COMMERCE BANCSHARES INC /MO/
Form 10-Q
August 06, 2018
Table of contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark One)

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

For the quarterly period ended June 30, 2018

OR

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

For the transition period from to
Commission File 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,<br>Kansas City, MO | 64106 |
| (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 þ No o

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

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 filer þ | Accelerated filer o | Non-accelerated filer o | Smaller reporting company £ | Emerging growth company £ |

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. o

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

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.

Commerce Bancshares, Inc. and Subsidiaries

Form 10-Q

INDEX

Table of contents

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) | |
| ASSETS | | |
| 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 |
| LIABILITIES AND EQUITY | | |
| 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 |

| | | |
|---|---|---|
| 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.

3

Table of contents

Commerce Bancshares, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF INCOME

| | For the Three Months Ended June 30 | | For the Six Months Ended June 30 | |
|---|---|---|---|---|
| (In thousands, except per share data) | 2018 | 2017 | 2018 | 2017 |
| | (Unaudited) | | | |
| INTEREST INCOME | | | | |
| 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 |
| INTEREST EXPENSE | | | | |
| 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 |
| NON-INTEREST INCOME | | | | |
| 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 |
| INVESTMENT SECURITIES GAINS (LOSSES), NET | (3,075) | 1,651 | 2,335 | 879 |
| NON-INTEREST EXPENSE | | | | |
| 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 |

| | | | | |
|---|---|---|---|---|
| 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.

Table of contents

Commerce Bancshares, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

| | For the Three Months Ended June 30 | | For the Six Months Ended June 30 | |
|---|---|---|---|---|
| (In thousands) | 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.

Table of contents

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 depositary 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.

Table of contents

Commerce Bancshares, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF CASH FLOWS

| (In thousands) | For the Six Months Ended June 30 2018 | 2017 |
|---|---|---|
| | (Unaudited) | |
| OPERATING ACTIVITIES: | | |
| 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 |
| INVESTING ACTIVITIES: | | |
| 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 |
| FINANCING ACTIVITIES: | | |
| 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.

Table of contents

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.

Table of contents

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:

| | For the Three Months Ended June 30 | | | For the Six Months Ended June 30 | | |
|---|---|---|---|---|---|---|
| (In thousands) | 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 |

Table of contents

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.

| | Impaired Loans | | All Other Loans | |
|---|---|---|---|---|
| (In thousands) | 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 |

Table of contents

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 |

Table of contents

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.

| | For the Three Months Ended June 30 | | For the Six Months Ended June 30 | |
|---|---|---|---|---|
| (In thousands) | 2018 | 2017 | 2018 | 2017 |
| 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 |

Table of contents

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.

Table of contents

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 | Revolving Home Equity | 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 |

| | | | | |
|---|---|---|---|---|
| 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 % |

Table of contents

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 restructings 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 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.

| (In thousands) | June 30, 2018 | December 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 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.

Table of contents

| (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.

Table of contents

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 | | |