

COMMERCE BANCSHARES INC /MO/  
Form 10-Q  
August 06, 2018  
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q  
(Mark One)

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

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For the quarterly period ended June 30, 2018

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

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For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission File No. 0-2989  
COMMERCE BANCSHARES, INC.  
(Exact name of registrant as specified  
in its charter)

Missouri 43-0889454  
(State of Incorporation) (IRS Employer Identification No.)

1000 Walnut, 64106  
Kansas City, MO  
(Address of principal executive offices) (Zip Code)

(816) 234-2000  
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

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

Large accelerated	Accelerated	Non-accelerated	Smaller reporting	Emerging growth
filer <input checked="" type="checkbox"/>	filer <input type="checkbox"/>	filer <input type="checkbox"/>	company <input type="checkbox"/>	company <input type="checkbox"/>

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

As of August 1, 2018, the registrant had outstanding 106,616,850 shares of its \$5 par value common stock, registrant's only class of common stock.

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Commerce Bancshares, Inc. and Subsidiaries

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## PART I: FINANCIAL INFORMATION

## Item 1. FINANCIAL STATEMENTS

Commerce Bancshares, Inc. and Subsidiaries  
CONSOLIDATED BALANCE SHEETS

	June 30, 2018	December 31, 2017
	(Unaudited)	
	(In thousands)	
<b>ASSETS</b>		
Loans	\$ 13,954,111	\$ 13,983,674
Allowance for loan losses	(159,532 )	(159,532 )
Net loans	13,794,579	13,824,142
Loans held for sale (including \$10,750,000 and \$15,327,000 of residential mortgage loans carried at fair value at June 30, 2018 and December 31, 2017, respectively)	20,352	21,398
Investment securities:		
Available for sale debt (\$557,698,000 and \$662,515,000 pledged at June 30, 2018 and December 31, 2017, respectively, to secure swap and repurchase agreements)	8,412,376	8,725,442
Trading debt	31,156	18,269
Equity	4,444	50,591
Other	112,309	99,005
Total investment securities	8,560,285	8,893,307
Federal funds sold and short-term securities purchased under agreements to resell	31,500	42,775
Long-term securities purchased under agreements to resell	700,000	700,000
Interest earning deposits with banks	114,947	30,631
Cash and due from banks	386,339	438,439
Land, buildings and equipment, net	331,782	335,110
Goodwill	138,921	138,921
Other intangible assets, net	8,083	7,618
Other assets	437,954	401,074
Total assets	\$24,524,742	\$24,833,415
<b>LIABILITIES AND EQUITY</b>		
Deposits:		
Non-interest bearing	\$6,876,756	\$7,158,962
Savings, interest checking and money market	11,761,832	11,499,620
Time open and C.D.'s of less than \$100,000	603,629	634,646
Time open and C.D.'s of \$100,000 and over	1,079,340	1,132,218
Total deposits	20,321,557	20,425,446
Federal funds purchased and securities sold under agreements to repurchase	1,166,759	1,507,138
Other borrowings	9,291	1,758
Other liabilities	255,752	180,889
Total liabilities	21,753,359	22,115,231
Commerce Bancshares, Inc. stockholders' equity:		
Preferred stock, \$1 par value		
Authorized 2,000,000 shares; issued 6,000 shares	144,784	144,784
Common stock, \$5 par value		
Authorized 120,000,000 shares;		
issued 107,081,397 shares	535,407	535,407

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Capital surplus	1,804,057	1,815,360
Retained earnings	408,374	221,374
Treasury stock of 275,577 shares at June 30, 2018 and 276,968 shares at December 31, 2017, at cost	(15,854 )	(14,473 )
Accumulated other comprehensive income (loss)	(108,781 )	14,108
Total Commerce Bancshares, Inc. stockholders' equity	2,767,987	2,716,560
Non-controlling interest	3,396	1,624
Total equity	2,771,383	2,718,184
Total liabilities and equity	\$24,524,742	\$24,833,415

See accompanying notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF INCOME

	For the Three Months Ended June 30		For the Six Months Ended June 30	
	2018	2017	2018	2017
(In thousands, except per share data)				
	(Unaudited)			
<b>INTEREST INCOME</b>				
Interest and fees on loans	\$ 154,135	\$ 134,273	\$ 301,150	\$ 262,596
Interest and fees on loans held for sale	372	263	676	459
Interest on investment securities	65,564	54,975	118,806	110,240
Interest on federal funds sold and short-term securities purchased under agreements to resell	177	37	357	60
Interest on long-term securities purchased under agreements to resell	3,785	3,684	7,899	7,477
Interest on deposits with banks	1,590	362	2,730	759
Total interest income	225,623	193,594	431,618	381,591
<b>INTEREST EXPENSE</b>				
Interest on deposits:				
Savings, interest checking and money market	6,519	4,342	12,108	8,232
Time open and C.D.'s of less than \$100,000	694	674	1,356	1,318
Time open and C.D.'s of \$100,000 and over	3,483	2,822	6,322	5,585
Interest on federal funds purchased and securities sold under agreements to repurchase	3,956	2,038	7,957	3,577
Interest on other borrowings	12	911	24	1,799
Total interest expense	14,664	10,787	27,767	20,511
Net interest income	210,959	182,807	403,851	361,080
Provision for loan losses	10,043	10,758	20,439	21,886
Net interest income after provision for loan losses	200,916	172,049	383,412	339,194
<b>NON-INTEREST INCOME</b>				
Bank card transaction fees	43,215	37,295	84,668	73,046
Trust fees	37,036	33,120	73,098	65,134
Deposit account charges and other fees	23,893	22,861	46,875	44,803
Capital market fees	1,992	2,156	4,283	4,498
Consumer brokerage services	3,971	3,726	7,739	7,375
Loan fees and sales	3,229	4,091	6,091	7,259
Other	11,514	12,131	21,786	22,878
Total non-interest income	124,850	115,380	244,540	224,993
<b>INVESTMENT SECURITIES GAINS (LOSSES), NET</b>	(3,075)	)1,651	2,335	879
<b>NON-INTEREST EXPENSE</b>				
Salaries and employee benefits	115,589	108,829	231,483	221,198
Net occupancy	11,118	11,430	22,702	22,873
Equipment	4,594	4,776	9,025	9,385
Supplies and communication	5,126	5,446	10,439	11,155
Data processing and software	21,016	20,035	41,706	39,940
Marketing	5,142	4,488	9,947	7,712
Deposit insurance	3,126	3,592	6,583	7,063
Community service	656	2,916	1,385	5,860
Other	15,493	15,378	30,867	31,081
Total non-interest expense	181,860	176,890	364,137	356,267

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Income before income taxes	140,831	112,190	266,150	208,799
Less income taxes	29,507	33,201	52,765	58,108
Net income	111,324	78,989	213,385	150,691
Less non-controlling interest expense	994	29	2,071	227
Net income attributable to Commerce Bancshares, Inc.	110,330	78,960	211,314	150,464
Less preferred stock dividends	2,250	2,250	4,500	4,500
Net income available to common shareholders	\$108,080	\$76,710	\$206,814	\$145,964
Net income per common share — basic	\$1.02	\$.71	\$1.94	\$1.36
Net income per common share — diluted	\$1.01	\$.71	\$1.93	\$1.36

See accompanying notes to consolidated financial statements.

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Commerce Bancshares, Inc. and Subsidiaries

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)	For the Three Months Ended June 30		For the Six Months Ended June 30	
	2018	2017	2018	2017
	(Unaudited)			
Net income	\$ 111,324	\$ 78,989	\$ 213,385	\$ 150,691
Other comprehensive income (loss):				
Net unrealized gains (losses) on securities for which a portion of an other-than-temporary impairment has been recorded in earnings	(123	)76	(78	)171
Net unrealized gains (losses) on other securities	(19,489	)11,241	(93,210	)30,243
Pension loss amortization	394	341	787	681
Other comprehensive income (loss)	(19,218	)11,658	(92,501	)31,095
Comprehensive income	92,106	90,647	120,884	181,786
Less non-controlling interest expense	994	29	2,071	227
Comprehensive income attributable to Commerce Bancshares, Inc.	\$91,112	\$90,618	\$118,813	\$181,559
See accompanying notes to consolidated financial statements.				



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Commerce Bancshares, Inc. and Subsidiaries

## CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

Commerce Bancshares, Inc. Shareholders

(In thousands, except per share data)	Preferred Stock	Common Stock	Capital Surplus	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Non-Controlling Interest	Total
	(Unaudited)							
Balance December 31, 2017	\$ 144,784	\$ 535,407	\$ 1,815,360	\$ 221,374	\$ (14,473)	\$ 14,108	\$ 1,624	\$ 2,718,184
Adoption of ASU 2018-02				(2,932 )		2,932		—
Adoption of ASU 2016-01				33,320		(33,320 )		—
Net income				211,314			2,071	213,385
Other comprehensive income (loss)						(92,501 )		(92,501 )
Distributions to non-controlling interest							(299 )	(299 )
Purchases of treasury stock					(19,069 )			(19,069 )
Issuance of stock under purchase and equity compensation plans			(17,697 )		17,688			(9 )
Stock-based compensation			6,394					6,394
Cash dividends on common stock (\$.470 per share)				(50,202 )				(50,202 )
Cash dividends on preferred stock (\$.750 per depository share)				(4,500 )				(4,500 )
Balance June 30, 2018	\$ 144,784	\$ 535,407	\$ 1,804,057	\$ 408,374	\$ (15,854)	\$ (108,781 )	\$ 3,396	\$ 2,771,383
Balance December 31, 2016	\$ 144,784	\$ 510,015	\$ 1,552,454	\$ 292,849	\$ (15,294)	\$ 10,975	\$ 5,349	\$ 2,501,132
Adoption of ASU 2016-09			3,441	(2,144 )				1,297
Net income				150,464			227	150,691
Other comprehensive income						31,095		31,095
Distributions to non-controlling interest							(1,252 )	(1,252 )
Purchases of treasury stock					(10,628 )			(10,628 )
Issuance of stock under purchase and equity compensation plans			(15,556 )		15,549			(7 )
			6,195					6,195

Stock-based compensation								
Cash dividends on common stock (\$.429 per share)				(45,816 )				(45,816 )
Cash dividends on preferred stock (\$.750 per depositary share)				(4,500 )				(4,500 )
Balance June 30, 2017	\$ 144,784	\$510,015	\$1,546,534	\$390,853	\$(10,373)	\$ 42,070	\$ 4,324	\$2,628,207
See accompanying notes to consolidated financial statements.								

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CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)	For the Six Months Ended June 30	
	2018	2017
	(Unaudited)	
<b>OPERATING ACTIVITIES:</b>		
Net income	\$213,385	\$150,691
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	20,439	21,886
Provision for depreciation and amortization	19,180	19,890
Amortization of investment security premiums, net	11,679	17,827
Investment securities gains, net (A)	(2,335 )	(879 )
Net gains on sales of loans held for sale	(2,671 )	(3,547 )
Originations of loans held for sale	(89,183 )	(96,943 )
Proceeds from sales of loans held for sale	91,671	92,423
Net (increase) decrease in trading debt securities	(23,843 )	6,097
Stock-based compensation	6,394	6,195
Increase in interest receivable	(1,717 )	(428 )
Decrease in interest payable	(601 )	(692 )
Increase in income taxes payable	25,721	1,483
Other changes, net	19,958	(6,939 )
Net cash provided by operating activities	288,077	207,064
<b>INVESTING ACTIVITIES:</b>		
Proceeds from sales of investment securities (A)	192,522	6,552
Proceeds from maturities/pay downs of investment securities (A)	812,970	910,411
Purchases of investment securities (A)	(748,707 )	(625,931 )
Net (increase) decrease in loans	7,978	(234,405 )
Repayments of long-term securities purchased under agreements to resell	—	100,000
Purchases of land, buildings and equipment	(13,525 )	(14,117 )
Sales of land, buildings and equipment	1,667	2,527
Net cash provided by investing activities	252,905	145,037
<b>FINANCING ACTIVITIES:</b>		
Net increase (decrease) in non-interest bearing, savings, interest checking and money market deposits	(27,222 )	77,562
Net decrease in time open and C.D.'s	(83,895 )	(157,367 )
Net decrease in federal funds purchased and securities sold under agreements to repurchase	(340,379 )	(467,461 )
Repayment of long-term borrowings	(149 )	(146 )
Net increase in short-term borrowings	7,682	—
Purchases of treasury stock	(19,069 )	(10,628 )
Issuance of stock under equity compensation plans	(9 )	(7 )
Cash dividends paid on common stock	(50,202 )	(45,816 )
Cash dividends paid on preferred stock	(4,500 )	(4,500 )
Net cash used in financing activities	(517,743 )	(608,363 )
Increase (decrease) in cash, cash equivalents and restricted cash	23,239	(256,262 )
Cash, cash equivalents and restricted cash at beginning of year	524,352	801,641
Cash, cash equivalents and restricted cash at June 30	\$547,591	\$545,379
(A) Available for sale debt securities, equity securities and other securities		
Income tax payments, net	\$24,969	\$54,621

Interest paid on deposits and borrowings	\$28,368	\$21,203
Loans transferred to foreclosed real estate	\$1,044	\$461
See accompanying notes to consolidated financial statements.		

Restricted cash is comprised of cash collateral posted by the Company to secure interest rate swap agreements. This balance is included in other assets in the consolidated balance sheets and totaled \$14.8 million and \$14.3 million at June 30, 2018 and 2017, respectively.

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Commerce Bancshares, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2018 (Unaudited)

1. Principles of Consolidation and Presentation

The accompanying consolidated financial statements include the accounts of Commerce Bancshares, Inc. and all majority-owned subsidiaries (the Company). Most of the Company's operations are conducted by its subsidiary bank, Commerce Bank (the Bank). The consolidated financial statements in this report have not been audited by an independent registered public accounting firm, but in the opinion of management, all adjustments necessary to present fairly the financial position and the results of operations for the interim periods have been made. All such adjustments are of a normal recurring nature. All significant intercompany accounts and transactions have been eliminated. Certain reclassifications were made to 2017 data to conform to current year presentation. In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and revenues and expenses for the period. Actual results could differ significantly from those estimates. Management has evaluated subsequent events for potential recognition or disclosure. The results of operations for the three and six month periods ended June 30, 2018 are not necessarily indicative of results to be attained for the full year or any other interim period.

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial information and with the instructions to Form 10-Q adopted by the Securities and Exchange Commission. Accordingly, the financial statements do not include all of the information and footnotes required by GAAP for complete financial statements and should be read in conjunction with the Company's most recent Annual Report on Form 10-K, containing the latest audited consolidated financial statements and notes thereto.

These financial statements reflect the adoption of several FASB Accounting Standards Updates (ASUs) on January 1, 2018. In some cases, the adoption of these ASUs resulted in changes to former accounting policies as described in Note 1 to the financial statements in the 2017 Annual Report on Form 10-K. The ASUs which affected the Company's 2018 financial statements include:

• ASU 2014-09, Revenue from Contracts with Customers, which is discussed further in Note 13.

• ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, which is discussed further in Note 3 - Investment Securities, Note 8 - Accumulated Other Comprehensive Income, and Note 15 - Fair Value of Financial Instruments.

• ASU 2016-18, Restricted Cash, which requires that the beginning and end of period amounts shown on the statement of cash flows include not only cash and cash equivalents, but also restricted cash and restricted cash equivalents, as considered such by the reporting entity.

• ASU 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost, which is discussed further in Note 6 - Pension.

• ASU 2018-02, Reclassification for Certain Tax Effects from Accumulated Other Comprehensive Income, which is discussed further in Note 8 - Accumulated Other Comprehensive Income.



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## 2. Loans and Allowance for Loan Losses

Major classifications within the Company's held for investment loan portfolio at June 30, 2018 and December 31, 2017 are as follows:

(In thousands)	June 30, 2018	December 31, 2017
Commercial:		
Business	\$4,990,298	\$4,958,554
Real estate – construction and land	967,151	968,820
Real estate – business	2,727,580	2,697,452
Personal Banking:		
Real estate – personal	2,102,586	2,062,787
Consumer	2,012,644	2,104,487
Revolving home equity	374,557	400,587
Consumer credit card	775,214	783,864
Overdrafts	4,081	7,123
Total loans	\$13,954,111	\$13,983,674

At June 30, 2018, loans of \$3.7 billion were pledged at the Federal Home Loan Bank as collateral for borrowings and letters of credit obtained to secure public deposits. Additional loans of \$1.7 billion were pledged at the Federal Reserve Bank as collateral for discount window borrowings.

## Allowance for loan losses

A summary of the activity in the allowance for loan losses during the three and six months ended June 30, 2018 and 2017, respectively, follows:

(In thousands)	For the Three Months Ended June 30			For the Six Months Ended June 30		
	Commercial	Personal Banking	Total	Commercial	Personal Banking	Total
Balance at beginning of period	\$93,065	\$66,467	\$159,532	\$93,704	\$65,828	\$159,532
Provision	485	9,558	10,043	(409)	20,848	20,439
Deductions:						
Loans charged off	362	13,323	13,685	728	26,688	27,416
Less recoveries on loans	663	2,979	3,642	1,284	5,693	6,977
Net loan charge-offs (recoveries)	(301)	10,344	10,043	(556)	20,995	20,439
Balance June 30, 2018	\$93,851	\$65,681	\$159,532	\$93,851	\$65,681	\$159,532
Balance at beginning of period	\$92,951	\$64,881	\$157,832	\$91,361	\$64,571	\$155,932
Provision	(111)	10,869	10,758	1,002	20,884	21,886
Deductions:						
	531	13,415	13,946	1,077	25,745	26,822

Loans charged off						
Less recoveries on loans	430	2,758	3,188	1,453	5,383	6,836
Net loan charge-offs (recoveries)	101	10,657	10,758	(376	)20,362	19,986
Balance June 30, 2017	\$92,739	\$65,093	\$157,832	\$92,739	\$65,093	\$157,832



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The following table shows the balance in the allowance for loan losses and the related loan balance at June 30, 2018 and December 31, 2017, disaggregated on the basis of impairment methodology. Impaired loans evaluated under Accounting Standards Codification (ASC) 310-10-35 include loans on non-accrual status, which are individually evaluated for impairment, and other impaired loans discussed below, which are deemed to have similar risk characteristics and are collectively evaluated. All other loans are collectively evaluated for impairment under ASC 450-20.

(In thousands)	Impaired Loans		All Other Loans	
	Allowance for Loan Losses	Loans Outstanding	Allowance for Loan Losses	Loans Outstanding
June 30, 2018				
Commercial	\$2,631	\$ 90,724	\$91,220	\$8,594,305
Personal Banking	919	18,172	64,762	5,250,910
Total	\$3,550	\$ 108,896	\$ 155,982	\$13,845,215
December 31, 2017				
Commercial	\$3,067	\$ 92,613	\$90,637	\$8,532,213
Personal Banking	1,176	22,182	64,652	5,336,666
Total	\$4,243	\$ 114,795	\$ 155,289	\$13,868,879

## Impaired loans

The table below shows the Company's investment in impaired loans at June 30, 2018 and December 31, 2017. These loans consist of all loans on non-accrual status and other restructured loans whose terms have been modified and classified as troubled debt restructurings. These restructured loans are performing in accordance with their modified terms, and because the Company believes it probable that all amounts due under the modified terms of the agreements will be collected, interest on these loans is being recognized on an accrual basis. They are discussed further in the "Troubled debt restructurings" section on page 15.

(In thousands)	June 30, 2018	Dec. 31, 2017
Non-accrual loans	\$9,472	\$11,983
Restructured loans (accruing)	99,424	102,812
Total impaired loans	\$108,896	\$114,795

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The following table provides additional information about impaired loans held by the Company at June 30, 2018 and December 31, 2017, segregated between loans for which an allowance for credit losses has been provided and loans for which no allowance has been provided.

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance
June 30, 2018			
With no related allowance recorded:			
Business	\$ 4,946	\$ 8,936	\$ —
Real estate – business	1,210	1,300	—
	\$ 6,156	\$ 10,236	\$ —
With an allowance recorded:			
Business	\$ 70,871	\$ 71,157	\$ 2,090
Real estate – construction and land	1,342	1,346	39
Real estate – business	12,355	12,928	502
Real estate – personal	5,707	8,134	295
Consumer	5,464	5,464	52
Revolving home equity	114	114	11
Consumer credit card	6,887	6,887	561
	\$ 102,740	\$ 106,030	\$ 3,550
Total	\$ 108,896	\$ 116,266	\$ 3,550
December 31, 2017			
With no related allowance recorded:			
Business	\$ 5,356	\$ 9,000	\$ —
Real estate – business	1,299	1,303	—
Consumer	779	817	—
	\$ 7,434	\$ 11,120	\$ —
With an allowance recorded:			
Business	\$ 72,589	\$ 73,168	\$ 2,455
Real estate – construction and land	837	841	27
Real estate – business	12,532	13,071	585
Real estate – personal	9,126	11,914	532
Consumer	5,388	5,426	67
Revolving home equity	204	204	11
Consumer credit card	6,685	6,685	566
	\$ 107,361	\$ 111,309	\$ 4,243
Total	\$ 114,795	\$ 122,429	\$ 4,243

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Total average impaired loans for the three and six month periods ended June 30, 2018 and 2017, respectively, are shown in the table below.

(In thousands)	Commercial	Personal Banking	Total
Average Impaired Loans:			
For the three months ended June 30, 2018			
Non-accrual loans	\$ 7,676	\$ 2,005	\$ 9,681
Restructured loans (accruing)	81,832	17,122	98,954
Total	\$ 89,508	\$ 19,127	\$ 108,635
For the six months ended June 30, 2018			
Non-accrual loans	\$ 8,097	\$ 2,464	\$ 10,561
Restructured loans (accruing)	80,552	17,943	98,495
Total	\$ 88,649	\$ 20,407	\$ 109,056
For the three months ended June 30, 2017			
Non-accrual loans	\$ 9,867	\$ 4,539	\$ 14,406
Restructured loans (accruing)	34,765	15,780	50,545
Total	\$ 44,632	\$ 20,319	\$ 64,951
For the six months ended June 30, 2017			
Non-accrual loans	\$ 10,238	\$ 4,027	\$ 14,265
Restructured loans (accruing)	33,333	15,991	49,324
Total	\$ 43,571	\$ 20,018	\$ 63,589

The table below shows interest income recognized during the three and six month periods ended June 30, 2018 and 2017, respectively, for impaired loans held at the end of each period. This interest all relates to accruing restructured loans, as discussed in the "Troubled debt restructurings" section on page 15.

(In thousands)	For the		For the Six	
	Three Months Ended June 30	2018	2017	Months Ended June 30
Interest income recognized on impaired loans:				
Business	\$821	\$319	\$1,641	\$637
Real estate – construction and land	22	1	44	2
Real estate – business	147	88	294	175
Real estate – personal	52	36	103	71
Consumer	82	80	164	159
Revolving home equity	1	6	2	12
Consumer credit card	159	145	317	289
Total	\$1,284	\$675	\$2,565	\$1,345

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## Delinquent and non-accrual loans

The following table provides aging information on the Company's past due and accruing loans, in addition to the balances of loans on non-accrual status, at June 30, 2018 and December 31, 2017.

(In thousands)	Current or Less Than 30 Days Past Due	30 – 89 Days Past Due	90 Days Past Due and Still Accruing	Non-accrual	Total
June 30, 2018					
Commercial:					
Business	\$4,983,337	\$1,404	\$443	\$5,114	\$4,990,298
Real estate – construction and land	963,654	3,492	—	5	967,151
Real estate – business	2,718,888	6,227	—	2,465	2,727,580
Personal Banking:					
Real estate – personal	2,092,350	7,155	1,193	1,888	2,102,586
Consumer	1,985,195	25,096	2,353	—	2,012,644
Revolving home equity	372,865	708	984	—	374,557
Consumer credit card	758,230	8,504	8,480	—	775,214
Overdrafts	3,731	350	—	—	4,081
Total	\$13,878,250	\$52,936	\$13,453	\$9,472	\$13,954,111
December 31, 2017					
Commercial:					
Business	\$4,949,148	\$3,085	\$374	\$5,947	\$4,958,554
Real estate – construction and land	967,321	1,473	21	5	968,820
Real estate – business	2,694,234	482	—	2,736	2,697,452
Personal Banking:					
Real estate – personal	2,050,787	6,218	3,321	2,461	2,062,787
Consumer	2,067,025	32,674	3,954	834	2,104,487
Revolving home equity	397,349	1,962	1,276	—	400,587
Consumer credit card	764,568	10,115	9,181	—	783,864
Overdrafts	6,840	283	—	—	7,123
Total	\$13,897,272	\$56,292	\$18,127	\$11,983	\$13,983,674

## Credit quality

The following table provides information about the credit quality of the Commercial loan portfolio, using the Company's internal rating system as an indicator. The internal rating system is a series of grades reflecting management's risk assessment, based on its analysis of the borrower's financial condition. The "pass" category consists of a range of loan grades that reflect increasing, though still acceptable, risk. Movement of risk through the various grade levels in the "pass" category is monitored for early identification of credit deterioration. The "special mention" rating is applied to loans where the borrower exhibits negative financial trends due to borrower specific or systemic conditions that, if left uncorrected, threaten its capacity to meet its debt obligations. The borrower is believed to have sufficient financial flexibility to react to and resolve its negative financial situation. It is a transitional grade that is closely monitored for improvement or deterioration. The "substandard" rating is applied to loans where the borrower exhibits well-defined weaknesses that jeopardize its continued performance and are of a severity that the distinct possibility of default exists. Loans are placed on "non-accrual" when management does not expect to collect payments consistent with acceptable and agreed upon terms of repayment.



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## Commercial Loans

(In thousands)	Business	Real Estate-Construction	Real Estate- Business	Total
June 30, 2018				
Pass	\$4,771,613	\$ 954,492	\$2,648,144	\$8,374,249
Special mention	58,771	10,501	33,791	103,063
Substandard	154,800	2,153	43,180	200,133
Non-accrual	5,114	5	2,465	7,584
Total	\$4,990,298	\$ 967,151	\$2,727,580	\$8,685,029
December 31, 2017				
Pass	\$4,740,013	\$ 955,499	\$2,593,005	\$8,288,517
Special mention	59,177	10,614	50,577	120,368
Substandard	153,417	2,702	51,134	207,253
Non-accrual	5,947	5	2,736	8,688
Total	\$4,958,554	\$ 968,820	\$2,697,452	\$8,624,826

The credit quality of Personal Banking loans is monitored primarily on the basis of aging/delinquency, and this information is provided in the table in the above "Delinquent and non-accrual loans" section. In addition, FICO scores are obtained and updated on a quarterly basis for most of the loans in the Personal Banking portfolio. This is a published credit score designed to measure the risk of default by taking into account various factors from a borrower's financial history. The Bank normally obtains a FICO score at the loan's origination and renewal dates, and updates are obtained on a quarterly basis. Excluded from the table below are certain personal real estate loans for which FICO scores are not obtained because they generally pertain to commercial customer activities and are often underwritten with other collateral considerations. These loans totaled \$211.1 million at June 30, 2018 and \$219.2 million at December 31, 2017. The table also excludes consumer loans related to the Company's patient healthcare loan program, which totaled \$161.8 million at June 30, 2018 and \$145.0 million at December 31, 2017. As the healthcare loans are guaranteed by the hospital, FICO scores are not considered relevant for this program. The personal real estate loans and consumer loans excluded below totaled less than 8% of the Personal Banking portfolio. For the remainder of loans in the Personal Banking portfolio, the table below shows the percentage of balances outstanding at June 30, 2018 and December 31, 2017 by FICO score.

## Personal Banking Loans

	% of Loan Category			
	Real Estate - Personal	Consumer Home Equity	Revolving	Consumer Credit Card
June 30, 2018				
FICO score:				
Under 600	1.1 %	3.2 %	.8 %	4.6 %
600 - 659	2.0	5.1	1.6	14.1
660 - 719	10.0	18.0	9.2	35.3
720 - 779	23.6	23.6	22.1	26.4
780 and over	63.3	50.1	66.3	19.6
Total	100.0 %	100.0 %	100.0 %	100.0 %
December 31, 2017				
FICO score:				
Under 600	1.3 %	3.3 %	1.1 %	4.7 %
600 - 659	2.1	5.5	1.7	14.4
660 - 719	10.5	17.3	9.5	34.4

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720 - 779	25.6	26.8	21.4	26.0
780 and over	60.5	47.1	66.3	20.5
Total	100.0%	100.0 %	100.0 %	100.0 %

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## Troubled debt restructurings

As mentioned previously, the Company's impaired loans include loans which have been classified as troubled debt restructurings, as shown in the table below. Restructured loans are those extended to borrowers who are experiencing financial difficulty and who have been granted a concession. Restructured loans are placed on non-accrual status if the Company does not believe it probable that amounts due under the contractual terms will be collected. Other performing restructured loans are comprised of certain business, construction and business real estate loans classified as substandard. Upon maturity, the loans renewed at interest rates judged not to be market rates for new debt with similar risk and as a result were classified as troubled debt restructurings. These loans are performing in accordance with their modified terms, and because the Company believes it probable that all amounts due under the modified terms of the agreements will be collected, interest on these loans is being recognized on an accrual basis. Troubled debt restructurings also include certain credit card loans under various debt management and assistance programs. Modifications to credit card loans generally involve removing the available line of credit, placing loans on amortizing status, and lowering the contractual interest rate. The Company also classified certain loans as troubled debt restructurings because they were not reaffirmed by the borrower in bankruptcy proceedings. These loans are comprised of personal real estate, revolving home equity and consumer loans. Interest on these loans is being recognized on an accrual basis, as the borrowers are continuing to make payments.

(In thousands)	June 30, 2018	December 31, 2017
Accruing loans:		
Non-market interest rates	\$86,906	\$ 88,588
Assistance programs	6,887	6,685
Bankruptcy non-affirmation	5,335	7,283
Other	296	256
Non-accrual loans	7,156	7,796
Total troubled debt restructurings	\$106,580	\$ 110,608

The table below shows the balance of troubled debt restructurings by loan classification at June 30, 2018, in addition to the outstanding balances of these restructured loans which the Company considers to have been in default at any time during the past twelve months. For purposes of this disclosure, the Company considers "default" to mean 90 days or more past due as to interest or principal.

(In thousands)	June 30, 2018	Balance 90 days past due at any time during previous 12 months
Commercial:		
Business	\$75,680	\$ 32
Real estate - construction and land	1,337	—
Real estate - business	12,311	—
Personal Banking:		
Real estate - personal	4,787	303
Consumer	5,464	115
Revolving home equity	114	42
Consumer credit card	6,887	577



Total troubled debt restructurings \$ 106,580 \$ 1,069

For those loans on non-accrual status also classified as restructured, the modification did not create any further financial effect on the Company as those loans were already recorded at net realizable value. For those performing commercial loans classified as restructured, there were no concessions involving forgiveness of principal or interest and, therefore, there was no financial impact to the Company as a result of modification to these loans. No financial impact resulted from those performing loans where the debt was not reaffirmed in bankruptcy, as no changes to loan terms occurred in that process. The effects of modifications to consumer credit card loans were estimated to decrease interest income by approximately \$925 thousand on an annual, pre-tax basis, compared to amounts contractually owed.

The allowance for loan losses related to troubled debt restructurings on non-accrual status is determined by individual evaluation, including collateral adequacy, using the same process as loans on non-accrual status which are not classified as troubled debt restructurings. Those performing loans classified as troubled debt restructurings are accruing loans which management expects to

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collect under contractual terms. Performing commercial loans have had no other concessions granted other than being renewed at an interest rate judged not to be market. As such, they have similar risk characteristics as non-troubled debt commercial loans and are collectively evaluated based on internal risk rating, loan type, delinquency, historical experience and current economic factors. Performing personal banking loans classified as troubled debt restructurings resulted from the borrower not reaffirming the debt during bankruptcy and have had no other concession granted, other than the Bank's future limitations on collecting payment deficiencies or in pursuing foreclosure actions. As such, they have similar risk characteristics as non-troubled debt personal banking loans and are evaluated collectively based on loan type, delinquency, historical experience and current economic factors.

If a troubled debt restructuring defaults and is already on non-accrual status, the allowance for loan losses continues to be based on individual evaluation, using discounted expected cash flows or the fair value of collateral. If an accruing troubled debt restructuring defaults, the loan's risk rating is downgraded to non-accrual status and the loan's related allowance for loan losses is determined based on individual evaluation, or if necessary, the loan is charged off and collection efforts begun.

The Company had commitments of \$6.1 million at June 30, 2018 to lend additional funds to borrowers with restructured loans.

**Loans held for sale**

The Company designates certain long-term fixed rate personal real estate loans as held for sale, and the Company has elected the fair value option for these loans. The election of the fair value option aligns the accounting for these loans with the related economic hedges discussed in Note 10. The loans are primarily sold to FNMA, FHLMC, and GNMA. At June 30, 2018, the fair value of these loans was \$10.8 million, and the unpaid principal balance was \$10.4 million.

The Company also designates student loan originations as held for sale. The borrowers are credit-worthy students who are attending colleges and universities. The loans are intended to be sold in the secondary market, and the Company maintains contracts with Sallie Mae to sell the loans within 210 days after the last disbursement to the student. These loans are carried at lower of cost or fair value, which at June 30, 2018 totaled \$9.6 million.

At June 30, 2018, none of the loans held for sale were on non-accrual status or 90 days past due and still accruing.

**Foreclosed real estate/repossessed assets**

The Company's holdings of foreclosed real estate totaled \$1.0 million and \$681 thousand at June 30, 2018 and December 31, 2017, respectively. Personal property acquired in repossession, generally autos and marine and recreational vehicles, totaled \$2.3 million and \$2.7 million at June 30, 2018 and December 31, 2017, respectively. Upon acquisition, these assets are recorded at fair value less estimated selling costs at the date of foreclosure, establishing a new cost basis. They are subsequently carried at the lower of this cost basis or fair value less estimated selling costs.

**3. Investment Securities**

Investment securities as shown in this report reflect revised categories as required by the Company's adoption of ASU 2016-01, "Recognition and Measurement of Financial Assets and Financial Liabilities", on January 1, 2018. That new guidance refined the definition of equity securities and required their segregation from available for sale debt securities. For comparability purposes, prior period disclosures in this report have been revised to show the new categorization.

	June 30,	December
(In thousands)	2018	31, 2017
Available for sale debt securities	\$8,412,376	\$8,725,442
Trading debt securities	31,156	18,269

## Equity securities:

Readily determinable fair value	2,741	48,838
No readily determinable fair value	1,703	1,753

## Other:

Federal Reserve Bank stock	33,369	33,253
Federal Home Loan Bank stock	10,000	10,000
Private equity investments	68,940	55,752
Total investment securities	\$8,560,285	\$8,893,307

While changes in the fair value of available for sale debt securities continue to be recorded in the equity category of accumulated other comprehensive income, the new guidance requires changes in the fair value of equity securities to be recorded in current earnings. As required by the new guidance, the unrealized gain in fair value on equity securities (recorded in accumulated other

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comprehensive income at December 31, 2017) was reclassified to retained earnings on January 1, 2018. The amount of the reclassification was \$33.3 million, net of tax.

Equity securities include common and preferred stock with readily determinable fair values that totaled \$2.5 million at cost and \$2.7 million at fair value at June 30, 2018. The decline in these balances from prior periods was due to a third party merger transaction in June 2018, in which the majority of these securities were redeemed for cash of \$39.9 million. During the first six months of 2018, unrealized net losses of \$176 thousand were recognized in current earnings on equity securities still held at June 30, 2018.

Equity securities also include securities with a carrying value of \$1.7 million that do not have readily determinable fair values. The Company has elected, under the ASU, to measure these at cost minus impairment, if any, plus or minus changes resulting from observable price changes for the identical or similar investment of the same issuer. The Company did not record any impairment or other adjustments to the carrying amount of these investments during the period.

Other investment securities whose accounting is not addressed in the ASU include Federal Reserve Bank (FRB) stock, Federal Home Loan Bank (FHLB) stock, and investments in portfolio concerns held by the Company's private equity subsidiaries. FRB stock and FHLB stock are held for debt and regulatory purposes. Investment in FRB stock is based on the capital structure of the investing bank, and investment in FHLB stock is tied to the level of borrowings from the FHLB. These holdings are carried at cost. The private equity investments, in the absence of readily ascertainable market values, are carried at estimated fair value.

The majority of the Company's investment portfolio is comprised of available for sale debt securities, which are carried at fair value with changes in fair value reported in accumulated other comprehensive income (AOCI). A summary of the available for sale debt securities by maturity groupings as of June 30, 2018 is shown below. The investment portfolio includes agency mortgage-backed securities, which are guaranteed by agencies such as the FHLMC, FNMA, GNMA and FDIC, in addition to non-agency mortgage-backed securities, which have no guarantee but are collateralized by commercial and residential mortgages. Also included are certain other asset-backed securities, which are primarily collateralized by credit cards, automobiles, student loans, and commercial loans. These securities differ from traditional debt securities primarily in that they may have uncertain maturity dates and are priced based on estimated prepayment rates on the underlying collateral.

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(In thousands)	Amortized Cost	Fair Value
U.S. government and federal agency obligations:		
Within 1 year	\$52,660	\$52,603
After 1 but within 5 years	645,431	634,819
After 5 but within 10 years	157,967	155,108
After 10 years	69,202	68,562
Total U.S. government and federal agency obligations	925,260	911,092
Government-sponsored enterprise obligations:		
Within 1 year	117,562	117,444
After 1 but within 5 years	121,584	119,743
After 5 but within 10 years	34,984	33,946
After 10 years	42,852	40,228
Total government-sponsored enterprise obligations	316,982	311,361
State and municipal obligations:		
Within 1 year	147,325	147,668
After 1 but within 5 years	598,663	600,688
After 5 but within 10 years	591,819	590,950
After 10 years	40,963	39,858
Total state and municipal obligations	1,378,770	1,379,164
Mortgage and asset-backed securities:		
Agency mortgage-backed securities	3,194,764	3,131,025
Non-agency mortgage-backed securities	1,019,545	1,010,331
Asset-backed securities	1,351,461	1,338,542
Total mortgage and asset-backed securities	5,565,770	5,479,898
Other debt securities:		
Within 1 year	9,003	8,971
After 1 but within 5 years	257,704	252,151
After 5 but within 10 years	73,283	69,739
Total other debt securities	339,990	330,861
Total available for sale debt securities	\$8,526,772	\$8,412,376

Investments in U.S. government and federal agency obligations include U.S. Treasury inflation-protected securities, which totaled \$443.8 million, at fair value, at June 30, 2018. Interest paid on these securities increases with inflation and decreases with deflation, as measured by the Consumer Price Index. Included in state and municipal obligations are \$15.1 million, at fair value, of auction rate securities, which were purchased from bank customers in 2008. Interest on these bonds is currently being paid at the maximum failed auction rates.

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For debt securities classified as available for sale, the following table shows the unrealized gains and losses (pre-tax) in AOCI, by security type.

(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
June 30, 2018				
U.S. government and federal agency obligations	\$925,260	\$ 503	\$(14,671 )	\$911,092
Government-sponsored enterprise obligations	316,982	—	(5,621 )	311,361
State and municipal obligations	1,378,770	8,105	(7,711 )	1,379,164
Mortgage and asset-backed securities:				
Agency mortgage-backed securities	3,194,764	5,995	(69,734 )	3,131,025
Non-agency mortgage-backed securities	1,019,545	6,232	(15,446 )	1,010,331
Asset-backed securities	1,351,461	2,343	(15,262 )	1,338,542
Total mortgage and asset-backed securities	5,565,770	14,570	(100,442 )	5,479,898
Other debt securities	339,990	—	(9,129 )	330,861
Total	\$8,526,772	\$ 23,178	\$(137,574 )	\$8,412,376
December 31, 2017				
U.S. government and federal agency obligations	\$917,494	\$ 4,096	\$(4,443 )	\$917,147
Government-sponsored enterprise obligations	408,266	26	(1,929 )	406,363
State and municipal obligations	1,592,707	21,413	(2,754 )	1,611,366
Mortgage and asset-backed securities:				
Agency mortgage-backed securities	3,046,701	17,956	(23,744 )	3,040,913
Non-agency mortgage-backed securities	903,920	6,710	(4,837 )	905,793
Asset-backed securities	1,495,380	2,657	(5,237 )	1,492,800
Total mortgage and asset-backed securities	5,446,001	27,323	(33,818 )	5,439,506
Other debt securities	350,988	1,250	(1,178 )	351,060
Total	\$8,715,456	\$ 54,108	\$(44,122 )	\$8,725,442

The Company's impairment policy requires a review of all securities for which fair value is less than amortized cost. Special emphasis and analysis is placed on securities whose credit rating has fallen below A3 (Moody's) or A- (Standard & Poor's), whose fair values have fallen more than 20% below purchase price for an extended period of time, or who have been identified based on management's judgment. These securities are placed on a watch list, and for all such securities, cash flow analyses are prepared. For more complex analyses, detailed cash flow models are prepared which use inputs specific to each security. Inputs to these models include factors such as cash flow received, contractual payments required, and various other information related to the underlying collateral (including current delinquencies), collateral loss severity rates (including loan to values), expected delinquency rates, credit support from other tranches, and prepayment speeds. Stress tests are performed at varying levels of delinquency rates, prepayment speeds and loss severities in order to gauge probable ranges of credit loss. At June 30, 2018, the fair value of securities on this watch list was \$57.3 million compared to \$68.0 million at December 31, 2017.

As of June 30, 2018, the Company had recorded other-than-temporary impairment (OTTI) on certain non-agency mortgage-backed securities, part of the watch list mentioned above, which had an aggregate fair value of \$22.4 million. The cumulative credit-related portion of the impairment on these securities, which was recorded in earnings, totaled \$14.2 million. The Company does not intend to sell these securities and believes it is not likely that it will be required to sell the securities before the recovery of their amortized cost.

The credit-related portion of the loss on these securities was based on the cash flows projected to be received over the estimated life of the securities, discounted to present value, and compared to the current amortized cost bases of the securities. Significant inputs to the cash flow models used to calculate the credit losses on these securities at June 30,

2018 included the following:

Significant Inputs	Range
Prepayment CPR	0% -25%
Projected cumulative default	13%-52%
Credit support	0% -20%
Loss severity	14%-63%

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The following table presents a rollforward of the cumulative OTTI credit losses recognized in earnings on all available for sale debt securities.

(In thousands)	For the Six Months Ended June 30	
	2018	2017
Cumulative OTTI credit losses at January 1	\$ 14,199	\$ 14,080
Credit losses on debt securities for which impairment was not previously recognized	58	46
Credit losses on debt securities for which impairment was previously recognized	10	274
Increase in expected cash flows that are recognized over remaining life of security	(104)	(146)
Cumulative OTTI credit losses at June 30	\$ 14,163	\$ 14,254

Debt securities with unrealized losses recorded in AOCI are shown in the table below, along with the length of the impairment period.

(In thousands)	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
June 30, 2018						
U.S. government and federal agency obligations	\$ 707,018	\$ 12,156	\$ 90,340	\$ 2,515	\$ 797,358	\$ 14,671
Government-sponsored enterprise obligations	261,378	5,605	49,983	16	311,361	5,621
State and municipal obligations	458,880	5,700	51,863	2,011	510,743	7,711
Mortgage and asset-backed securities:						
Agency mortgage-backed securities	2,029,957	45,267	566,986	24,467	2,596,943	69,734
Non-agency mortgage-backed securities	773,890	12,076	134,679	3,370	908,569	15,446
Asset-backed securities	862,416	13,296	173,895	1,966	1,036,311	15,262
Total mortgage and asset-backed securities	3,666,263	70,639	875,560	29,803	4,541,823	100,442
Other debt securities	311,714	8,033	19,147	1,096	330,861	9,129
Total	\$ 5,405,253	\$ 102,133	\$ 1,086,893	\$ 35,441	\$ 6,492,146	\$ 137,574
December 31, 2017						
U.S. government and federal agency obligations	\$ 618,617	\$ 4,443	\$ —	\$ —	\$ 618,617	\$ 4,443
Government-sponsored enterprise obligations	286,393	1,712	49,766	217	336,159	1,929
State and municipal obligations	282,843	1,752	49,339	1,002	332,182	2,754
Mortgage and asset-backed securities:						
Agency mortgage-backed securities	1,320,689	9,433	619,300	14,311	1,939,989	23,744
Non-agency mortgage-backed securities	577,017	2,966	153,813	1,871	730,830	4,837
Asset-backed securities	786,048	3,168	264,295	2,069	1,050,343	5,237
Total mortgage and asset-backed securities	2,683,754	15,567	1,037,408	18,251	3,721,162	33,818
Other debt securities	144,090	727	20,202	451	164,292	1,178
Total	\$ 4,015,697	\$ 24,201	\$ 1,156,715	\$ 19,921	\$ 5,172,412	\$ 44,122

The available for sale debt portfolio included \$6.5 billion of securities that were in a loss position at June 30, 2018, compared to \$5.2 billion at December 31, 2017. The total amount of unrealized loss on these securities was \$137.6 million at June 30, 2018, an increase of \$93.5 million compared to the loss at December 31, 2017. This increase in losses was mainly due to a rising rate environment.



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The following tables present proceeds from sales of securities and the components of investment securities gains and losses which have been recognized in earnings.

For the  
Six  
Months  
Ended  
June 30