the EDT Transaction.

During the first half of 2011 and 2010, we incurred severance and restructuring charges of $1.9 million and $3.1 million, respectively, principally associated with realignment and restructuring of the R&D organisation within the BioNeurology business and a reduction of related support services.

As a direct result of the realignment of the BioNeurology business, we incurred facilities charges of $2.7 million in the first half of 2011 relating to a consolidation of facilities in South San Francisco.

During the first half of 2010, we divested of our Prialt assets and rights to Azur Pharma International Limited (Azur), which resulted in a net loss of $0.8 million.

Please refer to Note 10 for an analysis of other charges from the EDT business for the six months ended 30 June 2011 and 30 June 2010.

6. SETTLEMENT PROVISION CHARGE

In July 2010, we announced that we reached an agreement in principle with the U.S. Attorney s Office for the District of Massachusetts with respect to the previously disclosed U.S. Department of Justice s investigation of sales and marketing practices for Zonegran, which we divested in 2004. During the first half of 2010, we recorded a $206.3 million provision charge for the settlement, interest and related costs. The agreement was finalised in December 2010. Consistent with the terms of the agreement-in-principle announced in July 2010, we paid $203.5 million pursuant to the terms of a global settlement resolving all U.S. federal and related state Medicaid claims. The resolution of the Zonegran

investigation could give rise to other investigations of litigation by state government entities or private parties.

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7. NET INTEREST AND INVESTMENT GAINS AND LOSSES

For the first half of 2011, net interest and investment gains and losses from continuing operations were $81.7 million (2010: $45.1 million), consisting of the following:

	Six Months Ended 30 June	
	2011 $m	2010 $m
Interest expense (including amortisation of deferred financing costs):		
Interest on 8.75% Notes issued October 2009	28.6	28.4
Interest on 8.875% Notes	20.6	21.3
Interest on 8.75% Notes issued August 2010	9.5	
Interest on Floating Rate Notes due 2011		7.0
Interest on Floating Rate Notes due 2013	0.3	3.5
Total debt interest expense	59.0	60.2
Other financial charges	0.5	0.5
Interest expense	59.5	60.7
Interest income:		
Interest income	(0.3)	(0.5)
Net foreign exchange gains	(0.9)	(1.2)
Other financial gains	(0.2)	
Interest income	(1.4)	(1.7)
Investment gains:		
Gain on auction rate securities recovery		(7.9)
Gains on disposal of investments	(2.3)	(4.8)
Derivative fair value gains		(1.2)
Investment gains	(2.3)	(13.9)
Net loss on investments in associates (refer to Note 8)	25.9	
Net interest and investment gains and losses	81.7	45.1

8. INVESTMENTS IN ASSOCIATES

	Janssen AI $m	Proteostasis $m	Total 30 June 2011 $m
1 January 2011	209.0		209.0
Addition		20.0	20.0
Net loss on investments in associates	(25.5)	(0.4)	(25.9)
At 30 June 2011	183.5	19.6	203.1

Janssen AI

In September 2009, Janssen AI, a newly formed subsidiary of Johnson & Johnson, acquired substantially all of the assets and rights related to our AIP collaboration with Wyeth (which has been acquired by Pfizer Inc. (Pfizer)). Johnson & Johnson also committed to fund up to $500.0 million towards the further development and commercialisation of the AIP to the extent the funding is required by the collaboration. Any required additional expenditures in respect of Janssen AI s obligations under the AIP collaboration in excess of $500.0 million will be funded by Elan and Johnson & Johnson in proportion to their respective shareholdings up to a maximum additional commitment of $400.0 million in total. Based on current spend levels, we anticipate that we may be

called upon to provide funding to Janssen AI commencing in 2012. In the event that further funding is required beyond the $400.0 million, such funding will be on terms determined by the board of Janssen AI, with Johnson & Johnson and Elan having a right of first offer to provide additional funding. In the event that either an AIP product reaches market and Janssen AI is in a positive operating cash flow position, or the AIP is terminated, before the $500.0 million has been drawn down, Johnson & Johnson is not required to contribute the full $500.0 million.

In consideration for the transfer of these assets and rights, we received a 49.9% equity interest in Janssen AI. In general, we are entitled to a 49.9% share of all net profits generated by Janssen AI beginning from the date Janssen AI becomes net profitable and certain royalty payments upon the commercialisation of products under the AIP collaboration. Johnson & Johnson has also committed to fund up to an initial $500.0 million towards the further development and commercialisation of the AIP to the extent the funding is required by the collaboration. Our equity interest in Janssen AI is recorded as an investment in associate on the half year balance sheet at 30 June 2011, at a carrying value of $183.5 million (31 December 2010: $209.0 million). The carrying value is comprised of our proportionate 49.9% share of Janssen s AIP assets (30 June 2011: $117.3 million; 31 December 2010: $117.3 million) and our proportionate 49.9% interest in the Johnson & Johnson contingent funding commitment (30 June 2011: $66.2 million; 31 December 2010: $91.7 million).

Our proportionate interest in the Johnson & Johnson contingent funding commitment was remeasured as of 30 June 2011 and 31 December 2010 to reflect changes in the probability that the cash will be spent and thereby give rise to the expected cash flows under the commitment, and to reflect the time value of money. As at 30 June 2011, the range of assumed probabilities applied to the expected cash flows was 95%-57% (31 December 2010: 95%-43%). The range of discount rates applied remained at 1%-1.5% (31 December 2010: 1%-1.5%), which was also the range used for initial recognition. The remeasurement of our proportionate interest in the Johnson & Johnson contingent funding commitment as at 30 June 2011 resulted in an increase in the carrying value of our investment in associate during the first half of 2011 of $25.2 million (2010: $41.4 million).

The following table sets forth the computation of the net loss on the investment in Janssen AI for the periods ended 30 June 2011 and 2010:

	Six Months Ended 30 June	
	2011 $m	**2010 $m**
Net loss reported by Janssen AI	101.7	82.9
Elan s 49.9% proportionate interest of Janssen AI s reported net loss	50.7	41.4
Remeasurement of Elan s 49.9% proportionate interest in Johnson & Johnson funding commitment	(25.2)	(41.4)
Net loss on investment in Janssen AI associate	25.5	

As at 30 June 2011, the remaining unspent amount of the initial Johnson & Johnson $500.0 million funding commitment was $173.9 million (31 December 2010: $272.0 million).

Proteostasis

On 20 May 2011, we entered into a strategic business relationship with Proteostasis to advance Proteostasis platform for the discovery and development of disease-modifying, small molecule drugs and diagnostics for the treatment of neurodegenerative disorders such as Parkinson s, Huntington s, MS, ALS, and a broad array of dementia-related diseases including Alzheimer s.

Under terms of the agreement, we invested $20.0 million into equity capital of Proteostasis and became a 24% shareholder. We will have the opportunity to invest an additional $30 million in collaboration funding over five years and obtained a right of first negotiation to exclusively license potential compounds. Elan CEO, Kelly Martin, has joined the Board of Directors of Proteostasis and Elan Chief Scientific Officer, Dale Schenk, has joined its Scientific Advisory Board.

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Our $20.0 million equity interest in Proteostasis has been recorded as an investment in an associate on the balance sheet. The net loss recorded on the equity method investment in the first half of 2011 was $0.4 million, representing our share of the net losses of Proteostasis from the date of acquisition of the equity interest on 20 May through 30 June 2011.

9. INCOME TAX

The total tax expense of $6.4 million (2010: $2.8 million benefit) arises from and is presented in the half-year income statement as follows:

	Six Months Ended 30 June	
	2011 $m	2010 $m
Continuing Operations		
Current tax expense	1.7	0.8
Deferred tax expense/(benefit) origination and reversal of timing differences	2.1	(8.1)
Income tax expense/(benefit) continuing operations	3.8	(7.3)
Discontinued Operations		
Current tax expense	0.6	0.6
Deferred tax expense	2.0	3.9
Income tax expense discontinued operations	2.6	4.5
Total Operations		
Current tax expense	2.3	1.4
Deferred tax expense/(benefit) origination and reversal of timing differences	4.1	(4.2)
Total income tax expense/(benefit)	6.4	(2.8)

The total income tax expense for continuing and discontinued operations of $6.4 million in the first half of 2011 (2010: $2.8 million benefit) reflects tax at standard rates in the jurisdictions in which we operate, the availability of tax losses and foreign withholding tax. The income tax benefit for the first half of 2010 reflects changes to U.S. net income, in addition to one-off tax benefits, recorded during the period.

The income tax expense in the first half of 2011 includes a deferred tax charge of $4.1 million (2010: $4.2 million benefit) primarily as a result of deferred tax expense related to the DTA previously recognised in 2008, as the underlying loss carryforwards and other DTAs are utilised to shelter taxable income in the United States.

	Balance 1 January 2011 $m	Recognised In Income $m	Recognised In Equity $m	Reclassified as held for sale liability $m	Balance 30 June 2011 $m
Deferred taxation liabilities	(4.4)			3.1	(1.3)
Deferred taxation assets	341.1	(4.1)	9.6		346.6
Net deferred taxation asset	336.7	(4.1)	9.6	3.1	345.3

10. DISCONTINUED OPERATIONS AND HELD FOR SALE ASSETS AND LIABILITIES

On 9 May 2011, Alkermes and Elan announced the execution of a definitive agreement under which Alkermes will merge with EDT in a cash and stock transaction valued at approximately $960 million as of the date of announcement. Alkermes and EDT will be combined under a new holding company incorporated in Ireland. This newly created company will be named Alkermes plc. The EDT Transaction is expected to close in the third quarter of 2011. When the deal closes, we will receive $500 million in cash and 31.9 million ordinary shares of Alkermes plc common stock. We will hold approximately 25% of the equity of Alkermes plc, with the existing shareholders of Alkermes, holding the remaining 75% of the equity. We will account for our investment in Alkermes plc as an associate investment.

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Non-current assets and liabilities are classified as assets and liabilities held for sale when their carrying amount is to be recovered principally through a sale transaction and a sale is considered highly probable. They are stated at the lower of carrying amount and fair value less costs to sell if their carrying amount is to be recovered principally through a sale transaction rather than through continuing use and a sale is considered highly probable. Intangible assets and property, plant and equipment classified as held for sale are not amortised or depreciated. The results of a component of an entity that either has been disposed of, or is classified as held for sale, and represents a separate major line of business or geographical area of operations and is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations are presented as a discontinued operation in the financial statements.

Following the approval of the EDT Transaction by the Board of Elan on 8 May 2011, the EDT business met the criteria to be classified as held for sale and the assets and liabilities of the EDT business have been classified as held for sale on the half-year balance sheet at 30 June 2011. The results of EDT are presented as a discontinued operation in the half-year income statement for the first half of 2011 and the comparative amounts have been restated to reflect this classification.

(a) Income statement

The income statement financial information relating to the EDT business for the first half of 2011 and 2010 is set out below.

	Six Months Ended 30 June	
	2011	**2010**
	$m	**$m**
Product revenue	124.4	124.3
Contract revenue	4.4	8.1
Total revenue	128.8	132.4
Cost of sales	49.6	58.9
Gross margin	79.2	73.5
Operating expenses:		
Selling, general and administrative expenses	19.8	20.6
Research and development expenses	37.8	27.1
Gain on legal settlements	(84.5)	
Operating profit	106.1	25.8
Net interest expense	0.4	0.2
Net income before tax of discontinued operation	105.7	25.6
Income tax expense	2.6	4.5
Net income of discontinued operation	103.1	21.1

(b) Cash flows

There were no cash flows from financing activities attributable to EDT in the first half of 2011 and 2010. The net cash flows attributable to the operating and investing activities of EDT for the first half of 2011 and 2010 are set out below:

	Six Months Ended 30 June	
	2011	**2010**
	$m	**$m**
Net operating cash inflows	133.4	56.9
Net investing cash outflows	(5.1)	(6.5)

Total net cash inflows	128.3	50.4

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(c) Revenue

Revenue from the EDT business for the first half of 2011 and 2010 is set out below:

	Six Months Ended 30 June	
	2011 $m	2010 $m
Product revenue:		
Manufacturing revenue and royalties:		
TriCor 145	24.0	25.0
Ampyra	22.4	20.8
Focalin XR/Ritalin LA	18.2	16.6
Verelan	13.2	11.9
Skelaxin		5.2
Other	46.6	44.8
Total product revenue manufacturing revenue and royalties	124.4	124.3
Contract revenue:		
Research revenue	3.9	3.7
Milestone payments	0.5	4.4
Total contract revenue	4.4	8.1
Total revenue from the EDT business	128.8	132.4

(d) Other charges

Other charges from the EDT business for the first half of 2011 and 2010 are set out below:

2011

	Cost of Sales $m	SG&A $m	R&D $m	Total $m
Severance, restructuring and other costs	0.2	1.7	8.1	10.0
Asset impairment charges			5.1	5.1
Total other charges from discontinued operations	0.2	1.7	13.2	15.1

2010

	Cost of Sales $m	SG&A $m	R&D $m	Total $m
Severance, restructuring and other costs	0.4			0.4
Total other charges from discontinued operations	0.4			0.4

During the second quarter of 2011, we decided to close our King of Prussia, Pennsylvania site and consequently, EDT recorded a non-cash asset impairment of $5.1 million and severance and restructuring charges of $10.0 million for the first half of 2011. It is expected that the closure will take place in the second half of 2011.

Other charges for the first half of 2010 of $0.4 million relate to severance, restructuring and other costs, arising from the realignment of resources to meet our business structure.

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(e) Legal settlement gains

In May 2011, we entered into an agreement with Alcon to settle litigation in relation to the application of our *NanoCrystal* technology. As part of the settlement agreement with Alcon, we received $6.5 million in May 2011 in full and final settlement.

In June 2008, a jury ruled in the U.S. District Court for the District of Delaware that Abraxis (since acquired by Celgene Corporation) had infringed a patent owned by Elan in relation to the application of its *NanoCrystal* technology to Abraxane. We were awarded $55 million, applying a royalty rate of 6% to sales of Abraxane from 1 January 2005 through 13 June 2008 (the date of the verdict). This award and damages associated with the continuing sales of the Abraxane product were subject to interest. In February 2011, we entered into an agreement with Abraxis to settle this litigation. As part of the settlement agreement with Abraxis, we received $78.0 million in full and final settlement of the litigation in March 2011. We will not receive future royalties in respect of Abraxane.

(f) Held for sale assets and liabilities

The assets and liabilities related to EDT business have been classified as held for sale following the Elan Board approval of the EDT Transaction. The EDT Transaction is expected to close in the third quarter of 2011. The carrying amounts of the EDT assets were less than the fair value less costs to sell when the assets were reclassified to held for sale and accordingly, no remeasurements of the assets were necessary.

The assets and liabilities of the EDT disposal group classified as held for sale are as follows:

	30 June 2011 $m
Assets held for sale	
Property, plant and equipment	200.4
Goodwill (note 13)	45.2
Other intangible assets (note 13)	23.4
Inventory	18.1
Other current and non current assets	62.3
Total assets held for sale	349.4
Liabilities held for sale	
Accounts payable	2.1
Deferred tax liability	3.1
Accrued and other liabilities	18.2
Total liabilities held for sale	23.4
Total net assets held for sale	326.0

11. NET EARNINGS/(LOSS) PER SHARE

Basic earnings/(loss) per share is computed by dividing the net income/(loss) for the period available to ordinary shareholders by the weighted average number of Ordinary Shares outstanding during the period. Diluted earnings/(loss) per share is computed by dividing the net income/(loss) for the period by the weighted average number of Ordinary Shares outstanding and, when dilutive, adjusted for the effect of all potentially dilutive shares, including share options and Restricted Stock Units (RSUs).

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The following table sets forth the computation for basic and diluted net loss per share:

	Six Months Ended 30 June	
	2011	2010
Numerator (amounts in $m):		
Basic and diluted net loss from continuing operations	$ (53.0)	$ (240.9)
Basic and diluted net income from discontinued operations	$ 103.1	$ 21.1
Basic earnings/(loss) per share		
Denominator (amounts in millions):		
Basic weighted-average shares outstanding (in millions) continuing and discontinued operations	586.4	584.6
Basic earnings/(loss) per share:		
From continuing operations	$ (0.09)	$ (0.41)
From discontinued operations	$ 0.18	$ 0.04
Diluted earnings/(loss) per share		
Denominator (amounts in millions):		
Diluted weighted-average shares outstanding (in millions) continuing operations	586.4	584.6
Diluted weighted-average shares outstanding (in millions) discontinued operations	591.4	587.3
Diluted earnings/(loss) per share:		
From continuing operations	$ (0.09)	$ (0.41)
From discontinued operations	$ 0.17	$ 0.04

For the first half of 2011 and 2010, there were no differences in the weighted-average number of Ordinary Shares used for basic and diluted net loss per Ordinary Share from continuing operations as the effect of all potentially dilutive Ordinary Shares outstanding was anti-dilutive. As at 30 June 2011, there were 26.2 million (2010: 24.0 million) share options and RSUs outstanding that could potentially have a dilutive impact in the future but were anti-dilutive in the first half 2011 and 2010.

12. SHARE-BASED COMPENSATION

We grant equity awards from the Long Term Incentive Plan (2006 LTIP), which provides for the issuance of share options, RSUs and other equity awards. The terms and conditions of the equity award plans and equity award activities are disclosed in our 2010 Annual Report.

Share Options

Share options are granted at fixed exercise prices equal to the market value of our shares on the date of grant. We granted approximately 3,224,000 share options on similar terms to employees of Elan and an affiliate during the first half of 2011 (2010: approximately 2,089,000 share options).

Equity-settled share-based payments made to employees have been recognised in the financial statements based on the fair value of the awards measured at the date of grant. Equity-settled share-based payments made to non-employees have been recognised in the financial statements based on the fair value of the awards measured when services are rendered. The fair value of share options is calculated using a binomial option-pricing model, and the fair value of options issued under our employee equity purchase plan, which is described further below, is calculated using the Black-Scholes option-pricing model, taking into consideration the relevant terms and conditions.

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The estimated weighted-average grant date fair values of share options awarded during the first half of 2011 and 2010 were $3.03 and $3.90 per share option, respectively. The fair values were estimated using the binomial option-pricing model with the following weighted-average assumptions:

	Six Months Ended 30 June	
	2011	2010
Share price and exercise price	$ 6.84	$ 7.05
Risk-free interest rate	1.7%	2.1%
Expected volatility[1]	49.8%	66.0%
Expected dividend yield		
Expected life[2]		

[1] *The expected volatility was based on the implied volatility of traded options on our shares.*

[2] *The expected lives of options granted in the first half of 2011, as derived from the output of the binomial model, ranged from 4.8 years to 7.5 years (2010: 4.8 years to 7.5 years). The contractual life of the options, which is not later than 10 years from the date of grant, is used as an input into the binomial model.*

Restricted Stock Units

As disclosed in our 2010 Annual Report, we grant RSUs to certain employees, directors and consultants of Elan and affiliates under our 2006 LTIP. The terms and conditions of the RSU awards are disclosed in our 2010 Annual Report. We granted approximately 3,301,000 RSUs on similar terms to certain directors and employees of Elan and an affiliate during the first half of 2011 (2010: approximately 2,957,000 RSUs). The fair value of services received in return for the RSUs is measured by reference to the fair value of the underlying shares at grant date, for directors and employees, and as services are rendered for non-employees. The estimated weighted-average grant date fair values of RSUs granted during the first half of 2011 and 2010 were $6.80 and $6.87 per unit, respectively.

Employee Equity Purchase Plan

As disclosed in our 2010 Annual Report, we operate an employee equity purchase plan for eligible employees in the United States. The estimated weighted-average grant date fair values of options issued under the U.S. plan during the first half of 2011 and 2010 was $1.67 and $2.17 per share, respectively. The estimated fair values were calculated using the following weighted-average inputs into the Black-Scholes option-pricing model:

	Six Months Ended 30 June	
	2011	2010
Share price	$ 5.73	$ 6.52
Exercise price	$ 4.87	$ 5.54
Risk-free interest rate	0.2%	0.2%
Expected volatility[1]	51.0%	66.0%
Expected dividend yield		
Expected life	6 months	6 months

[1] *The expected volatility was based on the implied volatility of traded options on our shares.*

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Share-based compensation expense

We recognised total compensation expense related to equity-settled share-based awards of $19.5 million during the first half of 2011 (2010: $17.1 million). The expenses have been recognised in the following line items in the condensed consolidated half-year income statement:

	Six Months Ended 30 June	
	2011	**2010**
	$m	**$m**
Cost of sales	0.1	0.1
Selling, general and administrative expenses[1]	7.5	6.9
Research and development expenses[2]	6.8	5.9
Share based compensation expense continuing operations	14.4	12.9
Share based compensation expense discontinued operations[3]	5.1	4.2
Total share based compensation expense	19.5	17.1

[1] *SG&A expenses in the first half of 2011 include $0.2 million (2010: $Nil) that has been recorded in other charges.*

[2] *R&D expenses include $0.2 million credit in the first half of 2010 that has been recorded in other charges.*

[3] *Share based compensation expense in the first half of 2011 for discontinued operations includes $0.4 million (2010:$Nil) that has been recorded in other charges.*

Share-based compensation arose under the following share-based awards:

	Six Months Ended 30 June	
	2011	**2010**
	$m	**$m**
Share options	12.4	7.2
RSUs	6.8	9.4
Employee equity purchase plan	0.3	0.5
Total	19.5	17.1

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13. GOODWILL AND OTHER INTANGIBLE ASSETS

	Patents, Licences & Other $m	Acquired IPR&D $m	Goodwill $m	Total $m
Cost:				
At 1 January 2011	391.9	98.0	45.2	535.1
Additions	1.2			1.2
Transfer to assets held for sale	(152.4)	(41.6)	(45.2)	(239.2)
Disposals	(0.8)			(0.8)
At 30 June 2011	239.9	56.4		296.3
Accumulated amortisation:				
At 1 January 2011	(272.5)	(36.9)		(309.4)
Amortised in year	(8.5)	(1.6)		(10.1)
Impairment	(0.1)			(0.1)
Transfer to assets held for sale	149.1	21.5		170.6
Disposals	0.6			0.6
At 30 June 2011	(131.4)	(17.0)		(148.4)
Net book value:				
30 June 2011	108.5	39.4		147.9
31 December 2010	119.4	61.1	45.2	225.7

The components of the carrying value of patents, licences and acquired IPR&D, which have remaining useful lives between 1 and 10 years, were as follows:

	30 June 2011 $m	31 December 2010 $m
Tysabri	118.6	125.9
Other intangible assets	29.3	54.6
Total patents, licences and acquired IPR&D	147.9	180.5

The amortisation charge for total intangible assets is recognised in the following line items of the half-year income statement:

	Six Months Ended 30 June	
	2011 $m	2010 $m
Cost of sales	5.6	5.5
Selling, general and administrative expenses	1.3	1.2
Research and development expenses	2.0	2.4

Amortisation charge continuing operations	8.9	9.1
Amortisation charge discontinued operations	1.2	5.9
Total amortisation charge for intangible assets	10.1	15.0

14. INVENTORY

Our product inventory consisted of the following:

	30 June 2011 $m	31 December 2010 $m
Raw materials		10.0
Work-in-process		6.0
Finished goods	20.1	23.0
Total inventory	20.1	39.0

Inventory with a carrying value of $18.1 million is included in the assets held for sale at 30 June 2011 (raw materials of $9.9 million, work-in-process of $5.5 million and finished goods of $2.7 million). Please refer to Note 10 for an analysis of the assets and liabilities held for sale at 30 June 2011.

15. LONG-TERM DEBT

	Original Maturity	30 June 2011 $m	31 December 2010 $m
8.875% Notes	December 2013	445.8	445.1
Floating Rate Notes due 2013	December 2013	10.4	10.4
8.75% Notes issued October 2009	October 2016	607.2	605.9
8.75% Notes issued August 2010	October 2016	188.4	187.7
Total long-term debt		1,251.8	1,249.1

8.875% Notes

The outstanding principal amount of the 8.875% senior fixed rate notes due 1 December 2013 (8.875% Notes) was $449.5 million at 30 June 2011 (31 December 2010: $449.5 million), and has been recorded net of unamortised financing costs of $3.7 million (31 December 2010: $4.4 million).

Floating Rate Notes due 2013

The outstanding principal amount of the senior floating rate notes due 1 December 2013 (Floating Rate Notes due 2013) was $10.5 million at 30 June 2011 (31 December 2010: $10.5 million), and has been recorded net of unamortised financing costs of $0.1 million (31 December 2010: $0.1 million). These notes bear interest at a rate, adjusted quarterly, equal to three-months London Interbank Offer Rate (LIBOR) plus 4.125%.

8.75% Notes issued October 2009

The outstanding principal amount of the 8.75% senior fixed rate notes due 15 October 2016 that were issued in October 2009 (8.75% Notes issued October 2009) was $625.0 million at 30 June 2011 (31 December 2010: $625.0 million), and has been recorded net of unamortised financing costs of $17.8 million (31 December 2010: $19.1 million).

8.75% Notes issued August 2010

The outstanding principal amount of the 8.75% senior fixed rate notes due 15 October 2016 that were issued in August 2010 (8.75% Notes issued August 2010) was $200.0 million at 30 June 2011 (31 December 2010: $200.0 million), and has been recorded net of unamortised

financing costs of $11.6 million (31 December 2010: $12.3 million).

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16. ACCRUED AND OTHER LIABILITIES

Our accrued and other liabilities consisted of the following:

	30 June 2011 $m	31 December 2010 $m
Non-current liabilities:		
Deferred rent	17.9	18.8
Other liabilities	17.9	21.3
Non-current liabilities	35.8	40.1

	30 June 2011 $m	31 December 2010 $m
Current liabilities:		
Accrued royalties payable	74.1	63.3
Accrued rebates	28.6	22.6
Payroll and related taxes	24.7	40.9
Sales and marketing accruals	21.5	22.0
Accrued interest	18.3	18.3
Restructuring accrual	14.7	12.9
Clinical trial accruals	12.6	13.8
Deferred rent	2.6	3.5
Transition payment		9.0
Other accruals	23.2	29.2
Current liabilities	220.3	235.5

Current liabilities of $17.3 million and non-current liabilities of $0.9 million are included in liabilities held for sale at 30 June 2011. Please refer to Note 10 for an analysis of the assets and liabilities held for sale at 30 June 2011.

17. PROVISIONS

At 30 June 2011, we had a provisions balance of $0.7 million (31 December 2010: $207.0 million). At 31 December 2010, the provision included a $206.3 million settlement provision relating to the Zonegran settlement, interest and related costs. For further information, please refer to Notes 6 and 19.

18. FINANCIAL RISK MANAGEMENT

Financial risk factors

We are exposed to various financial risks arising in the normal course of business. Our financial risk exposures are predominantly related to changes in foreign currency exchange rates and interest rates, as well as the creditworthiness of our counterparties.

The half-year financial statements do not include all financial risk management information and disclosures required in the annual financial statements, and should be read in conjunction with the 2010 Annual Report.

There have been no changes in our risk management policies since year-end.

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Liquidity risk

Compared to year-end, there was no material change in the contractual undiscounted cash outflows for financial liabilities.

Our liquid resources and shareholders equity were as follows:

	30 June 2011 $m	31 December 2010 $m
Cash and cash equivalents	491.9	422.5
Restricted cash and cash equivalents current	2.6	208.2[1]
Available-for-sale investments current	1.2	2.0
Total liquid resources	495.7	632.7
Shareholders equity	295.4	214.0

(1) *Current restricted cash included $203.7 million held in an escrow account in relation to the Zonegran settlement, which was subsequently paid in March 2011.*

Fair value estimation

There were no significant changes in the business or economic circumstances during the first half of 2011 that affect the fair value of our financial assets and financial liabilities.

During the first half of 2011, there were no reclassifications of financial assets and no significant transfers between levels of the fair value hierarchy used in measuring the fair value of financial instruments.

19. LITIGATION

We are involved in legal and administrative proceedings, including proceedings with respect to *Tysabri* related product liability claims, that could have a material adverse effect on us.

Zonegran matter

In January 2006, we received a subpoena from the U.S. Department of Justice and the Department of Health and Human Services, Office of Inspector General, asking for documents and materials primarily related to our marketing practices for Zonegran, an antiepileptic prescription medicine that we divested to Eisai Inc. in April 2004.

In December 2010, we finalised our agreement with the U.S. Attorney s Office for the District of Massachusetts to resolve all aspects of the U.S. Department of Justice s investigation of sales and marketing practices for Zonegran. In addition, we pleaded guilty to a misdemeanour violation of the U.S. Food Drug & Cosmetic Act and entered into a Corporate Integrity Agreement with the Office of Inspector General of the Department of Health and Human Services to promote our compliance with the requirements of U.S. federal healthcare programmes and the FDA. If we materially fail to comply with the requirements of U.S. federal healthcare programmes or the FDA, or otherwise materially breach the terms of the Corporate Integrity Agreement, such as by a material breach of the compliance programme or reporting obligations of the Corporate Integrity Agreement, severe sanctions could be imposed upon us.

We paid $203.5 million pursuant to the terms of a global settlement resolving all U.S. federal and related state Medicaid claims in March 2011. This resolution of the Zonegran investigation could give rise to other investigations or litigation by state government entities or private parties.

Patent matters

In May 2011, we entered into an agreement with Alcon to settle litigation in relation to the application of our *NanoCrystal* technology. As part of the settlement agreement with Alcon, we received $6.5 million in May 2011 in full and final settlement.

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In June 2008, a jury ruled in the U.S. District Court for the District of Delaware that Abraxis, since acquired by Celgene Corporation, had infringed a patent owned by Elan in relation to the application of its *NanoCrystal* technology to Abraxane. We were awarded $55 million, applying a royalty rate of 6% to sales of Abraxane from 1 January 2005 through 13 June 2008 (the date of the verdict). This award and damages associated with the continuing sales of the Abraxane product were subject to interest. In February 2011, we entered into an agreement with Abraxis to settle this litigation. As part of the settlement agreement with Abraxis, we received $78.0 million in March 2011 in full and final settlement. We will not receive future royalties in respect of Abraxane.

Securities matters

In March 2005, we received a letter from the U.S. Securities and Exchange Commission (SEC) stating that the SEC s Division of Enforcement was conducting an informal inquiry into actions and securities trading relating to *Tysabri* events. The SEC s inquiry primarily relates to events surrounding the 28 February 2005 announcement of the decision to voluntarily suspend the marketing and clinical dosing of *Tysabri*. We have provided materials to the SEC in connection with the inquiry but have not received any additional requests for information or interviews relating to the inquiry.

The SEC notified us in January 2009 that the SEC was conducting an informal inquiry primarily relating to the 31 July 2008 announcement concerning the initial two *Tysabri*-related PML cases that occurred subsequent to the resumption of marketing *Tysabri* in 2006. We have provided the SEC with materials in connection with the inquiry.

On 24 September 2009, we received a subpoena from the SEC s New York Regional Office requesting records relating to an investigation captioned In the Matter of Elan Corporation, plc. The subpoena requests records and information relating to the 31 July 2008 announcement of the two *Tysabri*-related PML cases as well as records and information relating to the 29 July 2008 announcement at the International Conference of Alzheimer s Disease concerning the Phase 2 trial data for bapineuzumab. We have provided the SEC with materials in connection with the investigation.

We and some of our officers and directors have been named as defendants in five putative class action lawsuits filed in the U.S. District Court for the Southern District of New York in 2008. The cases have been consolidated as In Re: Elan Corporation Securities Litigation. The plaintiffs Consolidated Amended Complaint was filed on 17 August 2009, and alleges claims under the U.S. federal securities laws and seeks damages on behalf of all purchasers of our stock during periods ranging between 21 May 2007 and 21 October 2008. The complaints allege that we issued false and misleading public statements concerning the safety and efficacy of bapineuzumab. On 23 July 2010, a securities case was filed in the U.S. District Court for the Southern District of New York. This case has been accepted by the court as a related case to the existing 2008 matter. The 2010 case purports to be filed on behalf of all purchasers of Elan call options during the period from 17 June 2008 to 29 July 2008. We filed a Motion to Dismiss the Consolidated Amended Complaint. On 24 June 2011, the court rejected the plaintiffs claims during oral argument, and issued a Summary Order granting our Motion to Dismiss the class action complaints. The court provided the plaintiffs with the opportunity to file a single, coordinated brief by 29 July 2011 setting forth grounds for allowing them to amend their complaints. If the court believes that the plaintiffs brief has merit the court will notify Elan in order to provide Elan an opportunity to file an opposition brief prior to the court ruling whether an amended complaint can be filed.

We and some of our officers and directors have been named as defendants in a securities case filed on 24 June 2010 in the U.S. District Court in the Northern District of California. The complaint alleges that during the June/July 2008 timeframe we disseminated materially false and misleading statements/omissions related to *Tysabri* and bapineuzumab. Plaintiffs allege that they lost collectively approximately $4.5 million. Our Motion to Dismiss this case was granted on 9 February 2011; however, plaintiffs were given leave to amend and filed an amended complaint on 11 March 2011 and we filed a Motion to Dismiss the amended complaint on 13 May 2011. We expect a hearing on our renewed Motion to Dismiss in the second half of 2011.

We and some of our officers have been named as defendants in a putative class action lawsuit filed in the U.S. District Court for the Southern District of New York on 23 February 2011. The plaintiffs complaint alleges claims under U.S. federal securities laws and seeks damages on behalf of all purchasers of our stock during the

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period between 2 July 2009 and 5 August 2009. The original complaint filed on 27 April 2011 alleges that we issued false and misleading public statements concerning our September 2009 transaction with Johnson & Johnson. In response to the complaint, on 6 June 2011, we filed a Motion to Dismiss and an accompanying brief. Rather than respond to our filing, plaintiffs filed an amended complaint on 27 June 2011 and we filed a subsequent Motion to Dismiss and accompanying brief on 14 July 2011. Assuming the court schedules an oral hearing regarding our filing to dismiss the action, we expect that such a hearing would occur in the second half of 2011.

Antitrust matters

In 2002 and 2003, 10 actions were filed in the U.S. District Courts (seven in the District of Columbia and three in the Southern District of New York) claiming that we (and others) violated federal and state antitrust laws based on licensing and manufacturing arrangements between Elan, Teva Pharmaceuticals Inc. and Biovail Corporation relating to nifedipine. The complaints sought various forms of remedy, including damages and injunctive relief. The actions were brought by putative classes of direct purchasers, individual direct purchasers, and putative classes of indirect purchasers. On 29 May 2003, the Judicial Panel for Multidistrict Litigation coordinated and consolidated for pre-trial proceedings all pending cases in the U.S. District Court for the District of Columbia. In late 2007, we entered into a settlement agreement with the indirect purchaser class resulting in a dismissal of that segment of the lawsuit. In December 2009, we entered into a separate settlement agreement with the individual opt-out direct purchasers and agreed to pay $4.6 million to this opt-out direct purchaser class resulting in a dismissal of the second segment of the litigation. In October 2010, we agreed to pay $12.5 million to settle the third and final piece of this litigation. On 31 January 2011, the U.S. District Court for the District of Columbia approved the settlement and dismissed the case.

Paragraph IV litigation

We and/or our product licensees are involved in various sets of so-called Paragraph IV litigation proceedings in the United States. In the United States, putative generics of innovator drug products (including products in which the innovation comprises a new drug delivery method for an existing product, such as the drug delivery market occupied by us) may file Abbreviated New Drug Applications (ANDAs) and, in doing so, they are not required to include preclinical and clinical data to establish safety and effectiveness of their drug. Instead, they would rely on such data provided by the innovator drug New Drug Application (NDA) holder. However, to benefit from this less costly abbreviated procedure, the ANDA applicant must demonstrate that its drug is generic or bioequivalent to the innovator drug, and, to the extent that patents protect the innovator drug that are listed in the Orange Book , the ANDA applicant must write to the innovator NDA holder and the patent holder (to the extent that the Orange Book-listed patents are not owned by the innovator NDA holder) certifying that their product either does not infringe the innovator s patents and/or that the relevant patents are invalid. The innovator and the patent holder may sue the ANDA applicant within 45 days of receiving the certification and, if so, the FDA may not approve the ANDA for 30 months from the date of certification unless, at some point before the expiry of those 30 months, a court makes a final decision in the ANDA applicant s favour.

We are involved in a number of Paragraph IV suits in respect of seven different products (Tricor, Focalin XR, Avinza®, Zanaflex®, Rapamune, Luvox CR® and Megace® ES) either as plaintiff or as an interested party (where the suit is being taken in the name of one of our licensees). If we are unsuccessful in these and other similar type suits, our or our licensees products may be subject to generic competition, and our manufacturing revenue and royalties would be materially and adversely affected.

20. RELATED PARTIES

We have related party relationships with our subsidiaries, associates, directors and executive officers. All transactions with subsidiaries eliminate on consolidation and are not presented in accordance with revised IAS 24.

There were no related party transactions that have taken place in the six months ended 30 June 2011 that materially affected the financial position or the performance of the Company during that period and there were no changes in the related party transactions described in the 2010 Annual Report that could have a material effect on the financial position or performance of the Company in the same period.

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U.S. GAAP INFORMATION

The half-year financial statements of the Company have been prepared in accordance with IFRS, which differs in certain significant respects from accounting principles generally accepted in the United States (U.S. GAAP).

In June 2011, the Staff of the U.S. Securities and Exchange Commission s Division of Corporation Finance informed the Company that it had completed its review of Elan s 2009 Annual Report on Form 20-F. Following comments received from the Staff during this review, we revised our application of equity method accounting to our investment in Janssen AI under U.S. GAAP. Please refer to page 47 for a discussion of the revised accounting model under U.S. GAAP and how this model differs from IFRS. The change in accounting model under U.S. GAAP does not affect the economic rights or obligations under, or any other terms of, the September 2009 transaction with Johnson & Johnson, nor does it result in any adjustment to our historical revenue, Adjusted EBITDA or cash and cash equivalents.

Reconciliation from IFRS to U.S. GAAP

Unaudited Condensed Consolidated Half-Year Income Statement

For the Six Months Ended 30 June 2011

	IFRS $m	(A) Tysabri $m	(B) Other Intangible Assets $m	(C) Taxation $m	(D) Other Net Charges $m	(E) Discontinued Operations $m	(F) Investment in Associate $m	(G) & (H) Pensions & Other $m	U.S. GAAP $m
Continuing operations									
Revenue	324.9	192.8				128.8			646.5
Cost of sales	121.8	154.3			0.1	49.6			325.8
Gross profit	203.1	38.5			(0.1)	79.2			320.7
Selling, general and administrative expenses	73.0	38.5	(1.6)		(12.7)	19.8			117.0
Research and development expenses	97.6				(14.0)	37.8			121.4
Other net gains					26.6	(84.5)			(57.9)
Total operating expenses	170.6	38.5	(1.6)		(0.1)	(26.9)			180.5
Operating profit	32.5		1.6			106.1			140.2
Net interest and investment gains and losses	81.7					0.4	25.7	2.3	110.1
Net income/(loss) before tax	(49.2)		1.6			105.7	(25.7)	(2.3)	30.1
Income tax expense	3.8			2.6		2.6			9.0
Net income/(loss) from continuing operations	(53.0)		1.6	(2.6)		103.1	(25.7)	(2.3)	21.1
Discontinued operations									
Net income from discontinued operations	103.1					(103.1)			
Net income	50.1		1.6	(2.6)			(25.7)	(2.3)	21.1

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Unaudited Condensed Consolidated Half-Year Income Statement

For the Six Months Ended 30 June 2010

	IFRS $m	(A) Tysabri $m	(B) Goodwill $m	(B) Other Intangible Assets $m	(D) Other Net Charges $m	(E) Discontinued Operations $m	(G) & (H) Other $m	U.S. GAAP $m
Continuing operations								
Revenue	291.1	155.9				132.4		579.4
Cost of sales	105.1	122.6		1.2	(0.7)	58.9		287.1
Gross profit	186.0	33.3		(1.2)	0.7	73.5		292.3
Selling, general and administrative expenses	79.4	33.3		(1.9)	(3.5)	20.6	(0.1)	127.8
Research and development expenses	103.4				(0.1)	27.1	(0.1)	130.3
Settlement provision charge	206.3							206.3
Other net charges			0.6	0.2	4.3			5.1
Total operating expenses	389.1	33.3	0.6	(1.7)	0.7	47.7	(0.2)	469.5
Operating loss	(203.1)		(0.6)	0.5		25.8	0.2	(177.2)
Net interest and investment gains and losses	45.1					0.2	(4.6)	40.7
Net loss before tax	(248.2)		(0.6)	0.5		25.6	4.8	(217.9)
Income tax benefit	(7.3)					4.5		(2.8)
Net loss from continuing operations	(240.9)		(0.6)	0.5		21.1	4.8	(215.1)
Discontinued operations								
Net income from discontinued operations	21.1					(21.1)		
Net loss	(219.8)		(0.6)	0.5			4.8	(215.1)

Unaudited Condensed Consolidated Half-Year Balance Sheet

At 30 June 2011

	IFRS $m	(B) Goodwill $m	(B) Other Intangible Assets $m	(C) Taxation $m	(G) Pension $m	(E) Investment in Associate $m	(H) Other $m	U.S. GAAP $m
Non-Current Assets								
Goodwill and other intangible assets	147.9	207.4	(39.4)					315.9
Property, plant and equipment	77.9							77.9
Investment in associate	203.1					(25.7)		177.4
Available-for-sale investments	9.8						(0.2)	9.6
Deferred tax asset	345.3			(190.5)				154.8
Restricted cash and cash equivalents	15.0							15.0
Other non-current assets	29.3				(10.0)		19.6	38.9
Total Non-Current Assets	828.3	207.4	(39.4)	(190.5)	(10.0)	(25.7)	19.4	789.5
Current Assets								
Inventory	20.1							20.1
Accounts receivable	171.4							171.4
Other current assets	13.5							13.5
Deferred tax asset				37.7				37.7
Income tax prepayment	2.9			(2.9)				
Available-for-sale investments	1.2							1.2
Restricted cash and cash equivalents	2.6							2.6
Cash and cash equivalents	491.9							491.9
Assets held for sale	349.4	4.5	(20.1)					333.8
Total Current Assets	1,053.0	4.5	(20.1)	34.8				1,072.2
Total Assets	1,881.3	211.9	(59.5)	(155.7)	(10.0)	(25.7)	19.4	1,861.7
Non-Current Liabilities								
Long-term debt	1,251.8						19.6	1,271.4
Other liabilities	35.8				15.5			51.3
Income tax payable	14.4			(1.9)				12.5
Total Non-Current Liabilities	1,302.0			(1.9)	15.5		19.6	1,335.2
Current Liabilities								
Accounts payable	38.5							38.5
Accrued and other liabilities	220.3						0.7	221.0
Provisions	0.7						(0.7)	
Income tax payable	1.0			(1.0)				
Liabilities held for sale	23.4							23.4
Total Current Liabilities	283.9			(1.0)				282.9
Total Liabilities	1,585.9			(2.9)	15.5		19.6	1,618.1

Shareholders Equity								
Total Shareholders Equity	295.4	211.9	(59.5)	(152.8)	(25.5)	(25.7)	(0.2)	243.6
Total Shareholders Equity and Liabilities	1,881.3	211.9	(59.5)	(155.7)	(10.0)	(25.7)	19.4	1,861.7

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Audited Consolidated Balance Sheet

At 31 December 2010

	IFRS $m	(B) Goodwill $m	(B) Other Intangible Assets $m	(C) Taxation $m	(G) Pension $m	(H) Other $m	U.S. GAAP $m
Non-Current Assets							
Goodwill and other intangible assets	225.7	211.9	(61.1)				376.5
Property, plant and equipment	287.5						287.5
Investment in associate	209.0						209.0
Available-for-sale investments	8.9					0.5	9.4
Deferred tax asset	336.7			(182.4)			154.3
Restricted cash and cash equivalents	14.9						14.9
Other non-current assets	34.6				(10.5)	21.3	45.4
Total Non-Current Assets	1,117.3	211.9	(61.1)	(182.4)	(10.5)	21.8	1,097.0
Current Assets							
Inventory	39.0						39.0
Accounts receivable	191.6						191.6
Other current assets	15.4						15.4
Deferred tax asset				41.8			41.8
Income tax prepayment	3.1			(3.1)			
Available-for-sale investments	2.0						2.0
Restricted cash and cash equivalents	208.2						208.2
Cash and cash equivalents	422.5						422.5
Total Current Assets	881.8			38.7			920.5
Total Assets	1,999.1	211.9	(61.1)	(143.7)	(10.5)	21.8	2,017.5
Non-Current Liabilities							
Long-term debt	1,249.1					21.3	1,270.4
Other liabilities	40.1				19.9		60.0
Income tax payable	14.2			(3.1)			11.1
Total Non-Current Liabilities	1,303.4			(3.1)	19.9	21.3	1,341.5
Current Liabilities							
Accounts payable	39.2						39.2
Accrued and other liabilities	235.5					207.0	442.5
Provisions	207.0					(207.0)	
Total Current Liabilities	481.7						481.7
Total Liabilities	1,785.1			(3.1)	19.9	21.3	1,823.2
Shareholders Equity							
Total Shareholders Equity	214.0	211.9	(61.1)	(140.6)	(30.4)	0.5	194.3

Total Shareholders Equity and Liabilities	1,999.1	211.9	(61.1)	(143.7)	(10.5)	21.8	2,017.5

The principal differences between IFRS as adopted by the European Union and U.S. GAAP, as they apply to our financial statements, are as follows:

(A) Tysabri

Tysabri was developed and is now being marketed in collaboration with Biogen Idec. In general, subject to certain limitations imposed by the parties, we share with Biogen Idec most development and commercialisation costs. Biogen Idec is responsible for manufacturing the product. In the United States, we purchase *Tysabri* from

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Biogen Idec and are responsible for distribution. Under U.S. GAAP, we record as revenue the net sales of *Tysabri* in the U.S. market. We purchase product from Biogen Idec as required at a price that includes the cost of manufacturing plus Biogen Idec s gross profit on *Tysabri,* and this cost, together with royalties payable to other third parties, is included in cost of sales. Outside of the United States, Biogen Idec is responsible for distribution and, under U.S. GAAP, we record as revenue our share of the profit or loss on EU sales of *Tysabri* plus our directly incurred expenses on these sales.

Under IFRS, the *Tysabri* collaboration is a jointly controlled operation in accordance with IAS 31. A jointly controlled operation is an operation of a joint venture (as defined in IAS 31) that>

Total Business Banking

50,454

11,151

(11,419

)

2,981

47,741

Unallocated	
	4,590
	564
	4,026
Total	

$

75,865

17,555

(19,168

)

4,259

73,219

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The following table provides information related to the loan portfolio by portfolio segment and by class of financing receivable at September 30, 2014 (in thousands):

	Recorded investment in loans receivable	Allowance for loan losses	Recorded investment in loans on nonaccrual (1)	Recorded investment in loans past due 90 days or more and still accruing	TDRs	Allowance related to TDRs	Additional commitments to customers with loans classified as TDRs
Personal Banking:							
Residental mortgage loans	$ 2,511,272	7,566	22,773		5,860	1,079	
Home equity loans	1,071,540	6,054	9,284	29	2,404	251	
Other consumer loans	238,653	5,985	2,407	339			
Total Personal Banking	3,821,465	19,605	34,464	368	8,264	1,330	
Business Banking:							
Commercial real estate loans	1,732,234	35,105	43,940		41,680	6,111	269
Commercial loans	403,402	12,543	11,422	22	11,922	1,847	1,050
Total Business Banking	2,135,636	47,648	55,362	22	53,602	7,958	1,319
Total	$ 5,957,101	67,253	89,826	390	61,866	9,288	1,319

(1) Includes $21.9 million of nonaccrual TDRs.

The following table provides information related to the loan portfolio by portfolio segment and by class of financing receivable at December 31, 2013 (in thousands):

	Recorded investment in loans receivable	Allowance for loan losses	Recorded investment in loans on nonaccrual (1)	Recorded investment in loans past due 90 days or more and still accruing	TDRs	Allowance related to TDRs	Additional commitments to customers with loans classified as TDRs
Personal Banking:							
Residental mortgage loans	$ 2,483,004	7,875	27,277		4,004	863	
Home equity loans	1,083,939	7,245	9,863	1	2,240	371	
Other consumer loans	228,348	5,487	2,257	666			
Total Personal Banking	3,795,291	20,607	39,397	667	6,244	1,234	
Business Banking:							
Commercial real estate loans	1,608,399	34,969	41,803		48,829	4,503	301
Commercial loans	402,601	11,110	26,021	23	24,093	2,778	454
Total Business Banking	2,011,000	46,079	67,824	23	72,922	7,281	755
Total	$ 5,806,291	66,686	107,221	690	79,166	8,515	755

(1) Includes $28.9 million of nonaccrual TDRS.

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The following table provides geographical and delinquency information related to the loan portfolio by portfolio segment and class of financing receivable at September 30, 2014 (in thousands):

	Pennsylvania	New York	Ohio	Maryland	Other	Total
Recorded investment in loans receivable:						
Personal Banking:						
Residential mortgage loans	$ 2,142,552	160,652	18,300	134,696	55,072	2,511,272
Home equity loans	913,085	116,423	9,216	27,133	5,683	1,071,540
Other consumer loans	220,610	9,903	3,209	1,694	3,237	238,653
Total Personal Banking	3,276,247	286,978	30,725	163,523	63,992	3,821,465
Business Banking:						
Commercial real estate loans	956,607	563,769	27,115	121,231	63,512	1,732,234
Commercial loans	286,515	87,262	11,820	10,404	7,401	403,402
Total Business Banking	1,243,122	651,031	38,935	131,635	70,913	2,135,636
Total	$ 4,519,369	938,009	69,660	295,158	134,905	5,957,101
Percentage of total loans receivable	75.8%	15.7%	1.2%	5.0%	2.3%	100.0%

	Pennsylvania	New York	Ohio	Maryland	Other	Total
Loans 90 or more days delinquent:						
Personal Banking:						
Residential mortgage loans	$ 15,015	1,038	777	1,601	1,887	20,318
Home equity loans	4,772	798	35	1,126	71	6,802
Other consumer loans	2,063	32	4			2,099
Total Personal Banking	21,850	1,868	816	2,727	1,958	29,219
Business Banking:						
Commercial real estate loans	11,491	1,396		48	617	13,552
Commercial loans	2,432	285	16	76	353	3,162
Total Business Banking	13,923	1,681	16	124	970	16,714
Total	$ 35,773	3,549	832	2,851	2,928	45,933
Percentage of total loans 90 or more days delinquent	77.9%	7.7%	1.8%	6.2%	6.4%	100.0%

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The following table provides geographical and delinquency information related to the loan portfolio by portfolio segment and class of financing receivable at December 31, 2013 (in thousands):

	Pennsylvania	New York	Ohio	Maryland	Other	Total
Recorded investment in loans receivable:						
Personal Banking:						
Residential mortgage loans	$ 2,108,018	160,931	19,468	140,087	54,500	2,483,004
Home equity loans	923,365	117,081	10,152	27,400	5,941	1,083,939
Other consumer loans	207,243	9,890	3,007	1,256	6,952	228,348
Total Personal Banking	3,238,626	287,902	32,627	168,743	67,393	3,795,291
Business Banking:						
Commercial real estate loans	876,359	484,071	27,136	123,279	97,554	1,608,399
Commercial loans	276,469	63,689	14,645	27,496	20,302	402,601
Total Business Banking	1,152,828	547,760	41,781	150,775	117,856	2,011,000
Total	$ 4,391,454	835,662	74,408	319,518	185,249	5,806,291
Percentage of total loans receivable	75.6%	14.4%	1.3%	5.5%	3.2%	100.0%

	Pennsylvania	New York	Ohio	Maryland	Other	Total
Loans 90 or more days delinquent:						
Personal Banking:						
Residential mortgage loans	$ 15,995	1,184	229	3,891	3,326	24,625
Home equity loans	5,279	1,783	116	1,095	71	8,344
Other consumer loans	2,006	35	3		13	2,057
Total Personal Banking	23,280	3,002	348	4,986	3,410	35,026
Business Banking:						
Commercial real estate loans	15,581	1,669	962	108	113	18,433
Commercial loans	3,045	645		314	294	4,298
Total Business Banking	18,626	2,314	962	422	407	22,731
Total	$ 41,906	5,316	1,310	5,408	3,817	57,757
Percentage of total loans 90 or more days delinquent	72.5%	9.2%	2.3%	9.4%	6.6%	100.0%

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The following table provides information related to the composition of impaired loans by portfolio segment and by class of financing receivable at and for the nine months ended September 30, 2014 (in thousands):

		Nonaccrual loans 90 or more days delinquent	Nonaccrual loans less than 90 days delinquent	Loans less than 90 days delinquent reviewed for impairment	TDRs less than 90 days delinquent not included elsewhere	Total impaired loans	Average recorded investment in impaired loans	Interest income recognized on impaired loans
Personal Banking:								
Residental mortgage loans	$	20,319	2,454		5,266	28,039	28,787	627
Home equity loans		6,802	2,482		2,110	11,394	11,886	364
Other consumer loans		2,098	309			2,407	2,273	45
Total Personal Banking		29,219	5,245		7,376	41,840	42,946	1,036
Business Banking:								
Commercial real estate loans		13,552	30,388	40,470	12,539	96,949	91,048	2,734
Commercial loans		3,162	8,260	5,497	2,894	19,813	28,376	731
Total Business Banking		16,714	38,648	45,967	15,433	116,762	119,424	3,465
Total	$	45,933	43,893	45,967	22,809	158,602	162,370	4,501

The following table provides information related to the composition of impaired loans by portfolio segment and by class of financing receivable at and for the year ended December 31, 2013 (in thousands):

		Nonaccrual loans 90 or more days delinquent	Nonaccrual loans less than 90 days delinquent	Loans less than 90 days delinquent reviewed for impairment	TDRs less than 90 days delinquent not included elsewhere	Total impaired loans	Average recorded investment in impaired loans	Interest income recognized on impaired loans
Personal Banking:								
Residental mortgage loans	$	24,625	2,652		3,372	30,649	29,994	723
Home equity loans		8,344	1,519		1,810	11,673	10,828	383
Other consumer loans		2,057	200			2,257	1,976	44
Total Personal Banking		35,026	4,371		5,182	44,579	42,798	1,150
Business Banking:								
Commercial real estate loans		18,433	23,370	39,199	13,060	94,062	90,912	3,678
Commercial loans		4,298	21,723	5,219	3,963	35,203	41,303	1,127
Total Business Banking		22,731	45,093	44,418	17,023	129,265	132,215	4,805
Total	$	57,757	49,464	44,418	22,205	173,844	175,013	5,955

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The following table provides information related to the evaluation of impaired loans by portfolio segment and by class of financing receivable at September 30, 2014 (in thousands):

	Loans collectively evaluated for impairment	Loans individually evaluated for impairment	Loans individually evaluated for impairment for which there is a related impairment reserve	Related impairment reserve	Loans individually evaluated for impairment for which there is no related reserve
Personal Banking:					
Residental mortgage loans	$ 2,504,491	6,781	6,781	1,071	
Home equity loans	1,069,256	2,284	2,284	261	
Other consumer loans	238,584	69	69	9	
Total Personal Banking	3,812,331	9,134	9,134	1,341	
Business Banking:					
Commercial real estate loans	1,650,683	81,551	48,830	7,954	32,721
Commercial loans	387,950	15,452	10,382	2,218	5,070
Total Business Banking	2,038,633	97,003	59,212	10,172	37,791
Total	$ 5,850,964	106,137	68,346	11,513	37,791

The following table provides information related to the evaluation of impaired loans by portfolio segment and by class of financing receivable at December 31, 2013 (in thousands):

	Loans collectively evaluated for impairment	Loans individually evaluated for impairment	Loans individually evaluated for impairment for which there is a related impairment reserve	Related impairment reserve	Loans individually evaluated for impairment for which there is no related reserve
Personal Banking:					
Residental mortgage loans	$ 2,477,888	5,116	5,116	1,136	
Home equity loans	1,081,699	2,240	2,240	333	
Other consumer loans	228,227	121	121	1	
Total Personal Banking	3,787,814	7,477	7,477	1,470	
Business Banking:					
Commercial real estate loans	1,532,117	76,282	45,761	6,300	30,521
Commercial loans	371,287	31,314	21,395	4,133	9,919
Total Business Banking	1,903,404	107,596	67,156	10,433	40,440
Total	$ 5,691,218	115,073	74,633	11,903	40,440

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Our loan portfolios include loans that have been modified in a troubled debt restructuring (TDR), where concessions have been granted to borrowers who have experienced financial difficulties. These concessions typically result from our loss mitigation activities and could include: extending the note s maturity date, permitting interest only payments, reducing the interest rate to a rate lower than current market rates for new debt with similar risk, reducing the principal payment, principal forbearance or other actions. These concessions are applicable to all loan segments and classes. Certain TDRs are classified as nonperforming at the time of restructuring and may be returned to performing status after considering the borrower s sustained repayment performance for a reasonable period of at least six months.

When we modify loans in a TDR, we evaluate any possible impairment similar to other impaired loans based on the present value of expected future cash flows, discounted at the contractual interest rate of the original loan agreement, the loan s observable market price or the current fair value of the collateral, less selling costs, for collateral dependent loans. If we determine that the value of the modified loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), impairment is recognized through an allowance estimate or a charge-off to the allowance. In periods subsequent to modification, we evaluate all TDRs, including those that have payment defaults, for possible impairment, using ASC 310-10. As a result, loans modified in a TDR may have the financial effect of increasing the specific allowance associated with the loan.

Loans modified in a TDR are closely monitored for delinquency as an early indicator of possible future default. If loans modified in a TDR subsequently default, we evaluate the loan for possible further impairment. The allowance may be increased, adjustments may be made in the allocation of the allowance, partial charge-offs may be taken to further write-down the carrying value of the loan, or the loan may be charged-off completely.

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The following table provides a roll forward of troubled debt restructurings for the periods indicated (in thousands):

	For the quarters ended September 30,			
	2014		2013	
	Number of contracts		Number of contracts	
Beginning TDR balance:	265	$ 63,793	260	$ 86,517
New TDRs	14	5,302	19	1,977
Net paydowns		(5,411)		(2,878)
Charge-offs:				
Residential mortgage loans			2	(185)
Home equity loans				
Commercial real estate loans	4	(346)		
Commercial loans	1	(38)	3	(233)
Paid-off loans:				
Residential mortgage loans				
Home equity loans	2	(35)	1	(2)
Commercial real estate loans	4	(633)	2	(2,268)
Commercial loans	8	(766)	12	(1,468)
Transferred to real estate owned:				
Commercial loans			1	(2,070)
Ending TDR balance:	260	$ 61,866	258	$ 79,390
Accruing TDRs		$ 39,995		$ 41,871
Non-accrual TDRs		21,871		37,519

The following table provides a roll forward of troubled debt restructurings for the periods indicated (in thousands):

	For the nine months ended September 30,			
	2014		2013	
	Number of contracts		Number of contracts	
Beginning TDR balance:	276	$ 79,166	225	$ 89,444
New TDRs	30	8,113	84	11,310
Net paydowns		(12,431)		(10,784)
Charge-offs:				
Residential mortgage loans			4	(357)
Home equity loans	1	(130)	4	(99)
Commercial real estate loans	6	(377)	4	(1,063)
Commercial loans	9	(8,289)	5	(250)
Paid-off loans:				
Residential mortgage loans			1	(109)
Home equity loans	3	(74)	3	(9)
Commercial real estate loans	10	(1,471)	7	(3,119)
Commercial loans	17	(2,641)	22	(3,504)
Transferred to real estate owned:				
Commercial loans			1	(2,070)
Ending TDR balance:	260	$ 61,866	258	$ 79,390
Accruing TDRs		$ 39,995		$ 41,871
Non-accrual TDRs		21,871		37,519

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The following table provides information related to troubled debt restructurings (including re-modified TDRs) by portfolio segment and by class of financing receivable during the periods indicated (dollars in thousands):

	For the quarter ended September 30, 2014				For the nine months ended September 30, 2014			
	Number of contracts	Recorded investment at the time of modification	Current recorded investment	Current allowance	Number of contracts	Recorded investment at the time of modification	Current recorded investment	Current allowance
Troubled debt restructurings:								
Personal Banking:								
Residential mortgage loans	1	$ 145	108	37	10	$ 2,067	1,964	221
Home equity loans	1	136	106	30	3	512	451	32
Other consumer loans								
Total Personal Banking	2	281	214	67	13	2,579	2,415	253
Business Banking:								
Commercial real estate loans	5	454	453	30	8	543	533	61
Commercial loans	7	4,567	3,777	1,198	9	4,991	4,209	1,233
Total Business Banking	12	5,021	4,230	1,228	17	5,534	4,742	1,294
Total	14	$ 5,302	4,444	1,295	30	$ 8,113	7,157	1,547
Troubled debt restructurings modified within the previous twelve months that have subsequently defaulted:								
Personal Banking:								
Residential mortgage loans		$				$		
Home equity loans	1	4	3		1	4	3	
Other consumer loans								
Total Personal Banking	1	4	3		1	4	3	
Business Banking:								
Commercial real estate loans								
Commercial loans					3	7,572	417	18
Total Business Banking					3	7,572	417	18
Total	1	$ 4	3		4	$ 7,576	420	18

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The following table provides information related to troubled debt restructurings (including re-modified TDRs) by portfolio segment and by class of financing receivable during the periods indicated (dollars in thousands):

	For the quarter ended September 30, 2013				For the nine months ended September 30, 2013			
	Number of contracts	Recorded investment at the time of modification	Current recorded investment	Current allowance	Number of contracts	Recorded investment at the time of modification	Current recorded investment	Current allowance
Troubled debt restructurings:								
Personal Banking:								
Residential mortgage loans		$			2	$ 179	172	16
Home equity loans	1	6	6		5	296	286	134
Other consumer loans								
Total Personal Banking	1	6	6		7	475	458	150
Business Banking:								
Commercial real estate loans	14	1,900	1,780	277	49	8,982	7,353	1,641
Commercial loans	4	71	71	3	28	1,853	1,384	204
Total Business Banking	18	1,971	1,851	280	77	10,835	8,737	1,845
Total	19	$ 1,977	1,857	280	84	$ 11,310	9,195	1,995
Troubled debt restructurings modified within the previous twelve months that have subsequently defaulted:								
Personal Banking:								
Residential mortgage loans		$			1	$ 70	70	5
Home equity loans								
Other consumer loans								
Total Personal Banking					1	70	70	5
Business Banking:								
Commercial real estate loans	3	269	268	76	3	269	268	76
Commercial loans	1	23	8	2	1	23	8	2
Total Business Banking	4	292	276	78	4	292	276	78
Total	4	$ 292	276	78	5	$ 362	346	83

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The following table provides information as of September 30, 2014 for troubled debt restructurings (including re-modified TDRs) by type of modification, by portfolio segment and class of financing receivable for modifications during the quarter ended September 30, 2014 (dollars in thousands):

		Type of modification				
	Number of contracts	Rate	Payment	Maturity date	Other	Total
Personal Banking:						
Residental mortgage loans	1	$	108			108
Home equity loans	1		106			106
Other consumer loans						
Total Personal Banking	2		214			214
Business Banking:						
Commercial real estate loans	5			203	250	453
Commercial loans	7		1,453	2,319	5	3,777
Total Business Banking	12		1,453	2,522	255	4,230
Total	14	$	1,667	2,522	255	4,444

The following table provides information as of September 30, 2013 for troubled debt restructurings (including re-modified TDRs) by type of modification, by portfolio segment and class of financing receivable for modifications during the quarter ended September 30, 2013 (dollars in thousands):

		Type of modification				
	Number of contracts	Rate	Payment	Maturity date	Other	Total
Personal Banking:						
Residental mortgage loans		$				
Home equity loans	1			6		6
Other consumer loans						
Total Personal Banking	1			6		6
Business Banking:						
Commercial real estate loans	14		646	193	941	1,780
Commercial loans	4				71	71
Total Business Banking	18		646	193	1,012	1,851
Total	19	$	646	199	1,012	1,857

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The following table provides information as of September 30, 2014 for troubled debt restructurings (including re-modified TDRs) by type of modification, by portfolio segment and class of financing receivable for modifications during the nine months ended September 30, 2014 (dollars in thousands):

		Type of modification				
	Number of contracts	**Rate**	**Payment**	**Maturity date**	**Other**	**Total**
Personal Banking:						
Residental mortgage loans	10	$	108	1,856		1,964
Home equity loans	3		106	345		451
Other consumer loans						
Total Personal Banking	13		214	2,201		2,415
Business Banking:						
Commercial real estate loans	8			260	273	533
Commercial loans	9		1,563	2,319	327	4,209
Total Business Banking	17		1,563	2,579	600	4,742
Total	30	$	1,777	4,780	600	7,157

The following table provides information as of September 30, 2013 for troubled debt restructurings (including re-modified TDRs) by type of modification, by portfolio segment and class of financing receivable for modifications during the nine months ended September 30, 2013 (dollars in thousands):

		Type of modification				
	Number of contracts	**Rate**	**Payment**	**Maturity date**	**Other**	**Total**
Personal Banking:						
Residental mortgage loans	2	$		172		172
Home equity loans	5			286		286
Other consumer loans						
Total Personal Banking	7			458		458
Business Banking:						
Commercial real estate loans	49	728	1,086	3,892	1,647	7,353
Commercial loans	28	134	212	748	290	1,384
Total Business Banking	77	862	1,298	4,640	1,937	8,737
Total	84	$ 862	1,298	5,098	1,937	9,195

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The following table provides information related to re-modified troubled debt restructurings by portfolio segment and by class of financing receivable for the quarter ended September 30, 2014 (dollars in thousands):

	Number of re-modified TDRs	Type of re-modification				
		Rate	**Payment**	**Maturity date**	**Other**	**Total**
Personal Banking:						
Residental mortgage loans		$				
Home equity loans						
Other consumer loans						
Total Personal Banking						
Business Banking:						
Commercial real estate loans	2			114		114
Commercial loans	2			2,064		2,064
Total Business Banking	4			2,178		2,178
Total	4	$		2,178		2,178

The following table provides information related to re-modified troubled debt restructurings by portfolio segment and by class of financing receivable for the quarter ended September 30, 2013 (dollars in thousands):

	Number of re-modified TDRs	Type of re-modification				
		Rate	**Payment**	**Maturity date**	**Other**	**Total**
Personal Banking:						
Residental mortgage loans		$				
Home equity loans						
Other consumer loans						
Total Personal Banking						
Business Banking:						
Commercial real estate loans	4		227	430		657
Commercial loans						
Total Business Banking	4		227	430		657
Total	4	$	227	430		657

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The following table provides information related to re-modified troubled debt restructurings by portfolio segment and by class of financing receivable for the nine months ended September 30, 2014 (dollars in thousands):

	Number of re-modified TDRs	Type of re-modification				
		Rate	Payment	Maturity date	Other	Total
Personal Banking:						
Residental mortgage loans	1	$		76		76
Home equity loans						
Other consumer loans						
Total Personal Banking	1			76		76
Business Banking:						
Commercial real estate loans	4			171	18	189
Commercial loans	3			2,064	5	2,069
Total Business Banking	7			2,235	23	2,258
Total	8	$		2,311	23	2,334

The following table provides information related to re-modified troubled debt restructurings by portfolio segment and by class of financing receivable for the nine months ended September 30, 2013 (dollars in thousands):

	Number of re-modified TDRs	Type of re-modification				
		Rate	Payment	Maturity date	Other	Total
Personal Banking:						
Residental mortgage loans		$				
Home equity loans						
Other consumer loans						
Total Personal Banking						
Business Banking:						
Commercial real estate loans	6		227	4,007		4,234
Commercial loans	1					
Total Business Banking	7		227	4,007		4,234
Total	7	$	227	4,007		4,234

The following table provides information related to loan payment delinquencies at September 30, 2014 (in thousands):

		30-59 Days delinquent	60-89 Days delinquent	90 Days or greater delinquent	Total delinquency	Current	Recorded investment in loans receivable
Personal Banking:							
Residential mortgage loans	$	4,241	6,558	20,319	31,118	2,480,154	2,511,272
Home equity loans		5,856	1,727	6,802	14,385	1,057,155	1,071,540
Other consumer loans		5,076	1,958	2,098	9,132	229,521	238,653
Total Personal Banking		15,173	10,243	29,219	54,635	3,766,830	3,821,465
Business Banking:							
Commercial real estate loans		5,888	2,762	13,552	22,202	1,710,032	1,732,234
Commercial loans		1,413	970	3,162	5,545	397,857	403,402
Total Business Banking		7,301	3,732	16,714	27,747	2,107,889	2,135,636
Total	$	22,474	13,975	45,933	82,382	5,874,719	5,957,101

The following table provides information related to loan payment delinquencies at December 31, 2013 (in thousands):

		30-59 Days delinquent	60-89 Days delinquent	90 Days or greater delinquent	Total delinquency	Current	Recorded investment in loans receivable
Personal Banking:							
Residential mortgage loans	$	27,486	7,568	24,625	59,679	2,423,325	2,483,004
Home equity loans		6,946	2,243	8,344	17,533	1,066,406	1,083,939
Other consumer loans		4,515	1,866	2,057	8,438	219,910	228,348
Total Personal Banking		38,947	11,677	35,026	85,650	3,709,641	3,795,291
Business Banking:							
Commercial real estate loans		8,449	3,968	18,433	30,850	1,577,549	1,608,399
Commercial loans		9,243	1,555	4,298	15,096	387,505	402,601
Total Business Banking		17,692	5,523	22,731	45,946	1,965,054	2,011,000
Total	$	56,639	17,200	57,757	131,596	5,674,695	5,806,291

Credit quality indicators: We categorize loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. We analyze loans individually by classifying the loans by credit risk. Credit relationships greater than or equal to $1.0 million classified as special mention or substandard are reviewed quarterly for deterioration or improvement to determine if the loan is appropriately classified. We use the following definitions for risk ratings other than pass:

Special mention Loans designated as special mention have specific, well-defined risk issues, which create a high level of uncertainty regarding the long-term viability of the business. Loans in this class are considered to have high-risk characteristics. A special mention loan exhibits material negative financial trends due to company-specific or systemic conditions. If these potential weaknesses are not mitigated, they threaten the borrower s capacity to meet its debt obligations. Special mention loans still demonstrate sufficient financial flexibility to react to and

positively

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address the root cause of the adverse financial trends without significant deviations from their current business strategy. Their potential weaknesses deserve our close attention and warrant enhanced monitoring.

Substandard Loans classified as substandard are inadequately protected by the current net worth and payment capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that we will sustain some loss if the deficiencies are not corrected.

Doubtful Loans classified as doubtful have all the weaknesses inherent in those classified as substandard. In addition, those weaknesses make collection or liquidation in full highly questionable and improbable. A loan classified as doubtful exhibits discernible loss potential, but a complete loss seems very unlikely. The possibility of a loss on a doubtful loan is high, but because of certain important and reasonably specific pending factors that may strengthen the loan, its classification as an estimated loss is deferred until a more exact status can be determined.

Loss Loans classified as loss are considered uncollectible and of such value that the continuance as a loan is not warranted. A loss classification does not mean that the loan has no recovery or salvage value; instead, it means that it is not practical or desirable to defer writing off all or a portion of a basically worthless loan even though partial recovery may be possible in the future.

The following table sets forth information about credit quality indicators, which were updated during the quarter ended September 30, 2014 (in thousands):

		Pass	Special mention	Substandard	Doubtful	Loss	Recorded investment in loans receivable
Personal Banking:							
Residential mortgage loans	$	2,494,746		15,102		1,424	2,511,272
Home equity loans		1,064,738		6,802			1,071,540
Other consumer loans		237,134		1,519			238,653
Total Personal Banking		3,796,618		23,423		1,424	3,821,465
Business Banking:							
Commercial real estate loans		1,545,245	40,655	144,244	2,090		1,732,234
Commercial loans		350,377	14,391	35,343	3,291		403,402
Total Business Banking		1,895,622	55,046	179,587	5,381		2,135,636
Total	$	5,692,240	55,046	203,010	5,381	1,424	5,957,101

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The following table sets forth information about credit quality indicators, which were updated during the year ended December 31, 2013 (in thousands):

	Pass	Special mention	Substandard	Doubtful	Loss	Recorded investment in loans receivable
Personal Banking:						
Residential mortgage loans	$ 2,464,057		17,626		1,321	2,483,004
Home equity loans	1,075,595		8,344			1,083,939
Other consumer loans	226,922		1,426			228,348
Total Personal Banking	3,766,574		27,396		1,321	3,795,291
Business Banking:						
Commercial real estate loans	1,398,652	46,557	161,906	1,284		1,608,399
Commercial loans	345,612	12,045	43,040	1,904		402,601
Total Business Banking	1,744,264	58,602	204,946	3,188		2,011,000
Total	$ 5,510,838	58,602	232,342	3,188	1,321	5,806,291

(5) Goodwill and Other Intangible Assets

The following table provides information for intangible assets subject to amortization at the dates indicated (in thousands):

	September 30, 2014	December 31, 2013
Amortizable intangible assets:		
Core deposit intangibles gross	$ 30,578	30,578
Acquisitions		
Less: accumulated amortization	(30,556)	(30,491)
Core deposit intangibles net	22	87
Customer and Contract intangible assets gross	6,197	6,197
Acquisitions	2,037	
Less: accumulated amortization	(4,892)	(3,965)
Customer and Contract intangible assets net	$ 3,342	2,232

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The following table shows the actual aggregate amortization expense for the quarters and nine months ended September 30, 2014 and 2013, as well as the estimated aggregate amortization expense, based upon current levels of intangible assets, for the current fiscal year and each of the five succeeding fiscal years (in thousands):

For the quarter ended September 30, 2014	$	330
For the quarter ended September 30, 2013		291
For the nine months ended September 30, 2014		992
For the nine months ended September 30, 2013		988
For the year ending December 31, 2014		1,323
For the year ending December 31, 2015		1,008
For the year ending December 31, 2016		779
For the year ending December 31, 2017		550
For the year ending December 31, 2018		391
For the year ending December 31, 2019		232

The following table provides information for the changes in the carrying amount of goodwill (in thousands):

		Community Banks	Consumer Finance	Total
Balance at December 31, 2012	$	173,029	1,613	174,642
Goodwill acquired		2		2
Impairment losses				
Balance at December 31, 2013		173,031	1,613	174,644
Goodwill acquired		1,525		1,525
Impairment losses				
Balance at September 30, 2014	$	174,556	1,613	176,169

We performed our annual goodwill impairment test as of June 30, 2014 and concluded that goodwill was not impaired. At September 30, 2014, there were no changes in our operations or other factors that would cause us to update that test. See the Overview of Critical Accounting Policies Involving Estimates section for a description of our testing procedures.

(6) Guarantees

We issue standby letters of credit in the normal course of business. Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Standby letters of credit generally are contingent upon the failure of the customer to perform according to the terms of the underlying contract with the third party. We are required to perform under a standby letter of credit when drawn upon by the guaranteed third party in the case of nonperformance by our customer. The credit risk associated with standby letters of credit is essentially the same as that involved in extending loans to customers and is subject to normal loan underwriting procedures. Collateral may be obtained based on management s credit assessment of the customer. At September 30, 2014, the maximum potential amount of future payments we could be required to make under these standby letters of credit was $23.8 million, of which $22.9 million is fully collateralized. At September 30, 2014, we had a liability, which represents deferred income, of $1.0 million related to the standby letters of credit. There are no recourse provisions that would enable us to recover any amounts from third parties.

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(7) Earnings Per Share

Basic earnings per common share (EPS) is computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding for the period, without considering any dilutive items. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Company. Stock options to purchase 584,711 shares of common stock with a weighted average exercise price of $13.15 per share were outstanding during the quarter ended September 30, 2014 but were not included in the computation of diluted earnings per share because the options exercise price was greater than the average market price of the common shares of $12.63. All stock options outstanding during the nine months ended September 30, 2014 were included in the computation of diluted earnings per share because the stock options exercise price was less than the average market price of the common shares of $13.60. All stock options outstanding during the quarter and nine months ended September 30, 2013 were included in the computation of diluted earnings per share because the stock options exercise price was less than the average market price of the common shares of $13.77 and $12.92, respectively.

The computation of basic and diluted earnings per share follows (in thousands, except share data and per share amounts):

		Quarter ended September 30,		Nine months ended September 30,	
		2014	2013	2014	2013
Reported net income	$	17,332	17,567	44,617	46,187
Weighted average common shares outstanding		91,745,512	90,760,402	91,465,986	90,530,417
Dilutive potential shares due to effect of stock options		372,642	1,063,982	867,124	679,623
Total weighted average common shares and dilutive potential shares		92,118,154	91,824,384	92,333,110	91,210,040
Basic earnings per share:	$	0.19	0.19	0.49	0.51
Diluted earnings per share:	$	0.19	0.19	0.48	0.51

(8) Pension and Other Post-retirement Benefits

During 2013, the defined benefit pension plan was amended to lock-in all benefits earned through March 31, 2013 based on the plan formula using years of service and average monthly compensation as of March 31, 2013 and provide that, for service commencing January 1, 2013, additional benefits will be earned equal to 1% of career average pay for each year that a participant completes at least 1,000 hours of service. Also, effective April 1, 2013, participants who are eligible to receive required minimum distributions due to attaining age 70 ½ will be required to begin payment of benefits even though they may remain employed by us.

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The following table sets forth the net periodic costs for the defined benefit pension plans and post retirement healthcare plans for the periods indicated (in thousands):

Components of net periodic benefit cost

	Quarter ended September 30,			
	Pension benefits		Other post-retirement benefits	
	2014	2013	2014	2013
Service cost	$ 1,035	1,138		
Interest cost	1,457	1,301	16	16
Expected return on plan assets	(2,416)	(2,138)		
Amortization of prior service cost	(581)	(580)		
Amortization of the net loss	357	919	12	13
Net periodic (benefit)/ cost	$ (148)	640	28	29

Components of net periodic benefit cost

	Nine months ended September 30,			
	Pension benefits		Other post-retirement benefits	
	2014	2013	2014	2013
Service cost	$ 3,105	3,414		
Interest cost	4,371	3,903	49	49
Expected return on plan assets	(7,248)	(6,414)		
Amortization of prior service cost	(1,743)	(1,740)		
Amortization of the net loss	1,070	2,757	36	38
Net periodic (benefit)/ cost	$ (445)	1,920	85	87

We made no contribution to our pension or other post-retirement benefit plans during the nine months ended September 30, 2014 and do not anticipate making a contribution to our defined benefit pension plan during the year ending December 31, 2014.

(9) Disclosures About Fair Value of Financial Instruments

Fair value information about financial instruments, whether or not recognized in the consolidated statement of financial condition, is required to be disclosed. These requirements exclude certain financial instruments and all nonfinancial instruments. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Company.

Financial assets and liabilities recognized or disclosed at fair value on a recurring basis and certain financial assets and liabilities on a non-recurring basis are accounted for using a three-level hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. This hierarchy gives the highest priority to quoted prices with readily available independent data in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable market inputs (Level 3). When various inputs

for measurement fall within different levels of the fair value hierarchy, the lowest level input that has a significant impact on fair value measurement is used.

Financial assets and liabilities are categorized based upon the following characteristics or inputs to the valuation techniques:

- Level 1 Financial assets and liabilities for which inputs are observable and are obtained from reliable quoted prices for identical assets or liabilities in actively traded markets. This is the most reliable fair value measurement and includes, for example, active exchange-traded equity securities.

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- Level 2 Financial assets and liabilities for which values are based on quoted prices in markets that are not active or for which values are based on similar assets or liabilities that are actively traded. Level 2 also includes pricing models in which the inputs are corroborated by market data, for example, matrix pricing.

- Level 3 Financial assets and liabilities for which values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. Level 3 inputs include the following:

- Quotes from brokers or other external sources that are not considered binding;

- Quotes from brokers or other external sources where it cannot be determined that market participants would in fact transact for the asset or liability at the quoted price;

- Quotes and other information from brokers or other external sources where the inputs are not deemed observable.

We are responsible for the valuation process and as part of this process may use data from outside sources in establishing fair value. We perform due diligence to understand the inputs used or how the data was calculated or derived. We also corroborate the reasonableness of external inputs in the valuation process.

The carrying amounts reported in the consolidated statement of financial condition approximate fair value for the following financial instruments: cash on hand, interest-earning deposits in other institutions, federal funds sold and other short-term investments, accrued interest receivable, accrued interest payable, and marketable securities available-for-sale.

Marketable Securities

Where available, market values are based on quoted market prices, dealer quotes, and prices obtained from independent pricing services.

Debt securities available for sale - Generally, debt securities are valued using pricing for similar securities, recently executed transactions and other pricing models utilizing observable inputs. The valuation for most debt securities is classified as Level 2. Securities within Level 2 include corporate bonds, municipal bonds, mortgage-backed securities and US government obligations. Certain corporate debt securities do not have an active market and as such the broker pricing received uses alternative methods. The fair value of these corporate debt securities is determined by using a discounted cash flow model using market assumptions, which generally include cash flow, collateral and other market assumptions. As such, these securities are included herein as Level 3 assets.

Equity securities available for sale Level 1 securities include publicly traded securities valued using quoted market prices. We consider the financial condition of the issuer to determine if the securities have indicators of impairment.

Debt securities held to maturity - The fair value of debt securities held to maturity is determined in the same manner as debt securities available for sale.

Loans Receivable

Loans with comparable characteristics including collateral and re-pricing structures are segregated for valuation purposes. Characteristics include remaining term, coupon interest, and estimated prepayment speeds. Delinquent loans are separately evaluated given the impact delinquency has on the projected future cash flow of the loan and the approximate discount or market rate. Each loan pool is separately valued utilizing a discounted cash flow analysis. Projected monthly cash flows are discounted to present value using a market rate for comparable loans, which is not considered an exit price.

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FHLB Stock

Due to the restrictions placed on the transferability of FHLB stock it is not practical to determine the fair value.

Deposit Liabilities

The estimated fair value of deposits with no stated maturity, which includes demand deposits, money market, and other savings accounts, is the amount payable on demand. Although market premiums paid for depository institutions reflect an additional value for these low-cost deposits, adjusting fair value for any value expected to be derived from retaining those deposits for a future period of time or from the benefit that results from the ability to fund interest-earning assets with these deposit liabilities is prohibited. The fair value estimates of deposit liabilities do not include the benefit that results from the low-cost funding provided by these deposits compared to the cost of borrowing funds in the market. Fair values for time deposits are estimated using a discounted cash flow calculation that applies contractual cost currently being offered in the existing portfolio to current market rates being offered locally for deposits of similar remaining maturities. The valuation adjustment for the portfolio consists of the present value of the difference of these two cash flows, discounted at the assumed market rate of the corresponding maturity.

Borrowed Funds

Fixed rate advances are valued by comparing their contractual cost to the prevailing market cost. The carrying amount of collateralized borrowings approximates the fair value.

Junior Subordinated Debentures

The fair value of junior subordinated debentures is calculated using the discounted cash flows at the prevailing rate of interest.

Cash flow hedges Interest rate swap agreements (swaps)

The fair value of the swaps is the amount we would expect to pay to terminate the agreements and is based upon the present value of the expected future cash flows using the LIBOR swap curve, the basis for the underlying interest rate.

Off-Balance Sheet Financial Instruments

These financial instruments generally are not sold or traded, and estimated fair values are not readily available. However, the fair value of commitments to extend credit and standby letters of credit is estimated using the fees currently charged to enter into similar agreements. Commitments to extend credit are generally short-term in nature and, if drawn upon, are issued under current market terms. At September 30, 2014 and December 31, 2013, there was no significant unrealized appreciation or depreciation on these financial instruments.

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The following table sets forth the carrying amount and estimated fair value of our financial instruments included in the consolidated statement of financial condition at September 30, 2014:

		Carrying amount	Estimated fair value	Level 1	Level 2	Level 3
Financial assets:						
Cash and cash equivalents	$	293,789	293,789	293,789		
Securities available-for-sale		930,913	930,913	3,248	916,799	10,866
Securities held-to-maturity		110,214	113,322		113,322	
Loans receivable, net		5,885,451	6,225,823			6,225,823
Accrued interest receivable		19,505	19,505	19,505		
FHLB Stock		43,985	43,985			
Total financial assets	$	7,283,857	7,627,337	316,542	1,030,121	6,236,689
Financial liabilities:						
Savings and checking deposits	$	4,174,908	4,174,908	4,174,908		
Time deposits		1,532,815	1,555,888			1,555,888
Borrowed funds		878,448	905,011	153,040		751,971
Junior subordinated debentures		103,094	109,609			109,609
Cash flow hedges - swaps		6,453	6,453		6,453	
Accrued interest payable		880	880	880		
Total financial liabilities	$	6,696,598	6,752,749	4,328,828	6,453	2,417,468

The following table sets forth the carrying amount and estimated fair value of our financial instruments included in the consolidated statement of financial condition at December 31, 2013:

		Carrying amount	Estimated fair value	Level 1	Level 2	Level 3
Financial assets:						
Cash and cash equivalents	$	391,905	391,905	391,905		
Securities available-for-sale		1,016,767	1,016,767	9,850	994,666	12,251
Securities held-to-maturity		121,366	124,061		124,061	
Loans receivable, net		5,734,943	6,026,711	221		6,026,490
Accrued interest receivable		19,152	19,152	19,152		
FHLB Stock		43,715	43,715			
Total financial assets	$	7,327,848	7,622,311	421,128	1,118,727	6,038,741
Financial liabilities:						
Savings and checking accounts	$	4,001,482	4,001,482	4,001,482		
Time deposits		1,667,397	1,699,937			1,699,937
Borrowed funds		881,645	896,408	156,198		740,210
Junior subordinated debentures		103,094	111,220			111,220
Cash flow hedges - swaps		8,037	8,037		8,037	
Accrued interest payable		888	888	888		
Total financial liabilities	$	6,662,543	6,717,972	4,158,568	8,037	2,551,367

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Fair value estimates are made at a point-in-time, based on relevant market data and information about the instrument. The methods and assumptions detailed above were used in estimating the fair value of financial instruments at both September 30, 2014 and December 31, 2013. There were no transfers of financial instruments between Level 1 and Level 2 during the nine months ended September 30, 2014.

The following table represents assets and liabilities measured at fair value on a recurring basis at September 30, 2014 (in thousands):

	Level 1	Level 2	Level 3	Total assets at fair value
Equity securities	$ 3,248			3,248
Debt securities:				
U.S. government and agencies		27		27
Government sponsored enterprises		319,385		319,385
States and political subdivisions		76,368		76,368
Corporate		10,591	10,866	21,457
Total debt securities		406,371	10,866	417,237
Residential mortgage-backed securities:				
GNMA		30,137		30,137
FNMA		76,529		76,529
FHLMC		44,700		44,700
Non-agency		648		648
Collateralized mortgage obligations:				
GNMA		9,113		9,113
FNMA		146,260		146,260
FHLMC		188,605		188,605
SBA		10,804		10,804
Non-agency		3,632		3,632
Total mortgage-backed securities		510,428		510,428
Interest rate swaps		(6,453)		(6,453)
Total assets and liabilities	$ 3,248	910,346	10,866	924,460

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The following table represents assets and liabilities measured at fair value on a recurring basis at December 31, 2013 (in thousands):

	Level 1	Level 2	Level 3	Total assets at fair value
Equity securities	$ 9,850			9,850
Debt securities:				
U.S. government and agencies		32		32
Government sponsored enterprises		316,057		316,057
States and political subdivisions		92,578		92,578
Corporate		8,925	12,251	21,176
Total debt securities		417,592	12,251	429,843
Residential mortgage-backed securities:				
GNMA		32,263		32,263
FNMA		85,665		85,665
FHLMC		51,076		51,076
Non-agency		667		667
Collateralized mortgage obligations:				
GNMA		11,494		11,494
FNMA		168,661		168,661
FHLMC		210,029		210,029
SBA		12,569		12,569
Non-agency		4,650		4,650
Total mortgage-backed securities		577,074		577,074
Interest rate swaps		(8,037)		(8,037)
Total assets and liabilities	$ 9,850	986,629	12,251	1,008,730

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The table below presents a reconciliation of all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the periods indicated (in thousands):

		Quarter ended		Nine months ended	
		September 30, 2014	September 30, 2013	September 30, 2014	September 30, 2013
Beginning balance	$	12,543	11,345	12,251	11,119
Total net realized investment gains/ (losses) and net change in unrealized appreciation/ (depreciation):					
Included in net income as OTTI					
Included in other comprehensive income		(1,677)	363	(1,385)	589
Purchases					
Sales					
Transfers in to Level 3					
Transfers out of Level 3					
Ending balance	$	10,866	11,708	10,866	11,708

Certain assets and liabilities are measured at fair value on a nonrecurring basis after initial recognition such as loans measured for impairment and real estate owned. The following table represents the fair value measurement for nonrecurring assets at September 30, 2014 (in thousands):

		Level 1	Level 2	Level 3	Total assets at fair value
Loans measured for impairment	$			56,833	56,833
Real estate owned				15,007	15,007
Total assets	$			71,840	71,840

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Certain assets and liabilities are measured at fair value on a nonrecurring basis after initial recognition such as loans measured for impairment and real estate owned. The following table represents the fair value measurement for nonrecurring assets at December 31, 2013 (in thousands):

		Level 1	Level 2	Level 3	Total assets at fair value
Loans measured for impairment	$			62,730	62,730
Real estate owned				18,203	18,203
Total assets	$			80,933	80,933

Impaired loans A loan is considered to be impaired as described in the Overview of Critical Accounting Policies Involving Estimates, Allowance for Loan Losses section. We classify loans individually evaluated for impairment that require a specific or TDR reserve as nonrecurring Level 3.

Real Estate Owned Real estate owned is comprised of property acquired through foreclosure or voluntarily conveyed by delinquent borrowers. These assets are recorded on the date acquired at the lower of the related loan balance or fair value, less estimated disposition costs, with the fair value being determined by appraisal. Subsequently, foreclosed assets are valued at the lower of the amount recorded at acquisition date or fair value, less estimated disposition costs. We classify all real estate owned as nonrecurring Level 3.

The table presents additional quantitative information about assets measured at fair value on a recurring and nonrecurring basis and for which we have utilized Level 3 inputs to determine fair value at September 30, 2014 (dollar amounts in thousands):

		Fair value	Valuation techniques	Significant unobservable inputs	Range (weighted average)
Debt securities	$	10,866	Discounted cash flow	Discount margin Default rates Prepayment speeds	0.35% to 2.1% (0.69)% 1.00% 1.00% annually
Loans measured for impairment		56,833	Appraisal value (1)	Estimated cost to sell	10%
Real estate owned		15,007	Appraisal value (1)	Estimated cost to sell	10%

(1) Fair value is generally determined through independent appraisals of the underlying collateral, which may include level 3 inputs that are not identifiable, or by using the discounted cash flow method if the loan is not collateral dependent.

The significant unobservable inputs used in the fair value measurement of our debt securities are discount margins, default rates and prepayment speeds. Significant increases in any of those rates would result in a significantly lower fair value measurement.

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(10) Guaranteed Preferred Beneficial Interests in the Company s Junior Subordinated Deferrable Interest Debentures (Trust Preferred Securities) and Interest Rate Swaps

We have two statutory business trusts: Northwest Bancorp Capital Trust III, a Delaware statutory business trust and Northwest Bancorp Statutory Trust IV, a Connecticut statutory business trust (Trusts). These trusts exist solely to issue preferred securities to third parties for cash, issue common securities to the Company in exchange for capitalization of the Trusts, invest the proceeds from the sale of the trust securities in an equivalent amount of debentures of the Company, and engage in other activities that are incidental to those previously listed.

Northwest Bancorp Capital Trust III (Trust III) issued 50,000 cumulative trust preferred securities in a private transaction to a pooled investment vehicle on December 5, 2006 (liquidation value of $1,000 per preferred security or $50,000,000) with a stated maturity of December 30, 2035. These securities carry a floating interest rate, which is reset quarterly, equal to three-month LIBOR plus 1.38%. Northwest Bancorp Statutory Trust IV (Trust IV) issued 50,000 cumulative trust preferred securities in a private transaction to a pooled investment vehicle on December 15, 2006 (liquidation value of $1,000 per preferred security or $50,000,000) with a stated maturity of December 15, 2035. These securities carry a floating interest rate, which is reset quarterly, equal to three-month LIBOR plus 1.38%. The Trusts have invested the proceeds of the offerings in junior subordinated deferrable interest debentures issued by the Company. The structure of these debentures mirrors the structure of the trust-preferred securities. Trust III holds $51,547,000 of the Company s junior subordinated debentures and Trust IV holds $51,547,000 of the Company s junior subordinated debentures. These subordinated debentures are the sole assets of the Trusts. Cash distri-butions on the trust securities are made on a quarterly basis to the extent interest on the debentures is received by the Trusts. We have the right to defer payment of interest on the subordinated debentures at any time, or from time-to-time, for periods not exceeding five years. If interest payments on the subordinated debentures are deferred, the distributions on the trust preferred securities are also deferred. Interest on the subordinated debentures and distributions on the trust securities is cumulative. To date, there have been no interest deferrals. Our obligation constitutes a full, irrevocable, and unconditional guarantee on a subordinated basis of the obligations of the trust under the preferred securities.

We are currently a counterparty to three interest rate swap agreements (swaps), designating the swaps as cash flow hedges. The swaps are intended to protect against the variability of cash flows associated with Trust III and Trust IV. The first swap modifies the re-pricing characteristics of Trust III, wherein for a ten year period expiring in September 2018, the Company receives interest of three-month LIBOR from a counterparty and pays a fixed rate of 4.61% to the same counterparty calculated on a notional amount of $25.0 million. The other two swaps modify the re-pricing characteristics of Trust IV, wherein (i) for a seven year period expiring in September 2015, the Company receives interest of three-month LIBOR from a counterparty and pays a fixed rate of 3.85% to the same counterparty calculated on a notional amount of $25.0 million and (ii) for a ten year period expiring in September 2018, the Company receives interest of three-month LIBOR from a counterparty and pays a fixed rate of 4.09% to the same counterparty calculated on a notional amount of $25.0 million. The swap agreements were entered into with a counterparty that met our credit standards and the agreements contain collateral provisions protecting the at-risk party. We believe that the credit risk inherent in the contracts is not significant. At September 30, 2014, $6.9 million of cash was pledged as collateral to the counterparty.

At September 30, 2014, the fair value of the swap agreements was $(6.5) million and was the amount we would have expected to pay if the contracts were terminated. There was no material hedge ineffectiveness for these swaps.

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The following table shows liability derivatives, included in other liabilities, at September 30, 2014 and December 31, 2013 (in thousands):

		September 30, 2014	December 31, 2013
Fair value	$	6,453	8,037
Notional amount		75,000	75,000
Collateral posted		6,905	8,405

(11) Legal Proceedings

We establish accruals for legal proceedings when information related to the loss contingencies represented by those matters indicates both that a loss is probable and that the amount of loss can be reasonably estimated. As of September 30, 2014 we have accrued $2.4 million. This amount is based on our analysis of currently available information and is subject to significant judgment and a variety of assumptions and uncertainties. Any such accruals are adjusted thereafter as appropriate to reflect changes in circumstances. Due to the inherent subjectivity of assessments and unpredictability of outcomes of legal proceedings, any amounts accrued may not represent the ultimate loss to us from legal proceedings.

Toth v. Northwest Savings Bank

On May 7, 2012, Ashley Toth (Plaintiff) filed a putative class action complaint in the Court of Common Pleas of Allegheny County, Pennsylvania against Northwest Savings Bank (Northwest). Plaintiff s complaint alleged state law claims related to Northwest s order of posting ATM and debit card transactions and the assessment of overdraft fees on deposit customer accounts. Northwest filed preliminary objections to the putative class action complaint on June 29, 2012. On September 6, 2012, Plaintiff filed an amended putative class action complaint containing substantially the same allegations as the initial putative class action complaint. On November 5, 2012, Northwest filed preliminary objections to the amended putative class action complaint. Plaintiff filed her opposition to Northwest s preliminary objections on December 6, 2012, and Northwest filed its reply in support of the preliminary objections on January 3, 2013. On June 25, 2013, the court entered an order, granting in part and overruling in part, Northwest s preliminary objections.

On November 18, 2013, the parties participated in a mediation and reached an agreement in principle, subject to the preparation and execution of a mutually acceptable settlement agreement and release, to fully, finally and completely settle, resolve, discharge and release all claims that have been or could have been asserted in the action on a class-wide basis. The proposed settlement contemplates that, in return for a full and complete release of claims by Plaintiff and the settlement class members, Northwest will create a settlement fund for distribution to the settlement class members after certain court-approved reductions, including for attorney s fees and expenses. The proposed settlement is subject to preliminary and final court approval.

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(12) Changes in Accumulated Other Comprehensive Income

The following table shows the changes in accumulated other comprehensive income by component for the periods indicated (in thousands):

	For the quarter ended September 30, 2014				
		Unrealized gains and (losses) on securities available-for-sale	Change in fair value of interest rate swaps	Change in defined benefit pension plans	Total
Balance as of June 30, 2014	$	3,378	(4,875)	(3,719)	(5,216)
Other comprehensive income before reclassification adjustments		(1,570)	680		(890)
Amounts reclassified from accumulated other comprehensive income (1), (2)		(419)		(138)	(557)
Net other comprehensive income		(1,989)	680	(138)	(1,447)
Balance as of September 30, 2014	$	1,389	(4,195)	(3,857)	(6,663)

	For the quarter ended September 30, 2013				
		Unrealized gains and (losses) on securities available-for-sale	Change in fair value of interest rate swaps	Change in defined benefit pension plans	Total
Balance as of June 30, 2013	$	4,990	(6,099)	(18,478)	(19,587)
Other comprehensive income before reclassification adjustments		110	294		404
Amounts reclassified from accumulated other comprehensive income (3), (4)		(87)		229	142
Net other comprehensive income		23	294	229	546
Balance as of September 30, 2013	$	5,013	(5,805)	(18,249)	(19,041)

(1) Consists of realized gains on securities (gain on sales of investments, net) of $687, net of tax (income tax expense) of $(268).

(2) Consists of amortization of prior service cost (compensation and employee benefits) of $581 and amortization of net loss (compensation and employee benefits) of $(369), net of tax (income tax expense) of $(74). See note 8.

(3) Consists of realized gains on securities (gain on sales of investments, net) of $142, net of tax (income tax expense) of $(55).

(4) Consists of amortization of prior service cost (compensation and employee benefits) of $580 and amortization of net loss (compensation and employee benefits) of $(932), net of tax (income tax expense) of $123. See note 8.

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The following table shows the changes in accumulated other comprehensive income by component for the periods indicated (in thousands):

	For the nine months ended September 30, 2014			
	Unrealized gains and (losses) on securities available-for-sale	Change in fair value of interest rate swaps	Change in defined benefit pension plans	Total
Balance as of December 31, 2013	$ (3,233)	(5,224)	(3,443)	(11,900)
Other comprehensive income before reclassification adjustments	7,149	1,029		8,178
Amounts reclassified from accumulated other comprehensive income (1), (2)	(2,527)		(414)	(2,941)
Net other comprehensive income	4,622	1,029	(414)	5,237
Balance as of September 30, 2014	$ 1,389	(4,195)	(3,857)	(6,663)

	For the nine months ended September 30, 2013			
	Unrealized gains and (losses) on securities available-for-sale	Change in fair value of interest rate swaps	Change in defined benefit pension plans	Total
Balance as of December 31, 2012	$ 15,853	(8,405)	(18,936)	(11,488)
Other comprehensive income before reclassification adjustments	(10,619)	2,600		(8,019)
Amounts reclassified from accumulated other comprehensive income (3), (4)	(221)		687	466
Net other comprehensive income	(10,840)	2,600	687	(7,553)
Balance as of September 30, 2013	$ 5,013	(5,805)	(18,249)	(19,041)

(1) Consists of realized gains on securities (gain on sales of investments, net) of $4,143, net of tax (income tax expense) of $(1,616).

(2) Consists of amortization of prior service cost (compensation and employee benefits) of $1,743 and amortization of net loss (compensation and employee benefits) of $(1,106), net of tax (income tax expense) of $(223). See note 8.

(3) Consists of realized gains on securities (gain on sales of investments, net) of $363, net of tax (income tax expense) of $(142).

(4) Consists of amortization of prior service cost (compensation and employee benefits) of $1,740 and amortization of net loss (compensation and employee benefits) of $(2,796), net of tax (income tax expense) of $369. See note 8.

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

Forward-Looking Statements:

In addition to historical information, this document may contain certain forward-looking statements, as defined in the Private Securities Litigation Reform Act of 1995. These forward-looking statements contained herein are subject to certain risks and uncertainties that could cause actual results to differ materially from those expressed or implied in the forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, as they reflect management s analysis only as of the date of this report. We have no obligation to revise or update these forward-looking statements to reflect events or circumstances that arise after the date of this report.

Important factors that might cause such a difference include, but are not limited to:

- changes in laws, government regulations or policies affecting financial institutions, including regulatory fees and capital requirements;
- general economic conditions, either nationally or in our market areas, that are worse than expected;
- competition among depository and other financial institutions;
- inflation and changes in the interest rate environment that reduce our margins or reduce the fair value of financial instruments;
- adverse changes in the securities markets;
- our ability to enter new markets successfully, capitalize on growth opportunities and our ability to successfully integrate acquired entities, if any;
- changes in consumer spending, borrowing and savings habits;
- our ability to continue to increase and manage our business and personal loans;
- possible impairments of securities held by us, including those issued by government entities and government sponsored enterprises;
- the impact of the economy on our loan portfolio (including cash flow and collateral values), investment portfolio, customers and capital market activities;
- the impact of the current governmental effort to restructure the U.S. financial and regulatory system;
- changes in the financial performance and/or condition of our borrowers; and

- the effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Securities and Exchange Commission, the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standard setters.

Overview of Critical Accounting Policies Involving Estimates

Refer to Note 1 of the Notes to Consolidated Financial Statements in Item 8 of Part II of our 2013 Annual Report on Form 10-K.

Executive Summary and Comparison of Financial Condition

Total assets at September 30, 2014 were $7.827 billion, a decrease of $53.1 million, or 0.7%, from $7.880 billion at December 31, 2013. This decrease in assets was due to decreases in investment securities of $97.0 million and interest-earning deposits in other financial institutions of $84.0 million, which was partially offset by an increase in net loans receivable of $150.5 million. The net decrease in total assets was the result of utilizing excess cash to pay dividends of $1.49 per share during 2014, which includes a special dividend of $0.10 per share paid in the first quarter and a special $1.00 per share dividend declared and paid in the second quarter of this year.

Total loans receivable increased by $150.8 million, or 2.6%, to $5.957 billion at September 30, 2014, from $5.806 billion at December 31, 2013. Loans funded during the nine months ended September 30, 2014, of $1.470 billion exceeded loan maturities and principal repayments of $1.296 billion and mortgage loan sales of $1.0 million. Our business banking loan portfolio increased by $124.6 million, or 6.2%, to $2.136 billion at September 30, 2014 from $2.011 billion at December 31, 2013, as we continue to emphasize the origination and retention of commercial and commercial real estate loans. Our personal banking loan portfolio increased by $26.2 million, or 0.7%, to $3.821 billion at September 30, 2014 from $3.795 billion at December 31, 2013. This increase is primarily attributable to our wholesale lending group which resulted in a $28.3 million increase in the residential mortgage loan portfolio.

Total deposits increased by $38.8 million, or 0.7%, to $5.708 billion at September 30, 2014 from $5.669 billion at December 31, 2013. All deposit account types, with the exception of time deposits, increased during the nine months ended September 30, 2014. Noninterest-bearing demand deposits increased by $95.7 million, or 12.1%, to $884.8 million at September 30, 2014 from $789.1 million at December 31, 2013. Interest-bearing demand deposits increased by $42.5 million, or 5.0%, to $895.3 million at September 30, 2014 from $852.8 million at December 31, 2013. Money market deposit accounts increased by $12.6 million, or 1.1%, to $1.181 billion at September 30, 2014 from $1.168 billion at December 31, 2013. Savings deposits increased by $22.7 million, or 1.9%, to $1.214 billion at September 30, 2014 from $1.192 billion at December 31, 2013. Partially offsetting these increases was a decrease in time deposits of $134.6 million, or 8.1%, to $1.533 billion at September 30, 2014 from $1.667 billion at December 31, 2013. We believe the increase in more liquid deposit accounts is due primarily to customers reluctance to lock in time deposits at these historically low rates. In addition, the marketing campaign which was initiated in March 2014 has been successful in attracting demand deposit customers.

Borrowed funds decreased by $3.2 million, or 0.4%, to $878.4 million at September 30, 2014, from $881.6 million at December 31, 2013. This decrease is the result of a $3.2 million decrease in collateralized borrowings. None of our FHLB advances matured during the quarter and the next scheduled maturity is in February 2015.

Total shareholders equity at September 30, 2014 was $1.077 billion, or $11.33 per share, a decrease of $78.6 million, or 6.8%, from $1.155 billion, or $12.26 per share, at December 31, 2013. This decrease in equity was the result of cash dividend payments during the nine months ended September 30, 2014 of $137.9 million. Partially offsetting this decrease was year-to-date net income of $44.6 million, an increase in paid-in-capital of $8.1 million related to employee incentive stock option exercises and a decrease in accumulated other comprehensive loss of $5.2 million due to an improvement in the unrealized gain position of the investment securities portfolio.

Financial institutions and their holding companies are subject to various regulatory capital requirements administered by state and federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary actions by the regulators that, if undertaken, could have a direct material effect on a company s financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, financial institutions must meet specific capital guidelines that involve quantitative measures of its assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting guidelines. Capital amounts and classifications are also subject to qualitative judgments made by the regulators about components, risk-weighting and other factors.

Quantitative measures, established by regulation to ensure capital adequacy, require financial institutions to maintain minimum amounts and ratios (set forth in the table below) of Total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital to total

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assets (as defined). Capital ratios are presented in the tables below. Dollar amounts in the accompanying tables are in thousands.

	At September 30, 2014					
	Actual		Minimum capital requirements (1)		Well capitalized requirements (1)	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital (to risk weighted assts)						
Northwest Bancshares, Inc.	$ 1,058,562	20.29%				
Northwest Savings Bank	925,044	17.78%	416,275	8.00%	520,344	10.00%
Tier I capital (to risk weighted assets)						
Northwest Bancshares, Inc.	992,963	19.03%				
Northwest Savings Bank	859,904	16.53%	208,138	4.00%	312,206	6.00%
Tier I capital (leverage) (to average assets)						
Northwest Bancshares, Inc.	992,963	12.79%				
Northwest Savings Bank	859,904	11.21%	306,828	4.00%	383,535	5.00%

	At December 31, 2013					
	Actual		Minimum capital requirements (1)		Well capitalized requirements (1)	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital (to risk weighted assts)						
Northwest Bancshares, Inc.	$ 1,145,591	22.44%				
Northwest Savings Bank	945,095	18.58%	406,947	8.00%	508,684	10.00%
Tier I capital (to risk weighted assets)						
Northwest Bancshares, Inc.	1,079,624	21.15%				
Northwest Savings Bank	880,798	17.32%	203,474	4.00%	305,210	6.00%
Tier I capital (leverage) (to average assets)						
Northwest Bancshares, Inc.	1,079,624	13.85%				
Northwest Savings Bank	880,798	11.40%	309,069	4.00%	386,337	5.00%

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(1) The Federal Reserve does not yet have formal capital requirements established for savings and loan holding companies.

In July 2013, the FDIC and the other federal bank regulatory agencies issued a final rule that will revise their leverage and risk-based capital requirements and the method for calculating risk-weighted assets to make them consistent with agreements that were reached by the Basel Committee on Banking Supervision and certain provisions of the Dodd-Frank Act. Among other things, the rule establishes a new common equity Tier 1 minimum capital requirement (4.5% of risk-weighted assets), increases the minimum Tier 1 capital to risk-based assets requirement (from 4% to 6% of risk-weighted assets) and assigns a higher risk weight (150%) to exposures that are more than 90 days past due or are on nonaccrual status and to certain commercial real estate facilities that finance the acquisition, development or construction of real property. The final rule also requires unrealized gains and losses on certain available-for-sale securities holdings to be included for purposes of calculating regulatory capital requirements unless a one-time opt-in or opt-out is exercised. The rule limits a banking organization s capital distributions and certain discretionary bonus payments if the banking organization does not hold a capital conservation buffer consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets in addition to the amount necessary to meet its minimum risk-based capital

requirements.

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The final rule becomes effective for Northwest on January 1, 2015. The capital conservation buffer requirement will be phased in beginning January 1, 2016 and ending January 1, 2019, when the full capital conservation buffer requirement will be effective. The final rule also officially implements these consolidated capital requirements for savings and loan holding companies, such as the Company, effective January 1, 2015.

The following table shows the Basel III regulatory capital levels that must be maintained to avoid limitations on capital distributions and discretionary bonus payments for the periods indicated:

		Basel III Regulatory Capital Requirements				
	Current	**January 1, 2015**	**January 1, 2016**	**January 1, 2017**	**January 1, 2018**	**January 1, 2019**
New common equity tier 1 ratio plus capital conservation buffer		4.50%	5.125%	5.75%	6.375%	7.00%
Tier 1 risk-based capital ratio	4.00%					
Tier 1 risk-based capital ratio plus capital conservation buffer		6.00%	6.625%	7.25%	7.875%	8.50%
Total risk-based capital ratio	8.00%					
Total risk-based capital ratio plus capital conservation buffer		8.00%	8.625%	9.25%	9.875%	10.50%

We are required to maintain a sufficient level of liquid assets, as determined by management and reviewed for adequacy by the FDIC and the Pennsylvania Department of Banking during their regular examinations. Northwest monitors its liquidity position primarily using the ratio of unencumbered available-for-sale liquid assets as a percentage of deposits and borrowings (liquidity ratio). Northwest s liquidity ratio at September 30, 2014 was 9.1%. We adjust liquidity levels in order to meet funding needs for deposit outflows, payment of real estate taxes and insurance on mortgage loan escrow accounts, repayment of borrowings and loan commitments. At September 30, 2014 Northwest had $2.078 billion of additional borrowing capacity available with the FHLB, including $150.0 million on an overnight line of credit, as well as $192.6 million of borrowing capacity available with the Federal Reserve Bank and $80.0 million with two correspondent banks.

We paid $12.1 million and $11.9 million in cash dividends during the quarters ended September 30, 2014 and 2013, respectively, and $137.9 million and $33.9 million for the nine months ended September 30, 2014 and 2013, respectively. As was previously announced, we paid a special dividend of $1.00 per share in the second quarter of 2014. The common stock dividend payout ratio (dividends declared per share divided by net income per share) was 68.4% for both quarters ended September 30, 2014 and 2013, on dividends of $0.13 per share for both quarters. The common stock dividend payout ratio for the nine month periods ended September 30, 2014 and 2013 was 310.4% and 72.5%, respectively, on dividends of $1.49 and $0.37 per share, respectively. On October 14, 2014, the Board of Directors declared a dividend of $0.13 per share payable on November 10, 2014 to shareholders of record as of October 27, 2014. This represents the 80th consecutive quarter we have paid a cash dividend.

Nonperforming Assets

The following table sets forth information with respect to nonperforming assets. Nonaccrual loans are those loans on which the accrual of interest has ceased. Generally, when a loan is 90 days past due, we fully reverse all accrued interest thereon and cease to accrue interest thereafter. Exceptions are made for loans that have contractually matured, are in the process of being modified to extend the maturity date and are otherwise current as to principal and interest, and well secured loans that are in process of collection. Loans may also be placed on

nonaccrual before they reach 90 days past due if conditions exist that call into question our ability to collect all contractual interest. Other nonperforming assets represent property acquired through foreclosure or repossession. Foreclosed property is carried at the lower of its fair value less estimated costs to sell, or the principal balance of the related loan.

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	September 30, 2014	December 31, 2013
	(Dollars in thousands)	
Loans 90 days or more delinquent:		
Residential mortgage loans	$ 20,319	$ 24,625
Home equity loans	6,802	8,344
Other consumer loans	2,098	2,057
Commercial real estate loans	13,552	18,433
Commercial loans	3,162	4,298
Total loans 90 days or delinquent	$ 45,933	$ 57,757
Total real estate owned (REO)	15,007	18,203
Total loans 90 days or more delinquent and REO	60,940	75,960
Total loans 90 days or more delinquent to net loans receivable	0.78%	1.01%
Total loans 90 days or more delinquent and REO to total assets	0.78%	0.96%
Nonperforming assets:		
Nonaccrual loans - loans 90 days or more delinquent	$ 45,933	57,757
Nonaccrual loans - loans less than 90 days delinquent	43,893	49,464
Loans 90 days or more past maturity and still accruing	390	690
Total nonperforming loans	90,216	107,911
Total nonperforming assets	$ 105,223	126,114
Nonaccrual troubled debt restructured loans *	$ 21,871	28,889
Accruing troubled debt restructured loans	39,995	50,277
Total troubled debt restructured loans	$ 61,866	79,166

* Included in nonaccurual loans above.

A loan is considered to be impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement including both contractual principal and interest payments. The amount of impairment is required to be measured using one of three methods: (1) the present value of expected future cash flows discounted at the loan s effective interest rate; (2) the loan s observable market price; or (3) the fair value of collateral if the loan is collateral dependent. If the measure of the impaired loan is less than the recorded investment in the loan, a specific allowance is allocated for the impairment. Impaired loans at September 30, 2014 and December 31, 2013 were $158.6 million and $173.8 million, respectively.

Allowance for Loan Losses

Our Board of Directors has adopted an Allowance for Loan and Lease Losses (ALL) policy designed to provide management with a systematic methodology for determining and documenting the ALL each reporting period. This methodology was developed to provide a consistent process and review procedure to ensure that the ALL is in conformity with GAAP, our policies and procedures and other supervisory and regulatory guidelines.

On an ongoing basis, the Credit Administration department, as well as loan officers, branch managers and department heads, review and monitor the loan portfolio for problem loans. This portfolio monitoring includes a review of the monthly delinquency reports as well as historical comparisons and trend analysis. In addition, a meeting is held every quarter with each region to monitor the performance and status of loans on an internal watch list. On an on-going basis the loan officer in conjunction with a portfolio manager grades or classifies problem loans or potential problem loans based upon their knowledge of the lending relationship and other information previously accumulated. This rating is also reviewed independently by our Loan Review department on a periodic basis. Our loan grading system for

problem loans is consistent with industry regulatory guidelines which classify loans as substandard , doubtful or loss. Loans that do not expose us to risk sufficient to warrant classification in one of the previous categories, but which possess some weaknesses, are designated as special mention . A substandard loan is any loan that is 90 days or more contractually delinquent or is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified as doubtful have all the weaknesses inherent in those classified as substandard with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of currently existing facts, conditions or values, highly questionable and improbable. Loans classified as loss are considered uncollectible so that their continuance as assets without the establishment of a specific loss allowance is not warranted.

Credit relationships that have been classified as substandard or doubtful and are greater than or equal to $1.0 million are reviewed by the Credit Administration department for possible impairment. A loan is considered impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement, including both contractual principal and interest payments.

If an individual loan is deemed to be impaired, the Credit Administration department determines the proper measure of impairment for each loan based on one of three methods: (1) the present value of expected future cash flows discounted at the loan s effective interest rate; (2) the loan s observable market price; or (3) the fair value of the collateral if the loan is collateral dependent, less costs of sale or disposal. If the measurement of the impaired loan is more or less than the recorded investment in the loan, the Credit Administration department adjusts the specific allowance associated with that individual loan accordingly.

If a substandard or doubtful loan is not considered individually for impairment, it is grouped with other loans that possess common characteristics for impairment evaluation and analysis. This segmentation is accomplished by grouping loans of similar product types, risk characteristics and industry concentration into homogeneous pools. Historical loss ratios are analyzed and adjusted based on delinquency trends as well as the current economic, political, regulatory and interest rate environment and used to estimate the current measure of impairment.

The individual impairment measures along with the estimated loss for each homogeneous pool are consolidated into one summary document. This summary schedule along with the support documentation used to establish this schedule is presented to management s Credit Committee on a quarterly basis. The Credit Committee reviews the processes and documentation presented, reviews the concentration of credit by industry and customer, lending products and activity, competition and collateral values, as well as economic conditions in general and in each of our market areas. Based on this review and discussion, the appropriate amount of ALL is estimated and any adjustments to reconcile the actual ALL with this estimate are determined. In addition, the Credit Committee considers if any changes to the methodology are needed. The Credit Committee also reviews and discusses delinquency trends, nonperforming asset amounts and ALL levels and ratios compared to our peer group as well as state and national statistics. Similarly, following the Credit Committee s review and approval, a review is performed by the Risk Management Committee of the Board of Directors on a quarterly basis.

In addition to the reviews by management s Credit Committee and the Board of Directors Risk Management Committee, regulators from either the FDIC or the Pennsylvania Department of Banking perform an extensive review on an annual basis for the adequacy of the ALL and its conformity with regulatory guidelines and pronouncements. Any recommendations or enhancements from these

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independent parties are considered by management and the Credit Committee and implemented accordingly.

We acknowledge that this is a dynamic process and consists of factors, many of which are external and out of our control that can change often, rapidly and substantially. The adequacy of the ALL is based upon estimates using all the information previously discussed as well as current and known circumstances and events. There is no assurance that actual portfolio losses will not be substantially different than those that were estimated.

We utilize a consistent methodology each period when analyzing the adequacy of the allowance for loan losses and the related provision for loan losses. As part of the analysis as of September 30, 2014, we considered the economic conditions in our markets, such as unemployment and bankruptcy levels as well as changes in real estate collateral values. In addition, we considered the overall trends in asset quality, specific reserves already established for criticized loans, historical loss rates and collateral valuations. As a result of this analysis, the allowance for loan losses increased by $302,000, or 0.4%, to $71.7 million, or 1.20% of total loans, at September 30, 2014 from $71.3 million, or 1.23% of total loans, at December 31, 2013. This increase is primarily attributable to several business banking loans requiring additional reserves. Partially offsetting these factors was the continued improvement in overall asset quality as classified loans, TDRs and non-accrual loans delinquent 90 days or more decreased by $27.0 million, $17.3 million and $11.8 million, respectively, compared to December 31, 2013.

We also consider how the level of non-accrual loans and historical charge-offs have influenced the required amount of allowance for loan losses. Nonaccrual loans of $89.8 million or 1.51% of total loans receivable, at September 30, 2014 decreased by $17.4 million, or 16.2%, from $107.2 million, or 1.85% of total loans receivable, at December 31, 2013. As a percentage of average loans, annualized net charge-offs increased to 0.43% for the nine months ended September 30, 2014 compared to 0.36% for the year ended December 31, 2013, as the result of the charge-off of three commercial loans totaling $8.6 million.

Comparison of Operating Results for the Quarters Ended September 30, 2014 and 2013

Net income for the quarter ended September 30, 2014 was $17.3 million, or $0.19 per diluted share, a decrease of $235,000, or 1.3%, from $17.6 million, or $0.19 per diluted share, for the quarter ended September 30, 2013. The decrease in net income resulted from a decrease in net interest income of $565,000, or 0.9%, and an increase in noninterest expense of $3.1 million, or 6.1%. Partially offsetting these factors was an increase in noninterest income of $2.1 million, or 12.9%, and a decrease in the provision for loan losses of $1.5 million, or 30.6%. Annualized, net income for the quarter ended September 30, 2014 represents a 6.43% and 0.87% return on average equity and return on average assets, respectively, compared to 6.18% and 0.88% for the same quarter last year. A discussion of significant changes follows.

Interest Income

Total interest income decreased by $1.6 million, or 2.1%, to $76.1 million for the quarter ended September 30, 2014 due primarily to a decrease in the average yield earned on interest earning assets to 4.17% for the quarter ended September 30, 2014 from 4.22% for the quarter ended September 30, 2013. The average yield on all categories of interest earning assets decreased when compared to the prior year period, with the exception of Federal Home Loan Bank of Pittsburgh stock (FHLB). Additionally, the average balance of interest earning assets decreased by $35.7 million, or 0.5%, to $7.339 billion for the quarter ended September 30, 2014 from $7.374 billion for the quarter ended September 30, 2013.

Interest income on loans receivable decreased by $602,000, or 0.8%, to $70.8 million for the quarter ended September 30, 2014 from to $71.4 million for the quarter ended September 30, 2013. This decrease in interest income on loans receivable can be attributed to a decline in the average yield which

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decreased to 4.75% for the quarter ended September 30, 2014 from 4.97% for the quarter ended September 30, 2013. The continued decline in average yield is due primarily to the historically low level of market interest rates in general and continued competitive pricing pressure for new, as well as existing, credit relationships. Partially offsetting this decrease was an increase in the average balance of loans receivable which increased by $209.4 million, or 3.7%, to $5.913 billion for the quarter ended September 30, 2014 from $5.704 billion for the quarter ended September 30, 2013. This increase is due to continued success in growing business banking relationships and the retention of the residential mortgage loans originated by our wholesale lending function rather than selling a portion of these originations in the secondary market.

Interest income on mortgage-backed securities decreased by $609,000, or 19.6%, to $2.5 million for the quarter ended September 30, 2014 from $3.1 million for the quarter ended September 30, 2013. This decrease is the result of decreases in both the average balance and average yield. The average balance of mortgage-backed securities decreased by $132.0 million, or 18.8%, to $569.5 million for the quarter ended September 30, 2014 from $701.5 for the quarter ended September 30, 2013 due primarily to redirecting cash flows from these securities to fund loan growth and time deposit runoff. The average yield on mortgage-backed securities decreased slightly to 1.76% for the quarter ended September 30, 2014 from 1.78% for the quarter ended September 30, 2013 due primarily to the pay-down of higher rate securities.

Interest income on investment securities decreased by $377,000, or 12.8%, to $2.6 million for the quarter ended September 30, 2014 from $2.9 million for the quarter ended September 30, 2013. This decrease is the result of decreases in both the average balance and average yield. The average balance of investment securities decreased by $56.1 million, or 10.3%, to $488.9 million for the quarter ended September 30, 2014 from $545.0 million for the quarter ended September 30, 2013. This decrease is due primarily to the maturity or call of municipal and government bonds and the use of these proceeds to fund loan growth. The average yield of investment securities decreased to 2.10% for the quarter ended September 30, 2014 from 2.16% for the quarter ended September 30, 2013. This decrease is primarily the result of higher rate, tax-free, municipal securities maturing or being called and when replaced, being replaced by lower yielding, shorter duration government agency securities.

For the quarter ended September 30, 2014 we received dividends on FHLB stock of $452,000 on an average balance of $44.0 million, resulting in a yield of 4.11%, compared to dividends of $120,000 on an average balance of $47.7 million, resulting in a yield of 1.01% for the quarter ended September 30, 2013. As a result of the improved financial condition of the FHLB of Pittsburgh, they have been able to increase their dividends to member financial institutions. These dividends are reported as other operating income on our Consolidated Statements of Income.

Interest income on interest-earning deposits decreased by $66,000, or 26.1%, to $187,000 for the quarter ended September 30, 2014 from $253,000 for the quarter ended September 30, 2013. This decrease is due to a decrease in the average balance which decreased by $53.3 million, or 14.1%, to $323.4 million for the quarter ended September 30, 2014 from $376.7 million for the quarter ended September 30, 2013, due to the utilization of cash to fund loan growth and the payment of dividends over the past year.

Interest Expense

Interest expense decreased by $1.1 million, or 7.1%, to $14.2 million for the quarter ended September 30, 2014 from $15.3 million for the quarter ended September 30, 2013. This decrease in interest expense was due to a decrease in the average cost of interest-bearing liabilities, which decreased to 0.96% for the quarter ended September 30, 2014 from 1.03% for the quarter ended September 30, 2013, as well as a decrease in the average balance of interest-bearing liabilities, which decreased by $64.8 million, or 1.1%, to $5.847 billion for the quarter ended September 30, 2014 from $5.912 billion for the quarter

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ended September 30, 2013. The decrease in the cost of funds resulted primarily from the current level of market interest rates which enabled us to reduce the rate of interest paid on time deposit products. Also contributing to the decrease was the maturity of an interest rate swap used to hedge the interest rate on our junior subordinated debentures. The decrease in average interest-bearing liabilities resulted from a reduction in average time deposits of $182.0 million, or 10.5%, compared to last year, as consumers continue to shift investment priorities to shorter duration or demand products as well as to utilize funds for living expenses. The decrease in time deposits was partially offset by a combined increase in the average balance of interest-bearing demand deposits, savings deposits and money market deposit accounts of $105.5 million, or 3.3%, compared to the average balance for the quarter ended September 30, 2013.

Net Interest Income

Net interest income decreased by $565,000, or 0.9%, to $61.9 million for the quarter ended September 30, 2014 from $62.5 million for the quarter ended September 30, 2013. This decrease is attributable to the factors discussed above. Loan growth enabled us to redirect cash flows from lower yielding assets which helped offset overall lower market interest rates and maintain our net interest spread and margin. Our net interest rate spread increased to 3.21% for the quarter ended September 30, 2014 from 3.19% for the quarter ended September 30, 2013 and our net interest margin increased one basis point to 3.40% for the quarter ended September 30, 2014 from 3.39% for the quarter ended September 30, 2013.

Provision for Loan Losses

The provision for loan losses decreased by $1.5 million, or 30.6%, to $3.5 million for the quarter ended September 30, 2014 from $5.0 million for the quarter ended September 30, 2013. This decrease is due primarily to improvements in overall asset quality as classified loans decreased by $35.6 million, or 14.5%, to $209.8 million at September 30, 2014 from $245.4 million at September 30, 2013. In addition, TDRs decreased by $17.5 million, or 22.1%, to $61.9 million at September 30, 2014 from $79.4 million at September 30, 2013 and loans 90 days or more delinquent decreased by $12.6 million, or 21.5%, to $45.9 million at September 30, 2014 from $58.5 million at September 30, 2013.

In determining the amount of the current period provision, we considered current economic conditions, including unemployment levels and bankruptcy filings, and changes in real estate values and the impact of these factors on the quality of our loan portfolio and historical loss factors. We analyze the allowance for loan losses as described in the section entitled Allowance for Loan Losses. The provision that is recorded is sufficient, in our judgment, to bring this reserve to a level that reflects the losses inherent in our loan portfolio relative to loan mix, economic conditions and historical loss experience.

Noninterest Income

Noninterest income increased by $2.1 million, or 12.9%, to $18.2 million for the quarter ended September 30, 2014 from $16.1 million for the quarter ended September 30, 2013. The increase is primarily attributable to increases in the gain on sale of investments, trust and other financial services income and service charges and fees. Gain on sale of investments increased by $743,000 to $852,000 for the quarter ended September 30, 2014 from $109,000 for the quarter ended September 30, 2013 as a result of the sale of equity securities. Trust and other financial services income increased by $596,000, or 25.0%, to $3.0 million for the quarter ended September 30, 2014 from $2.4 million for the quarter ended September 30, 2013. This increase is due to our acquisition of Evans Capital Management, Inc. as of January 1, 2014 as well as

increases in the amount of assets under management. Service charges and fees increased by $383,000, or 4.1%, to $9.7 million for the quarter ended September 30, 2014 from $9.3 million for the quarter ended September 30, 2013. In addition to growth in the number of transaction deposit customers, we adjusted deposit account fees to better match market competition.

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Noninterest Expense

Noninterest expense increased by $3.1 million, or 6.1%, to $53.4 million for the quarter ended September 30, 2014 from $50.3 million for the quarter ended September 30, 2013. This increase is primarily the result of increases in marketing expenses, processing expenses and professional services. Marketing expenses increased by $1.2 million, or 114.2%, to $2.2 million for the quarter ended September 30, 2014 from $1.0 million for the quarter ended September 30, 2013. This increase is primarily the result of the timing of ongoing loan and deposit account marketing campaigns. Processing expense increased by $687,000, or 11.4%, to $6.7 million for the quarter ended September 30, 2014 from $6.0 million for the quarter ended September 30, 2013 due primarily to software and software amortization expense related to upgrades to programs used to address regulatory compliance requirements. Additionally, professional services increased by $523,000, or 39.3%, to $1.9 million for the quarter ended September 30, 2014 from $1.3 million for the quarter ended September 30, 2013. This increase is due primarily to compliance related consulting engagements as we continue to strengthen and test our compliance management system.

Income Taxes

The provision for income taxes increased by $199,000, or 3.5%, to $5.9 million for the quarter ended September 30, 2014 from $5.7 million for the quarter ended September 30, 2013. This increase in income tax expense is primarily the result of a decrease in tax free income on municipal loans and bonds. Our effective tax rate for the quarter ended September 30, 2014 was 25.5% compared to 24.6% for the quarter ended September 30, 2013. We anticipate our effective tax rate to be between 25.0% and 27.0% for the year.

Comparison of operating results for the nine months ended September 30, 2014 and 2013

Net income for the nine months ended September 30, 2014 was $44.6 million, or $0.48 per diluted share, a decrease of $1.6 million, or 3.4%, from $46.2 million, or $0.51 per diluted share, for the same period last year. The decrease in net income resulted primarily from a decrease in net interest income of $4.7 million as well as an increase in the provision for loan losses of $1.6 million and an increase in noninterest expense of $5.7 million. These changes were partially offset by an increase in noninterest income of $9.1 million and a decrease in income tax expense of $1.5 million. Annualized, net income for the nine months ended September 30, 2014 represents a 5.44% and 0.75% return on average equity and return on average assets, respectively, compared to 5.46% and 0.78% for the same period last year. A discussion of significant changes follows.

Interest Income

Total interest income decreased by $8.5 million, or 3.6%, to $227.4 million for the nine months ended September 30, 2014 from $235.9 million for the nine months ended September 30, 2013, due to both a decrease in the average yield earned on interest earning assets and a decrease in the average balance of interest earning assets. The average yield on interest earning assets decreased to 4.15% for the nine months ended September 30, 2014 from 4.27% for the nine months ended September 30, 2013. The average yield on all categories of interest earning assets decreased compared to the same period last year with the exception of dividends on FHLB stock. Average interest earning assets decreased by $13.6 million to $7.351 billion for the nine months ended September 30, 2014 from $7.365 billion for the nine months ended September 30, 2013. A discussion of significant changes follows.

Interest income on loans receivable decreased by $5.2 million, or 2.4%, to $210.9 million for the nine months ended September 30, 2014 from $216.1 million for the nine months ended September 30, 2013. The average yield on loans receivable decreased to 4.81% for the nine months ended September 30, 2014 from 5.11% for the nine months ended September 30, 2013. The decrease in average yield is primarily attributable to the origination of new loans and rate reductions for existing variable rate loans in this historically low interest rate and highly competitive environment. This decrease was partially offset by an

increase in the average balance of loans receivable of $201.4 million, or 3.6%, to $5.857 billion at September 30, 2014 from $5.656 billion at September 30, 2013. This increase is primarily attributable to our continued emphasis on building business banking loan relationships.

Interest income on mortgage-backed securities decreased by $1.9 million, or 19.3%, to $8.0 million for the nine months ended September 30, 2014 from $9.9 million for the nine months ended September 30, 2013. This decrease is the result of decreases in both the average balance and average yield. The average balance of mortgage-backed securities decreased by $120.7 million, or 16.8%, to $597.0 million for the nine months ended September 30, 2014 from $717.8 for the nine months ended September 30, 2013 due primarily to redirecting cash flows to fund loan growth and time deposit runoff, as well as the payment of cash dividends. The average yield on mortgage-backed securities decreased five basis points to 1.78% for the nine months ended September 30, 2014 from 1.83% for the nine months ended September 30, 2013.

Interest income on investment securities decreased by $1.1 million, or 12.5%, to $7.9 million for the nine months ended September 30, 2014 from $9.0 million for the nine months ended September 30, 2013. This decrease was the result of a decrease in the average yield on investment securities to 2.11% for the nine months ended September 30, 2014 from 2.34% for the nine months ended September 30, 2013, as a result of higher rate municipal bonds maturing or being called and replaced with lower yielding shorter duration government agency bonds. Additionally, the average balance of investment securities decreased by $14.7 million, or 2.8%, to $501.1 million for the nine months ended September 30, 2014 from $515.8 million for the nine months ended September 30, 2013, due to deploying excess cash flow to fund loan growth.

For the nine months ended September 30, 2014 we received dividends on FHLB stock of $1.4 million on an average balance of $43.9 million, resulting in a yield of 4.33%, compared to dividends of $191,000 on an average balance of $47.5 million, resulting in a yield of 0.54% for the nine months ended September 30, 2013. These dividends are reported as other operating income on our Consolidated Statements of Income.

Interest income on interest-earning deposits decreased by $171,000, or 20.3%, to $673,000 for the nine months ended September 30, 2014 from $844,000 for the nine months ended September 30, 2013. This decrease is due to the average balance decreasing by $76.0 million, or 17.7%, to $352.4 million for the nine months ended September 30, 2014 from $428.4 million for the nine months ended September 30, 2013. The average balance decreased due to common stock dividend payments, loan growth and time deposit runoff. The average yield on interest-earning deposits decreased one basis point to 0.25% for the nine months ended September 30, 2014 from 0.26% for the nine months ended September 30, 2013.

Interest Expense

Interest expense decreased by $3.8 million, or 8.1%, to $42.6 million for the nine months ended September 30, 2014 from $46.4 million for the nine months ended September 30, 2013. This decrease in interest expense was due primarily to a decrease in the average cost of interest-bearing liabilities by seven basis points to 0.97% for the nine months ended September 30, 2014 from 1.04% for the nine months ended September 30, 2013. The decrease in the cost of funds was due primarily to a reduction in the rates paid on time deposit products and the maturity of an interest rate swap on our junior subordinated debentures. In addition, the average balance of interest-bearing liabilities decreased by $69.8 million, or 1.2%, to $5.868 billion for the nine months ended September 30, 2014 from $5.937 billion for the nine months ended September 30, 2013. The decrease in interest-bearing liabilities is the result of a decrease in the average balance of time deposits of $192.9 million, or 10.8%, as we believe consumers continue to prefer more liquid deposit accounts as protection against possible higher interest rates in the future.

Partially offsetting this decrease was an increase of $108.0 million, or 3.4%, in all other interest-bearing deposit products.

Net Interest Income

Net interest income decreased by $4.7 million, or 2.5%, to $184.8 million for the nine months ended September 30, 2014 from $189.5 million for the nine months ended September 30, 2013. This decrease in net interest income was attributable to the factors discussed above. Our net interest rate spread decreased to 3.18% for the nine months ended September 30, 2014 from 3.23% for the nine months ended September 30, 2013, and our net interest margin decreased to 3.38% for the nine months ended September 30, 2014 from 3.43% for the nine months ended September 30, 2013.

Provision for Loan Losses

The provision for loan losses increased by $1.6 million, or 9.6%, to $19.2 million for the nine months ended September 30, 2014 from $17.6 million for the nine months ended September 30, 2013. This increase is due to five business banking loans requiring combined provisions of $10.1 million during the 2014 period. Improvements in overall asset quality partially offset these increases. Classified loans decreased by $35.6 million, or 14.5%, to $209.8 million at September 30, 2014 from $245.4 million at September 30, 2013. In addition, total nonaccrual loans decreased by $33.1 million, or 26.9%, to $89.8 million at September 30, 2014 from $122.9 million at September 30, 2013 and loans 90 days or more delinquent decreased by $12.6 million, or 21.5%, to $45.9 million at September 30, 2014 from $58.5 million at September 30, 2013.

In determining the amount of the current period provision, we considered current economic conditions, including unemployment levels and bankruptcy filings, and changes in real estate values and the impact of these factors on the quality of our loan portfolio and historical loss factors. Net charge-offs for the nine months ended September 30, 2014 were $18.9 million compared to $14.9 million for the nine months ended September 30, 2013. Annualized net charge-offs to average loans increased to 0.43% for the nine months ended September 30, 2014 from 0.35% for the nine months ended September 30, 2013. We analyze the allowance for loan losses as described in the section entitled Allowance for Loan Losses. The provision that is recorded is sufficient, in our judgment, to bring this reserve to a level that reflects the losses inherent in our loan portfolio relative to loan mix, economic conditions and historical loss experience.

Noninterest Income

Noninterest income increased by $9.1 million, or 19.8%, to $55.0 million for the nine months ended September 30, 2014 from $45.9 million for the nine months ended September 30, 2013. The increase is primarily attributable to increases in the gain on sale of investments and trust and other financial services income as well as a decrease in loss on real estate owned. Gain on sale of investments increased by $4.3 million to $4.5 million for the nine months ended September 30, 2014 from $229,000 for the nine months ended September 30, 2013, due to the sale of equity securities during the current year. Trust and other financial services income increased by $2.3 million, or 32.6% to $9.1 million for the nine months ended September 30, 2014 from $6.8 million for the nine months ended September 30, 2013. This increase is due to our acquisition of Evans Capital Management, Inc. as of January 1, 2014 as well as increases in the amount of assets under management. Loss on real estate owned decreased by $1.6 million, or 62.9%, to $937,000 for the nine months ended September 30, 2014 from $2.5 million for the nine months ended September 30, 2013, as a result of a write-down of our largest REO property during 2013. Partially offsetting these favorable variances was a decrease in mortgage banking income of $642,000, or 46.0%, to $753,000 for the nine months ended September 30, 2014 from $1.4

million for the nine months ended September 30, 2013. This decrease resulted primarily from fewer sales of residential mortgage loans into the secondary market during the current year compared to the same period last year.

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Noninterest Expense

Noninterest expense increased by $5.7 million, or 3.7%, to $160.3 million for the nine months ended September 30, 2014 from $154.6 million for the nine months ended September 30, 2013. Almost all categories experienced increases over the prior year as explained below. Marketing expenses increased by $1.8 million, or 34.9%, to $6.8 million for the nine months ended September 30, 2014 from $5.0 million for the nine months ended September 30, 2013. This increase is primarily the result of loan and demand deposit marketing campaigns which started during March 2014. Professional services increased by $1.5 million, or 34.8%, to $5.7 million for the nine months ended September 30, 2014 from $4.2 million for the nine months ended September 30, 2013, due primarily to consulting engagements to test and refine our compliance management system. Compensation and employee benefits increased by $847,000, or 1.0%, to $84.6 million for the nine months ended September 30, 2014 from $83.7 million for the nine months ended September 30, 2013. This increase is primarily the result of our acquisition of Evans Capital Management, Inc. Other operating expense increased by $710,000, or 10.1%, to $7.8 million for the nine months ended September 30, 2014 from $7.0 million for the nine months ended September 30, 2013, due primarily to the timing of contributions made to organizations that qualify for Pennsylvania s Educational Improvement Tax Credit program for which we receive state income tax credits. Processing expenses increased by $672,000, or 3.5%, to $20.0 million for the nine months ended September 30, 2014 from $19.3 million for the nine months ended September 30, 2013, due primarily to additional software purchases and the related amortization expense of our Compliance Management Program. Premises and occupancy costs increased by $409,000, or 2.3%, to $17.9 million for the nine months ended September 30, 2014 from $17.5 million for the nine months ended September 30, 2013. This increase is due primarily to elevated snow removal costs in the first quarter of 2014. These increases were partially offset by a decrease in federal deposit insurance premiums of $362,000, or 8.5%, to $3.9 million for the nine months ended September 30, 2014 from $4.2 million for the nine months ended September 30, 2013.

Income Taxes

The provision for income taxes decreased by $1.5 million, or 8.8%, to $15.6 million for the nine months ended September 30, 2014 from $17.1 million for the nine months ended September 30, 2013. This decrease in income tax expense is primarily a result of the decrease in income before income taxes of $3.1 million, or 4.8% and additional Pennsylvania tax credits relating to certain charitable contributions. Our effective tax rate for the nine months ended September 30, 2014 was 25.9% compared to 27.0% for the nine months ended September 30, 2013. We anticipate our effective tax rate to be between 25.0% and 27.0% for the year.

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Average Balance Sheet

(Dollars in thousands)

The following table sets forth certain information relating to the Company s average balance sheet and reflects the average yield on interest-earning assets and average cost of interest-bearing 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 presented. Average balances are calculated using daily averages.

	Quarter ended September 30,					
	2014			2013		
	Average balance	Interest	Avg. yield/ cost (f)	Average balance	Interest	Avg. yield/ cost (f)
Assets:						
Interest-earning assets:						
Loans receivable (a) (b) (includes FTE adjustments of $486 and $571, respectively)	$ 5,912,890	71,306	4.78%	5,703,527	71,993	5.01%
Mortgage-backed securities (c)	569,482	2,504	1.76%	701,510	3,113	1.78%
Investment securities (c) (includes FTE adjustments of $840 and $1,030, respectively)	488,893	3,405	2.79%	545,005	3,972	2.92%
FHLB stock	43,986	452	4.11%	47,650	120	1.01%
Other interest-earning deposits	323,447	187	0.23%	376,699	253	0.26%
Total interest-earning assets (includes FTE adjustments of $1,326 and $1,601, respectively)	7,338,698	77,854	4.24%	7,374,391	79,451	4.31%
Noninterest earning assets (d)	537,065			551,760		
Total assets	$ 7,875,763			7,926,151		
Liabilities and shareholders equity:						
Interest-bearing liabilities:						
Savings deposits	$ 1,228,105	834	0.27%	1,209,726	882	0.29%
Interest-bearing checking deposits	899,231	152	0.07%	854,600	144	0.07%
Money market deposit accounts	1,187,024	802	0.27%	1,144,522	768	0.27%
Time deposits	1,553,867	4,517	1.15%	1,735,898	5,356	1.22%
Borrowed funds (e)	876,034	6,700	3.03%	864,315	6,690	3.07%
Junior subordinated debentures	103,094	1,182	4.49%	103,094	1,436	5.45%
Total interest-bearing liabilities	5,847,355	14,187	0.96%	5,912,155	15,276	1.03%
Noninterest-bearing checking deposits	891,842			794,411		
Noninterest-bearing liabilities	66,432			91,385		
Total liabilities	6,805,629			6,797,951		
Shareholders equity	1,070,134			1,128,200		

Total liabilities and shareholders equity	$ 7,875,763			7,926,151		
Net interest income/ Interest rate spread		63,667	3.28%		64,175	3.28%
Net interest-earning assets/ Net interest margin	$ 1,491,343		3.47%	1,462,236		3.48%
Ratio of interest-earning assets to interest-bearing liabilities	1.26X			1.25X		

(a) Average gross loans includes loans held as available-for-sale and loans placed on nonaccrual status.

(b) Interest income includes accretion/ amortization of deferred loan fees/ expenses, which were not material.

(c) Average balances do not include the effect of unrealized gains or losses on securities held as available-for-sale.

(d) Average balances include the effect of unrealized gains or losses on securities held as available-for-sale.

(e) Average balances include FHLB borrowings and collateralized borrowings.

(f) Annualized. Shown on a fully tax-equivalent basis (FTE). The FTE basis adjusts for the tax benefit of income on certain tax exempt loans and investments using the federal statutory rate of 35% for each period presented. We believe this measure to be the preferred industry measurement of net interest income and provides relevant comparison between taxable and non-taxable amounts. GAAP basis yields were: Loans 4.75% and 4.97%, respectively; Investment securities 2.10% and 2.16%, respectively; interest-earning assets 4.17% and 4.22%, respectively. GAAP basis net interest rate spreads were 3.21% and 3.19%, respectively; and GAAP basis net interest margins were 3.40% and 3.39%, respectively.

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Rate/ Volume Analysis

(Dollars in Thousands)

The following table represents the extent to which changes in interest rates and changes in the volume of interest-earning assets and interest-bearing liabilities have affected interest income and interest expense during the periods indicated. Information is provided in each category with respect to (i) changes attributable to changes in volume (changes in volume multiplied by prior rate), (ii) changes attributable to changes in rate (changes in rate multiplied by prior volume), and (iii) net change. Changes that cannot be attributed to either rate or volume have been allocated to both rate and volume.

Quarters ended September 30, 2014 and 2013

	Rate	Volume	Net Change
Interest earning assets:			
Loans receivable	$ (3,308)	2,621	(687)
Mortgage-backed securities	(28)	(581)	(609)
Investment securities	(158)	(409)	(567)
FHLB stock	369	(37)	332
Other interest-earning deposits	(35)	(31)	(66)
Total interest-earning assets	(3,160)	1,563	(1,597)
Interest-bearing liabilities:			
Savings deposits	(61)	13	(48)
Interest-bearing checking deposits		8	8
Money market deposit accounts	5	29	34
Time deposits	(310)	(529)	(839)
Borrowed funds	(81)	91	10
Junior subordinated debentures	(254)		(254)
Total interest-bearing liabilities	(701)	(388)	(1,089)
Net change in net interest income	$ (2,459)	1,951	(508)

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Average Balance Sheet

(Dollars in thousands)

The following table sets forth certain information relating to the Company s average balance sheet and reflects the average yield on interest-earning assets and average cost of interest-bearing 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 presented. Average balances are calculated using daily averages.

	Nine months ended September 30,					
	2014			2013		
	Average balance	Interest	Avg. yield/ cost (f)	Average balance	Interest	Avg. yield/ cost (f)
Assets:						
Interest-earning assets:						
Loans receivable (a) (b) (includes FTE adjustments of $1,569 and $1,686, respectively)	$ 5,856,940	212,437	4.85%	$ 5,655,512	217,799	5.15%
Mortgage-backed securities (c)	597,042	7,963	1.78%	717,785	9,862	1.83%
Investment securities (c) (includes FTE adjustments of $2,592 and $3,269, respectively)	501,120	10,504	2.79%	515,751	12,307	3.18%
FHLB stock	43,882	1,425	4.33%	47,545	191	0.54%
Other interest-earning deposits	352,370	673	0.25%	428,395	844	0.26%
Total interest-earning assets (includes FTE adjustments of $4,161 and $4,955, respectively)	7,351,354	233,002	4.23%	7,364,988	241,003	4.36%
Noninterest earning assets (d)	563,902			574,423		
Total assets	$ 7,915,256			7,939,411		
Liabilities and shareholders equity:						
Interest-bearing liabilities:						
Savings deposits	$ 1,225,411	2,459	0.27%	$ 1,200,106	2,676	0.30%
Interest-bearing checking deposits	882,465	440	0.07%	856,269	433	0.07%
Money market deposit accounts	1,181,056	2,376	0.27%	1,124,572	2,258	0.27%
Time deposits	1,598,870	13,941	1.17%	1,791,819	17,001	1.27%
Borrowed funds (e)	876,606	19,880	3.03%	861,465	19,728	3.06%
Junior subordinated debentures	103,094	3,509	4.49%	103,094	4,261	5.45%
Total interest-bearing liabilities	5,867,502	42,605	0.97%	5,937,325	46,357	1.04%
Noninterest-bearing checking deposits	853,294			776,087		
Noninterest-bearing liabilities	98,877			94,651		
Total liabilities	6,819,673			6,808,063		
Shareholders equity	1,095,583			1,131,348		

Total liabilities and shareholders equity	$ 7,915,256			7,939,411		
Net interest income/ Interest rate spread		190,397	3.26%		194,646	3.32%
Net interest-earning assets/ Net interest margin	$ 1,483,852		3.45%	1,427,663		3.52%
Ratio of interest-earning assets to interest-bearing liabilities	1.25X			1.24X		

(a) Average gross loans includes loans held as available-for-sale and loans placed on nonaccrual status.

(b) Interest income includes accretion/ amortization of deferred loan fees/ expenses, which were not material.

(c) Average balances do not include the effect of unrealized gains or losses on securities held as available-for-sale.

(d) Average balances include the effect of unrealized gains or losses on securities held as available-for-sale.

(e) Average balances include FHLB borrowings and collateralized borrowings.

(f) Annualized. Shown on a fully tax-equivalent basis (FTE). The FTE basis adjusts for the tax benefit of income on certain tax exempt loans and investments using the federal statutory rate of 35% for each period presented. We believe this measure to be the preferred industry measurement of net interest income and provides relevant comparison between taxable and non-taxable amounts. GAAP basis yields were: Loans 4.81% and 5.11%, respectively; Investment securities 2.11% and 2.34%, respectively; interest-earning assets 4.15% and 4.27%, respectively. GAAP basis net interest rate spreads were 3.18% and 3.23%, respectively; and GAAP basis net interest margins were 3.38% and 3.43%, respectively.

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Rate/ Volume Analysis

(Dollars in Thousands)

The following table represents the extent to which changes in interest rates and changes in the volume of interest-earning assets and interest-bearing liabilities have affected interest income and interest expense during the periods indicated. Information is provided in each category with respect to (i) changes attributable to changes in volume (changes in volume multiplied by prior rate), (ii) changes attributable to changes in rate (changes in rate multiplied by prior volume), and (iii) net change. Changes that cannot be attributed to either rate or volume have been allocated to both rate and volume.

Nine months ended September 30, 2014 and 2013

	Rate	Volume	Net Change
Interest earning assets:			
Loans receivable	$ (13,140)	7,778	(5,362)
Mortgage-backed securities	(240)	(1,659)	(1,899)
Investment securities	(1,454)	(349)	(1,803)
FHLB stock	1,353	(119)	1,234
Other interest-earning deposits	(21)	(150)	(171)
Total interest-earning assets	(13,502)	5,501	(8,001)
Interest-bearing liabilities:			
Savings deposits	(268)	51	(217)
Interest-bearing checking deposits	(6)	13	7
Money market deposit accounts	4	114	118
Time deposits	(1,377)	(1,683)	(3,060)
Borrowed funds	(194)	346	152
Junior subordinated debentures	(752)		(752)
Total interest-bearing liabilities	(2,593)	(1,159)	(3,752)
Net change in net interest income	$ (10,909)	6,660	(4,249)

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As the holding company for a savings bank, one of our primary market risks is interest rate risk. Interest rate risk is the sensitivity of net interest income to variations in interest rates over a specified time period. The sensitivity results from differences in the time periods in which interest rate sensitive assets and liabilities mature or re-price. We attempt to control interest rate risk by matching, within acceptable limits, the re-pricing periods of assets and liabilities. We have attempted to limit our exposure to interest sensitivity by increasing core deposits, enticing customers to extend certificates of deposit maturities, borrowing funds with fixed-rates and longer maturities and by shortening the maturities of our assets by emphasizing the origination of more short-term fixed rate loans and adjustable rate loans. We also continue to sell a portion of the long-term, fixed-rate mortgage loans that we originate. In addition, we purchase shorter term or adjustable-rate investment securities and mortgage-backed securities.

We have an Asset/ Liability Committee consisting of several members of management which meets monthly to review market interest rates, economic conditions, the pricing of interest-earning assets and

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interest-bearing liabilities and the balance sheet structure. On a quarterly basis, this Committee also reviews the interest rate risk position and cash flow projections.

The Board of Directors has a Risk Management Committee which meets quarterly and reviews interest rate risk and trends, our interest sensitivity position, the liquidity position and the market risk inherent in the investment portfolio.

In an effort to assess interest rate risk and market risk, we utilize a simulation model to determine the effect of immediate incremental increases and decreases in interest rates on net income and the market value of equity. Certain assumptions are made regarding loan prepayments and decay rates of savings and interest-bearing demand accounts. Because it is difficult to accurately project the market reaction of depositors and borrowers, the effect of actual changes in interest rates on these assumptions may differ from simulated results. We have established the following guidelines for assessing interest rate risk:

Net income simulation. Given a non-parallel shift of 100 basis points (bps), 200 bps and 300 bps in interest rates, the estimated net income may not decrease by more than 10%, 20% and 30%, respectively, within a one-year period.

Market value of equity simulation. The market value of equity is the present value of assets and liabilities. Given a non-parallel shift of 100 bps, 200 bps and 300 bps in interest rates, the market value of equity may not decrease by more than 15%, 30% and 35%, respectively, from the computed economic value at current interest rate levels.

The following table illustrates the simulated impact of a 100 bps, 200 bps or 300 bps upward or a 100 bps downward movement in interest rates on net income, return on average equity, earnings per share and market value of equity. This analysis was prepared assuming that interest-earning asset and interest-bearing liability levels at September 30, 2014 remain constant. The impact of the rate movements was computed by simulating the effect of an immediate and sustained shift in interest rates over a twelve-month period from September 30, 2014 levels.

		Increase		Decrease
Non-parallel shift in interest rates over the next 12 months	**100 bps**	**200 bps**	**300 bps**	**100 bps**
Projected percentage increase/ (decrease) in net income	(3.0)%	(3.3)%	(4.5)%	(13.9)%
Projected increase/ (decrease) in return on average equity	(2.9)%	(3.3)%	(4.4)%	(13.6)%
Projected increase/ (decrease) in earnings per share	$ (0.02)	$ (0.02)	$ (0.02)	$ (0.08)
Projected percentage increase/ (decrease) in market value of equity	(3.3)%	(11.2)%	(17.6)%	(0.6)%

The figures included in the table above represent projections that were computed based upon certain assumptions including prepayment rates and decay rates. These assumptions are inherently uncertain and, as a result, cannot precisely predict the impact of changes in interest rates. Actual results may differ significantly due to timing, magnitude and frequency of interest rate changes and changes in market conditions.

ITEM 4. CONTROLS AND PROCEDURES

Under the supervision of and with the participation of management, including the Principal Executive Officer and Principal Financial Officer, we evaluated the effectiveness of the design and operation of its disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) as of the

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end of the period covered by this quarterly report (the Evaluation Date). Based upon that evaluation, the Principal Executive Officer and Principal Financial Officer concluded that, as of the Evaluation Date, these disclosure controls and procedures were effective.

There were no changes in the internal controls over financial reporting during the period covered by this report or in other factors that have materially affected, or are reasonably likely to materially affect the internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are subject to a number of asserted and unasserted claims encountered in the normal course of business. We believe that any additional liability, other than that which has already been accrued, that may result from such potential litigation will not have a material adverse effect on the financial statements. However, we cannot presently determine whether or not any claims against us will have a material adverse effect on our results of operations in any future reporting period. See note 11.

Item 1A. Risk Factors

There are no material changes to the risk factors as previously discussed in Item 1A, to Part I of our 2013 Annual Report on Form 10-K.

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

a.) Not applicable.

b.) Not applicable.

c.) The following table discloses information regarding the repurchase of shares of common stock during the quarter ending September 30, 2014:

Month	Number of shares purchased	Average price paid per share	Total number of shares purchased as part of a publicly announced repurchase plan (1)	Maximum number of shares yet to be purchased under the plan (1)
July		$		1,049,189
August				1,049,189
September				1,049,189
		$		

Month	Number of shares purchased	Average price paid per share	Total number of shares purchased as part of a publicly announced repurchase plan (2)	Maximum number of shares yet to be purchased under the plan (2)
July		$		5,000,000
August				5,000,000
September				5,000,000
		$		

(1) Reflects the program for 4,750,000 shares announced September 26, 2011. This program does not have an expiration date.

(2) Reflects the program for 5,000,000 shares announced December 13, 2012. This program does not have an expiration date.

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Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits

31.1 Certification of the Chief Executive Officer pursuant to Rule 13a-15 or 15d-15 of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of the Chief Financial Officer pursuant to Rule 13a-15 or 15d-15 of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of the Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101.INS XBRL Instance Document
101.SCH XBRL Taxonomy Extension Schema Document
101.CAL XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF XBRL Taxonomy Extension Definition Linkbase Document
101.LAB XBRL Taxonomy Extension Label Linkbase
101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

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Signature

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

		NORTHWEST BANCSHARES, INC. *(Registrant)*	
Date:	November 7, 2014	By:	/s/ William J. Wagner William J. Wagner President and Chief Executive Officer *(Duly Authorized Officer)*
Date:	November 7, 2014	By:	/s/ Gerald J. Ritzert Gerald J. Ritzert Controller *(Principal Accounting Officer)*