

COMMERCE BANCSHARES INC /MO/

Form 10-Q

August 05, 2011

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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**

For the quarterly period ended June 30, 2011
OR

**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
(State of Incorporation)

43-0889454
(IRS Employer Identification No.)

**1000 Walnut,
Kansas City, MO**
(Address of principal executive offices)

64106
(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, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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 July 21, 2011, the registrant had outstanding 86,852,616 shares of its \$5 par value common stock, registrant's only class of common stock.

Commerce Bancshares, Inc. and Subsidiaries

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	June 30 2011	December 31 2010
	<i>(Unaudited)</i>	
	<i>(In thousands)</i>	
ASSETS		
Loans	\$ 9,237,078	\$ 9,410,982
Allowance for loan losses	(191,538)	(197,538)
Net loans	9,045,540	9,213,444
Loans held for sale	42,359	63,751
Investment securities:		
Available for sale (\$425,864,000 and \$429,439,000 pledged in 2011 and 2010, respectively, to secure structured repurchase agreements)	7,717,634	7,294,303
Trading	32,074	11,710
Non-marketable	109,867	103,521
Total investment securities	7,859,575	7,409,534
Short-term federal funds sold and securities purchased under agreements to resell	10,845	10,135
Long-term securities purchased under agreements to resell	850,000	450,000
Interest earning deposits with banks	535,696	122,076
Cash and due from banks	340,594	328,464
Land, buildings and equipment, net	374,732	383,397
Goodwill	125,585	125,585
Other intangible assets, net	9,394	10,937
Other assets	376,540	385,016
Total assets	\$ 19,570,860	\$ 18,502,339

LIABILITIES AND EQUITY

Deposits:

Non-interest bearing	\$ 4,834,750	\$ 4,494,028
Savings, interest checking and money market	8,139,989	7,846,831
Time open and C.D. s of less than \$100,000	1,273,961	1,465,050
Time open and C.D. s of \$100,000 and over	1,407,866	1,279,112

Total deposits	15,656,566	15,085,021
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Federal funds purchased and securities sold under agreements to repurchase	1,282,470	982,827
Other borrowings	111,929	112,273
Other liabilities	388,328	298,754

Total liabilities	17,439,293	16,478,875
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Commerce Bancshares, Inc. stockholders' equity:

Preferred stock, \$1 par value		
Authorized and unissued 2,000,000 shares		
Common stock, \$5 par value		
Authorized 100,000,000 shares; issued 87,296,284 shares in 2011 and 86,788,322 shares in 2010	436,481	433,942
Capital surplus	979,247	971,293
Retained earnings	645,155	555,778
Treasury stock of 355,116 shares in 2011 and 61,839 shares in 2010, at cost	(14,515)	(2,371)
Accumulated other comprehensive income	83,000	63,345

Total Commerce Bancshares, Inc. stockholders' equity	2,129,368	2,021,987
Non-controlling interest	2,199	1,477

Total equity	2,131,567	2,023,464
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Total liabilities and equity	\$ 19,570,860	\$ 18,502,339
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See accompanying notes to consolidated financial statements.

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	
	2011	2010	2011	2010
<i>(In thousands, except per share data)</i>				
	<i>(Unaudited)</i>			
INTEREST INCOME				
Interest and fees on loans	\$ 116,769	\$ 128,781	\$ 235,146	\$ 259,703
Interest and fees on loans held for sale	309	2,261	607	4,165
Interest on investment securities	57,712	53,801	112,601	108,964
Interest on short-term federal funds sold and securities purchased under agreements to resell	22	13	32	28
Interest on long-term securities purchased under agreements to resell	3,165		5,327	
Interest on deposits with banks	110	201	200	266
Total interest income	178,087	185,057	353,913	373,126
INTEREST EXPENSE				
Interest on deposits:				
Savings, interest checking and money market	6,372	7,711	13,272	14,807
Time open and C.D. s of less than \$100,000	2,965	6,059	6,708	12,874
Time open and C.D. s of \$100,000 and over	2,434	3,562	5,107	7,485
Interest on federal funds purchased and securities sold under agreements to repurchase	687	826	1,309	1,646
Interest on other borrowings	919	3,791	1,834	10,496
Total interest expense	13,377	21,949	28,230	47,308
Net interest income	164,710	163,108	325,683	325,818
Provision for loan losses	12,188	22,187	27,977	56,509
Net interest income after provision for loan losses	152,522	140,921	297,706	269,309
NON-INTEREST INCOME				
Bank card transaction fees	41,304	37,659	78,766	70,149
Trust fees	22,544	20,358	44,116	39,676
Deposit account charges and other fees	20,789	25,472	40,089	49,453
Bond trading income	4,979	5,387	9,699	10,391

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Consumer brokerage services	2,880	2,372	5,543	4,489
Loan fees and sales	2,075	3,472	3,899	5,311
Other	6,773	6,738	15,138	15,178
Total non-interest income	101,344	101,458	197,250	194,647
INVESTMENT SECURITIES GAINS (LOSSES), NET				
Impairment (losses) reversals on debt securities	(2,119)	4,415	4,186	5,710
Noncredit-related losses (reversals) on securities not expected to be sold	1,469	(5,091)	(5,110)	(7,843)
Net impairment losses	(650)	(676)	(924)	(2,133)
Realized gains (losses) on sales and fair value adjustments	2,606	1,336	4,207	(872)
Investment securities gains (losses), net	1,956	660	3,283	(3,005)
NON-INTEREST EXPENSE				
Salaries and employee benefits	84,223	87,108	171,615	174,546
Net occupancy	11,213	11,513	23,250	23,611
Equipment	5,702	5,938	11,279	11,839
Supplies and communication	5,692	6,829	11,224	14,167
Data processing and software	17,531	17,497	33,998	34,103
Marketing	4,495	5,002	8,753	9,720
Deposit insurance	2,780	4,939	7,671	9,689
Indemnification obligation		(1,683)	(1,359)	(1,683)
Other	21,877	18,650	41,042	35,525
Total non-interest expense	153,513	155,793	307,473	311,517
Income before income taxes	102,309	87,246	190,766	149,434
Less income taxes	32,692	27,428	60,199	45,805
Net income	69,617	59,818	130,567	103,629
Less non-controlling interest expense (income)	583	84	1,080	(275)
Net income attributable to Commerce Bancshares, Inc.	\$ 69,034	\$ 59,734	\$ 129,487	\$ 103,904
Net income per common share basic	\$.80	\$.69	\$ 1.49	\$ 1.19

Net income per common share	diluted	\$.79	\$.68	\$	1.48	\$	1.18
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See accompanying notes to consolidated financial statements.

Table of Contents**Commerce Bancshares, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**

<i>(In thousands, except per share data)</i>	Commerce Bancshares, Inc. Shareholders						Total
	Common Stock	Capital Surplus	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Non- Controlling Interest	
	<i>(Unaudited)</i>						
Balance January 1, 2011	\$ 433,942	\$ 971,293	\$ 555,778	\$ (2,371)	\$ 63,345	\$ 1,477	\$ 2,023,464
Net income			129,487			1,080	130,567
Change in unrealized gain (loss) related to available for sale securities for which a portion of an other-than-temporary impairment has been recorded in earnings, net of tax					3,511		3,511
Change in unrealized gain (loss) on all other available for sale securities, net of tax					15,474		15,474
Amortization of pension loss, net of tax					670		670
Total comprehensive income							150,222
Distributions to non-controlling interest						(358)	(358)
Purchase of treasury stock				(18,341)			(18,341)
Issuance of stock under purchase and equity compensation plans	1,563	5,483		6,317			13,363
Net tax benefit related to equity compensation plans		955					955
Stock-based compensation		2,372					2,372
Issuance of nonvested stock awards	976	(856)		(120)			
Cash dividends paid (\$.460 per share)			(40,110)				(40,110)

Balance June 30, 2011	\$ 436,481	\$ 979,247	\$ 645,155	\$ (14,515)	\$ 83,000	\$ 2,199	\$ 2,131,567
Balance January 1, 2010	\$ 415,637	\$ 854,490	\$ 568,532	\$ (838)	\$ 46,407	\$ 1,677	\$ 1,885,905
Net income			103,904			(275)	103,629
Change in unrealized gain (loss) related to available for sale securities for which a portion of an other-than-temporary impairment has been recorded in earnings, net of tax					7,420		7,420
Change in unrealized gain (loss) on all other available for sale securities, net of tax					21,267		21,267
Amortization of pension loss, net of tax					703		703
Total comprehensive income							133,019
Distributions to non-controlling interest						(235)	(235)
Purchase of treasury stock				(943)			(943)
Issuance of stock under purchase and equity compensation plans	1,229	4,640		(198)			5,671
Net tax benefit related to equity compensation plans		1,026					1,026
Stock-based compensation		3,386					3,386
Issuance of nonvested stock awards	751	(577)		(174)			
Cash dividends paid (\$.448 per share)			(39,215)				(39,215)
Balance June 30, 2010	\$ 417,617	\$ 862,965	\$ 633,221	\$ (2,153)	\$ 75,797	\$ 1,167	\$ 1,988,614

See accompanying notes to consolidated financial statements.

Table of Contents**Commerce Bancshares, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF CASH FLOWS**

<i>(In thousands)</i>	For the Six Months Ended June 30	
	2011	2010
	<i>(Unaudited)</i>	
OPERATING ACTIVITIES:		
Net income	\$ 130,567	\$ 103,629
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	27,977	56,509
Provision for depreciation and amortization	23,732	24,864
Amortization of investment security premiums, net	2,413	8,752
Investment securities (gains) losses, net(A)	(3,283)	3,005
Net gains on sales of loans held for sale	(1,147)	(2,466)
Originations of loans held for sale	(28,631)	(288,903)
Proceeds from sales of loans held for sale	51,297	146,747
Net increase in trading securities	(374)	(2,121)
Stock-based compensation	2,372	3,386
Increase in interest receivable	(1,095)	(512)
Decrease in interest payable	(2,686)	(3,829)
Increase in income taxes payable	5,594	7,598
Net tax benefit related to equity compensation plans	(955)	(1,026)
Other changes, net	(10,912)	39,097
Net cash provided by operating activities	194,869	94,730
INVESTING ACTIVITIES:		
Proceeds from sales of investment securities(A)	11,202	64,087
Proceeds from maturities/pay downs of investment securities(A)	1,400,631	954,133
Purchases of investment securities(A)	(1,809,501)	(1,040,529)
Net decrease in loans	139,927	356,824
Long-term securities purchased under agreements to resell	(500,000)	
Repayments of long-term securities purchased under agreements to resell	100,000	
Purchases of land, buildings and equipment	(11,133)	(9,395)
Sales of land, buildings and equipment	1,711	377
Net cash provided by (used in) investing activities	(667,163)	325,497
FINANCING ACTIVITIES:		
Net increase in non-interest bearing, savings, interest checking and money market deposits	705,923	295,593

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Net decrease in time open and C.D. s	(62,335)	(25,649)
Net increase (decrease) in short-term federal funds purchased and securities sold under agreements to repurchase	299,643	(96,835)
Repayment of long-term borrowings	(352)	(372,065)
Net increase in short-term borrowings	8	
Purchases of treasury stock	(18,341)	(943)
Issuance of stock under stock purchase and equity compensation plans	13,363	5,671
Net tax benefit related to equity compensation plans	955	1,026
Cash dividends paid on common stock	(40,110)	(39,215)
Net cash provided by (used in) financing activities	898,754	(232,417)
Increase in cash and cash equivalents	426,460	187,810
Cash and cash equivalents at beginning of year	460,675	463,834
Cash and cash equivalents at June 30	\$ 887,135	\$ 651,644

(A) Available for sale and non-marketable securities

Income tax net payments	\$ 54,661	\$ 38,182
Interest paid on deposits and borrowings	\$ 30,916	\$ 51,137
Loans transferred to foreclosed real estate	\$ 18,343	\$ 8,982

See accompanying notes to consolidated financial statements.

Table of Contents**Commerce Bancshares, Inc. and Subsidiaries****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

June 30, 2011 (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). The consolidated financial statements in this report have not been audited. All significant intercompany accounts and transactions have been eliminated. Certain reclassifications were made to 2010 data to conform to current year presentation. These included the reclassification of certain non-interest bearing deposits from money market accounts to non-interest bearing deposits, in order to more accurately present the Company's balances of non-interest bearing deposits. 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. The results of operations for the three and six month periods ended June 30, 2011 are not necessarily indicative of results to be attained for the full year or any other interim periods.

The significant accounting policies followed in the preparation of the quarterly financial statements are disclosed in the 2010 Annual Report on Form 10-K.

2. Loans and Allowance for Loan Losses

Major classifications within the Company's held to maturity loan portfolio at June 30, 2011 and December 31, 2010 are as follows:

<i>(In thousands)</i>	June 30 2011	December 31 2010
Commercial:		
Business	\$ 2,921,556	\$ 2,957,043
Real estate - construction and land	433,464	460,853
Real estate - business	2,097,691	2,065,837
Personal Banking:		
Real estate - personal	1,438,030	1,440,386
Consumer	1,108,909	1,164,327
Revolving home equity	467,391	477,518
Consumer credit card	764,844	831,035
Overdrafts	5,193	13,983
Total loans	\$ 9,237,078	\$ 9,410,982

At June 30, 2011, loans of \$3.0 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 \$1.2 billion were pledged at the Federal Reserve Bank as collateral for discount window borrowings.

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A summary of the activity in the allowance for loan losses during the three and six months ended June 30, 2011 follows:

<i>(In thousands)</i>	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	\$ 128,351	\$ 66,187	\$ 194,538	\$ 119,946	\$ 77,592	\$ 197,538
Provision	1,815	10,373	12,188	15,280	12,697	27,977
Deductions:						
Loans charged off	3,946	15,656	19,602	10,310	32,681	42,991
Less recoveries on loans	1,043	3,371	4,414	2,347	6,667	9,014
Net loans charged off	2,903	12,285	15,188	7,963	26,014	33,977
Balance at June 30, 2011	\$ 127,263	\$ 64,275	\$ 191,538	\$ 127,263	\$ 64,275	\$ 191,538

A summary of the activity in the allowance for loan losses during the three and six months ended June 30, 2010 follows:

<i>(In thousands)</i>	For the Three Months Ended June 30	For the Six Months Ended June 30
Balance at beginning of period	\$ 197,538	\$ 194,480
Provision for loan losses	22,187	56,509
Deductions:		
Loans charged off	26,818	62,338
Less recoveries on loans	4,631	8,887
Net loans charged off	22,187	53,451
Balance at June 30, 2010	\$ 197,538	\$ 197,538

The following table shows the balance in the allowance for loan losses and the related loan balance at June 30, 2011 and December 31, 2010, disaggregated on the basis of impairment methodology. Impaired loans evaluated under ASC 310-10-35 include loans on non-accrual status which are individually evaluated for impairment, and other impaired loans deemed to have similar risk characteristics, which are collectively evaluated. All other loans are collectively evaluated for impairment under ASC 450-20.

<i>(In thousands)</i>	Commercial	Personal Banking	Total
June 30, 2011			
Allowance for loan losses:			
Impaired loans	\$ 6,862	\$ 3,599	\$ 10,461
All other loans	120,401	60,676	181,077
Loans outstanding:			
Impaired loans	119,133	30,464	149,597
All other loans	5,333,578	3,753,903	9,087,481
December 31, 2010			
Allowance for loan losses:			
Impaired loans	\$ 6,127	\$ 3,243	\$ 9,370
All other loans	113,819	74,349	188,168
Loans outstanding:			
Impaired loans	118,532	26,828	145,360
All other loans	5,365,201	3,900,421	9,265,622

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Impaired loans

The table below shows the Company's investment in impaired loans at June 30, 2011 and December 31, 2010. These loans consist of loans on non-accrual status and other restructured loans whose terms have been modified and classified as troubled debt restructurings under ASC 310-40. The restructured loans have been extended to borrowers who are experiencing financial difficulty and who have been granted a concession. They are largely 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 totaled \$48.5 million and \$41.3 million at June 30, 2011 and December 31, 2010, respectively. 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. Troubled debt restructurings also include certain credit card loans under various debt management and assistance programs, which totaled \$21.4 million at June 30, 2011 and \$18.8 million at December 31, 2010.