



As of July 31, 2013, the registrant had outstanding 90,697,504 shares of its \$5 par value common stock, registrant's only class of common stock.

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Commerce Bancshares, Inc. and Subsidiaries

Form 10-Q

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## PART I: FINANCIAL INFORMATION

## Item 1. FINANCIAL STATEMENTS

## Commerce Bancshares, Inc. and Subsidiaries

## CONSOLIDATED BALANCE SHEETS

|                                                                                                                                       | June 30, 2013  | December 31,<br>2012 |
|---------------------------------------------------------------------------------------------------------------------------------------|----------------|----------------------|
|                                                                                                                                       | (Unaudited)    |                      |
|                                                                                                                                       | (In thousands) |                      |
| <b>ASSETS</b>                                                                                                                         |                |                      |
| Loans                                                                                                                                 | \$ 10,370,155  | \$ 9,831,384         |
| Allowance for loan losses                                                                                                             | (166,032 )     | (172,532 )           |
| Net loans                                                                                                                             | 10,204,123     | 9,658,852            |
| Loans held for sale                                                                                                                   | 8,941          | 8,827                |
| Investment securities:                                                                                                                |                |                      |
| Available for sale (\$746,141,000 and \$736,183,000 pledged in 2013 and 2012, respectively, to secure swap and repurchase agreements) | 8,927,815      | 9,522,248            |
| Trading                                                                                                                               | 14,670         | 28,837               |
| Non-marketable                                                                                                                        | 113,470        | 118,650              |
| Total investment securities                                                                                                           | 9,055,955      | 9,669,735            |
| Short-term federal funds sold and securities purchased under agreements to resell                                                     | 22,990         | 27,595               |
| Long-term securities purchased under agreements to resell                                                                             | 1,200,000      | 1,200,000            |
| Interest earning deposits with banks                                                                                                  | 6,816          | 179,164              |
| Cash and due from banks                                                                                                               | 399,687        | 573,066              |
| Land, buildings and equipment, net                                                                                                    | 352,462        | 357,612              |
| Goodwill                                                                                                                              | 125,585        | 125,585              |
| Other intangible assets, net                                                                                                          | 4,517          | 5,300                |
| Other assets                                                                                                                          | 529,275        | 353,853              |
| Total assets                                                                                                                          | \$ 21,910,351  | \$ 22,159,589        |
| <b>LIABILITIES AND EQUITY</b>                                                                                                         |                |                      |
| Deposits:                                                                                                                             |                |                      |
| Non-interest bearing                                                                                                                  | \$ 5,811,473   | \$ 6,299,903         |
| Savings, interest checking and money market                                                                                           | 9,573,390      | 9,817,943            |
| Time open and C.D.'s of less than \$100,000                                                                                           | 1,039,131      | 1,074,618            |
| Time open and C.D.'s of \$100,000 and over                                                                                            | 1,472,944      | 1,156,189            |
| Total deposits                                                                                                                        | 17,896,938     | 18,348,653           |
| Federal funds purchased and securities sold under agreements to repurchase                                                            | 1,620,694      | 1,083,550            |
| Other borrowings                                                                                                                      | 102,766        | 103,710              |
| Other liabilities                                                                                                                     | 183,166        | 452,102              |
| Total liabilities                                                                                                                     | 19,803,564     | 19,988,015           |
| 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 91,729,235 shares in 2013 and 2012                                                              | 458,646        | 458,646              |
| Capital surplus                                                                                                                       | 1,094,922      | 1,102,507            |
| Retained earnings                                                                                                                     | 563,166        | 477,210              |

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|                                                                              |              |              |   |
|------------------------------------------------------------------------------|--------------|--------------|---|
| Treasury stock of 934,853 shares in 2013 and 196,922 shares in 2012, at cost | (35,771      | ) (7,580     | ) |
| Accumulated other comprehensive income                                       | 21,864       | 136,344      |   |
| Total Commerce Bancshares, Inc. stockholders' equity                         | 2,102,827    | 2,167,127    |   |
| Non-controlling interest                                                     | 3,960        | 4,447        |   |
| Total equity                                                                 | 2,106,787    | 2,171,574    |   |
| Total liabilities and equity                                                 | \$21,910,351 | \$22,159,589 |   |

See accompanying notes to consolidated financial statements.

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Commerce Bancshares, Inc. and Subsidiaries

## CONSOLIDATED STATEMENTS OF INCOME

| (In thousands, except per share data)                                                         | For the Three Months |            | For the Six Months |            |
|-----------------------------------------------------------------------------------------------|----------------------|------------|--------------------|------------|
|                                                                                               | Ended June 30        |            | Ended June 30      |            |
|                                                                                               | 2013                 | 2012       | 2013               | 2012       |
|                                                                                               | (Unaudited)          |            |                    |            |
| <b>INTEREST INCOME</b>                                                                        |                      |            |                    |            |
| Interest and fees on loans                                                                    | \$ 108,018           | \$ 112,252 | \$ 215,804         | \$ 224,008 |
| Interest and fees on loans held for sale                                                      | 91                   | 88         | 176                | 193        |
| Interest on investment securities                                                             | 53,233               | 57,561     | 98,192             | 111,319    |
| Interest on short-term federal funds sold and securities purchased under agreements to resell | 28                   | 29         | 37                 | 46         |
| Interest on long-term securities purchased under agreements to resell                         | 5,810                | 4,582      | 11,639             | 8,857      |
| Interest on deposits with banks                                                               | 75                   | 112        | 152                | 167        |
| Total interest income                                                                         | 167,255              | 174,624    | 326,000            | 344,590    |
| <b>INTEREST EXPENSE</b>                                                                       |                      |            |                    |            |
| Interest on deposits:                                                                         |                      |            |                    |            |
| Savings, interest checking and money market                                                   | 3,375                | 4,634      | 7,299              | 9,715      |
| Time open and C.D.'s of less than \$100,000                                                   | 1,656                | 2,004      | 3,405              | 4,110      |
| Time open and C.D.'s of \$100,000 and over                                                    | 1,667                | 1,828      | 3,366              | 3,739      |
| Interest on federal funds purchased and securities sold under agreements to repurchase        | 270                  | 177        | 488                | 402        |
| Interest on other borrowings                                                                  | 829                  | 876        | 1,641              | 1,782      |
| Total interest expense                                                                        | 7,797                | 9,519      | 16,199             | 19,748     |
| Net interest income                                                                           | 159,458              | 165,105    | 309,801            | 324,842    |
| Provision for loan losses                                                                     | 7,379                | 5,215      | 10,664             | 13,380     |
| Net interest income after provision for loan losses                                           | 152,079              | 159,890    | 299,137            | 311,462    |
| <b>NON-INTEREST INCOME</b>                                                                    |                      |            |                    |            |
| Bank card transaction fees                                                                    | 40,700               | 38,434     | 79,250             | 73,167     |
| Trust fees                                                                                    | 25,734               | 23,833     | 50,903             | 46,647     |
| Deposit account charges and other fees                                                        | 19,602               | 19,975     | 38,314             | 39,311     |
| Capital market fees                                                                           | 3,305                | 5,010      | 7,696              | 11,881     |
| Consumer brokerage services                                                                   | 2,853                | 2,576      | 5,539              | 5,102      |
| Loan fees and sales                                                                           | 1,314                | 1,706      | 2,787              | 3,267      |
| Other                                                                                         | 9,168                | 9,282      | 18,064             | 16,024     |
| Total non-interest income                                                                     | 102,676              | 100,816    | 202,553            | 195,399    |
| <b>INVESTMENT SECURITIES GAINS (LOSSES), NET</b>                                              |                      |            |                    |            |
| Impairment (losses) reversals on debt securities                                              | (293)                | ) 3        | 1,096              | 5,590      |
| Noncredit-related reversals on securities not expected to be sold                             | (195)                | ) (353)    | (2,026)            | ) (6,260)  |
| Net impairment losses                                                                         | (488)                | ) (350)    | (930)              | ) (670)    |
| Realized gains (losses) on sales and fair value adjustments                                   | (1,080)              | ) 1,686    | (2,803)            | ) 6,046    |
| Investment securities gains (losses), net                                                     | (1,568)              | ) 1,336    | (3,733)            | ) 5,376    |
| <b>NON-INTEREST EXPENSE</b>                                                                   |                      |            |                    |            |
| Salaries and employee benefits                                                                | 89,569               | 87,511     | 180,450            | 177,054    |
| Net occupancy                                                                                 | 11,234               | 11,105     | 22,469             | 22,365     |
| Equipment                                                                                     | 4,680                | 4,999      | 9,363              | 10,188     |
| Supplies and communication                                                                    | 5,797                | 5,667      | 11,386             | 11,280     |
| Data processing and software                                                                  | 19,584               | 18,282     | 38,535             | 35,751     |

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|                                                      |          |          |           |           |
|------------------------------------------------------|----------|----------|-----------|-----------|
| Marketing                                            | 4,048    | 4,469    | 7,407     | 8,291     |
| Deposit insurance                                    | 2,790    | 2,618    | 5,557     | 5,138     |
| Other                                                | 19,264   | 21,689   | 36,836    | 36,734    |
| Total non-interest expense                           | 156,966  | 156,340  | 312,003   | 306,801   |
| Income before income taxes                           | 96,221   | 105,702  | 185,954   | 205,436   |
| Less income taxes                                    | 30,182   | 34,466   | 59,107    | 67,386    |
| Net income                                           | 66,039   | 71,236   | 126,847   | 138,050   |
| Less non-controlling interest expense                | 234      | 503      | 25        | 1,518     |
| Net income attributable to Commerce Bancshares, Inc. | \$65,805 | \$70,733 | \$126,822 | \$136,532 |
| Net income per common share — basic                  | \$.72    | \$.77    | \$1.39    | \$1.47    |
| Net income per common share — diluted                | \$.72    | \$.76    | \$1.39    | \$1.46    |

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<br>Months Ended June<br>30 |          | For the Six Months<br>Ended June 30 |           |
|-------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------|----------|-------------------------------------|-----------|
|                                                                                                                                           | 2013                                     | 2012     | 2013                                | 2012      |
|                                                                                                                                           | (Unaudited)                              |          |                                     |           |
| Net income                                                                                                                                | \$66,039                                 | \$71,236 | \$126,847                           | \$138,050 |
| Other comprehensive income (loss):                                                                                                        |                                          |          |                                     |           |
| Net unrealized gains (losses) on securities for<br>which a portion of an other-than-temporary<br>impairment has been recorded in earnings | (120                                     | )537     | 1,017                               | 3,897     |
| Net unrealized gains (losses) on other<br>securities                                                                                      | (108,254)                                | 17,686   | (116,447)                           | 21,392    |
| Pension loss amortization                                                                                                                 | 475                                      | 453      | 950                                 | 905       |
| Other comprehensive income (loss)                                                                                                         | (107,899)                                | 18,676   | (114,480)                           | 26,194    |
| Comprehensive income (loss)                                                                                                               | (41,860)                                 | 89,912   | 12,367                              | 164,244   |
| Less non-controlling interest expense                                                                                                     | 234                                      | 503      | 25                                  | 1,518     |
| Comprehensive income (loss) attributable to Commerce Bancshares, Inc.                                                                     | \$(42,094)                               | \$89,409 | \$12,342                            | \$162,726 |
| 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)                          | Common Stock | Capital Surplus | Retained Earnings | Treasury Stock | Accumulated                       |                          | Total       |
|----------------------------------------------------------------|--------------|-----------------|-------------------|----------------|-----------------------------------|--------------------------|-------------|
|                                                                |              |                 |                   |                | Other Comprehensive Income (Loss) | Non-Controlling Interest |             |
|                                                                | (Unaudited)  |                 |                   |                |                                   |                          |             |
| Balance January 1, 2013                                        | \$458,646    | \$1,102,507     | \$477,210         | \$(7,580)      | \$136,344                         | \$4,447                  | \$2,171,574 |
| Net income                                                     |              |                 | 126,822           |                |                                   | 25                       | 126,847     |
| Other comprehensive loss                                       |              |                 |                   |                | (114,480)                         |                          | (114,480)   |
| Distributions to non-controlling interest                      |              |                 |                   |                |                                   | (512)                    | (512)       |
| Purchase of treasury stock                                     |              |                 |                   | (45,292)       |                                   |                          | (45,292)    |
| Issuance of stock under purchase and equity compensation plans |              | (2,488)         |                   | 9,047          |                                   |                          | 6,559       |
| Net tax benefit related to equity compensation plans           |              | 209             |                   |                |                                   |                          | 209         |
| Stock-based compensation                                       |              | 2,748           |                   |                |                                   |                          | 2,748       |
| Issuance of nonvested stock awards                             |              | (8,054)         |                   | 8,054          |                                   |                          | —           |
| Cash dividends (\$.450 per share)                              |              |                 | (40,866)          |                |                                   |                          | (40,866)    |
| Balance June 30, 2013                                          | \$458,646    | \$1,094,922     | \$563,166         | \$(35,771)     | \$21,864                          | \$3,960                  | \$2,106,787 |
| Balance January 1, 2012                                        | \$446,387    | \$1,042,065     | \$575,419         | \$(8,362)      | \$110,538                         | \$4,314                  | \$2,170,361 |
| Net income                                                     |              |                 | 136,532           |                |                                   | 1,518                    | 138,050     |
| Other comprehensive income                                     |              |                 |                   |                | 26,194                            |                          | 26,194      |
| Distributions to non-controlling interest                      |              |                 |                   |                |                                   | (1,614)                  | (1,614)     |
| Purchase of treasury stock                                     |              |                 |                   | (71,652)       |                                   |                          | (71,652)    |
| Issuance of stock under purchase and equity compensation plans |              | (3,491)         |                   | 10,276         |                                   |                          | 6,785       |
| Net tax benefit related to equity compensation plans           |              | 744             |                   |                |                                   |                          | 744         |
| Stock-based compensation                                       |              | 2,555           |                   |                |                                   |                          | 2,555       |
| Issuance of nonvested stock awards                             |              | (8,350)         |                   | 8,350          |                                   |                          | —           |
| Cash dividends (\$.438 per share)                              |              |                 | (40,654)          |                |                                   |                          | (40,654)    |
| Balance June 30, 2012                                          | \$446,387    | \$1,033,523     | \$671,297         | \$(61,388)     | \$136,732                         | \$4,218                  | \$2,230,769 |

See accompanying notes to consolidated financial statements.



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Commerce Bancshares, Inc. and Subsidiaries

## CONSOLIDATED STATEMENTS OF CASH FLOWS

| (In thousands)                                                                                        | For the Six Months Ended<br>June 30 |             |
|-------------------------------------------------------------------------------------------------------|-------------------------------------|-------------|
|                                                                                                       | 2013                                | 2012        |
|                                                                                                       | (Unaudited)                         |             |
| <b>OPERATING ACTIVITIES:</b>                                                                          |                                     |             |
| Net income                                                                                            | \$126,847                           | \$138,050   |
| Adjustments to reconcile net income to net cash provided by operating activities:                     |                                     |             |
| Provision for loan losses                                                                             | 10,664                              | 13,380      |
| Provision for depreciation and amortization                                                           | 20,817                              | 21,847      |
| Amortization of investment security premiums, net                                                     | 17,227                              | 16,862      |
| Investment securities (gains) losses, net(A)                                                          | 3,733                               | (5,376 )    |
| Net gains on sales of loans held for sale                                                             | —                                   | (375 )      |
| Proceeds from sales of loans held for sale                                                            | —                                   | 22,508      |
| Net (increase) decrease in trading securities                                                         | 7,465                               | (4,006 )    |
| Stock-based compensation                                                                              | 2,748                               | 2,555       |
| Decrease in interest receivable                                                                       | 116                                 | 4,495       |
| Decrease in interest payable                                                                          | (238 )                              | (185 )      |
| Increase (decrease) in income taxes payable                                                           | (6,719 )                            | 1,999       |
| Net tax benefit related to equity compensation plans                                                  | (209 )                              | (744 )      |
| Other changes, net                                                                                    | (14,546 )                           | (7,617 )    |
| Net cash provided by operating activities                                                             | 167,905                             | 203,393     |
| <b>INVESTING ACTIVITIES:</b>                                                                          |                                     |             |
| Proceeds from sales of investment securities(A)                                                       | 4,096                               | 14,116      |
| Proceeds from maturities/pay downs of investment securities(A)                                        | 1,478,237                           | 1,479,062   |
| Purchases of investment securities(A)                                                                 | (1,309,380)                         | (1,477,434) |
| Net increase in loans                                                                                 | (555,935 )                          | (218,816 )  |
| Long-term securities purchased under agreements to resell                                             | (50,000 )                           | —           |
| Repayments of long-term securities purchased under agreements to resell                               | 50,000                              | —           |
| Purchases of land, buildings and equipment                                                            | (10,713 )                           | (11,703 )   |
| Sales of land, buildings and equipment                                                                | 715                                 | 1,743       |
| Net cash used in investing activities                                                                 | (392,980 )                          | (213,032 )  |
| <b>FINANCING ACTIVITIES:</b>                                                                          |                                     |             |
| Net increase (decrease) in non-interest bearing, savings, interest checking and money market deposits | (863,336 )                          | 335,614     |
| Net increase (decrease) in time open and C.D.'s                                                       | 281,268                             | (277,223 )  |
| Net increase in short-term federal funds purchased and securities sold under agreements to repurchase | 537,144                             | 49,664      |
| Repayment of long-term borrowings                                                                     | (943 )                              | (525 )      |
| Purchases of treasury stock                                                                           | (45,292 )                           | (71,652 )   |
| Issuance of stock under stock purchase and equity compensation plans                                  | 6,559                               | 6,785       |
| Net tax benefit related to equity compensation plans                                                  | 209                                 | 744         |
| Cash dividends paid on common stock                                                                   | (40,866 )                           | (40,654 )   |
| Net cash provided by (used in) financing activities                                                   | (125,257 )                          | 2,753       |
| Decrease in cash and cash equivalents                                                                 | (350,332 )                          | (6,886 )    |
| Cash and cash equivalents at beginning of year                                                        | 779,825                             | 517,551     |
| Cash and cash equivalents at June 30                                                                  | \$429,493                           | \$510,665   |

(A) Available for sale and non-marketable securities

|                                             |          |          |
|---------------------------------------------|----------|----------|
| Income tax payments, net                    | \$65,453 | \$64,799 |
| Interest paid on deposits and borrowings    | \$16,437 | \$19,933 |
| Loans transferred to foreclosed real estate | \$5,532  | \$5,488  |

See accompanying notes to consolidated financial statements.

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Commerce Bancshares, Inc. and Subsidiaries

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2013 (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. All significant intercompany accounts and transactions have been eliminated. Certain reclassifications were made to 2012 data to conform to current year presentation. 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, 2013 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 2012 Annual Report on Form 10-K.

## 2. Acquisition

On May 15, 2013, the Company and Summit Bancshares Inc. (Summit) signed a definitive merger agreement in which the Company will acquire all outstanding shares of Summit. Immediately after the merger, Summit's wholly-owned subsidiary, Summit Bank, will merge into the Bank. The Company's acquisition of Summit will add approximately \$257 million in assets (including \$214 million in loans), \$226 million in deposits, and two branch locations in Tulsa and Oklahoma City. Under the terms of the agreement, if the transaction closes, it is anticipated that the Company will issue approximately 1,000,000 shares of Company common stock. It is anticipated that the transaction will be completed in the third quarter of 2013, pending customary closing conditions, including regulatory approvals and Summit shareholder approval.

## 3. Loans and Allowance for Loan Losses

Major classifications within the Company's held to maturity loan portfolio at June 30, 2013 and December 31, 2012 are as follows:

| (In thousands)                      | June 30, 2013 | December 31, 2012 |
|-------------------------------------|---------------|-------------------|
| Commercial:                         |               |                   |
| Business                            | \$3,415,361   | \$3,134,801       |
| Real estate – construction and land | 398,625       | 355,996           |
| Real estate – business              | 2,210,260     | 2,214,975         |
| Personal Banking:                   |               |                   |
| Real estate – personal              | 1,700,060     | 1,584,859         |
| Consumer                            | 1,450,781     | 1,289,650         |
| Revolving home equity               | 422,902       | 437,567           |
| Consumer credit card                | 760,512       | 804,245           |
| Overdrafts                          | 11,654        | 9,291             |
| Total loans                         | \$10,370,155  | \$9,831,384       |

At June 30, 2013, loans of \$3.4 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 \$1.3 billion were pledged at the Federal Reserve Bank as collateral for discount window borrowings.

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## Allowance for loan losses

A summary of the activity in the allowance for loan losses during the three and six months ended June 30, 2013 and 2012, 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    | \$99,821                           | \$68,211         | \$168,032 | \$105,725                        | \$66,807         | \$172,532 |
| Provision                         | (800)                              | )8,179           | 7,379     | (7,390)                          | )18,054          | 10,664    |
| Deductions:                       |                                    |                  |           |                                  |                  |           |
| Loans charged off                 | 2,261                              | 12,430           | 14,691    | 2,966                            | 24,231           | 27,197    |
| Less recoveries on loans          | 1,839                              | 3,473            | 5,312     | 3,230                            | 6,803            | 10,033    |
| Net loan charge-offs (recoveries) | 422                                | 8,957            | 9,379     | (264)                            | )17,428          | 17,164    |
| Balance June 30, 2013             | \$98,599                           | \$67,433         | \$166,032 | \$98,599                         | \$67,433         | \$166,032 |
| Balance at beginning of period    | \$117,474                          | \$64,058         | \$181,532 | \$122,497                        | \$62,035         | \$184,532 |
| Provision                         | (4,448)                            | )9,663           | 5,215     | (7,646)                          | )21,026          | 13,380    |
| Deductions:                       |                                    |                  |           |                                  |                  |           |
| Loans charged off                 | 3,179                              | 13,841           | 17,020    | 5,707                            | 27,230           | 32,937    |
| Less recoveries on loans          | 4,824                              | 3,982            | 8,806     | 5,527                            | 8,031            | 13,558    |
| Net loan charge-offs (recoveries) | (1,645)                            | )9,859           | 8,214     | 180                              | 19,199           | 19,379    |
| Balance June 30, 2012             | \$114,671                          | \$63,862         | \$178,533 | \$114,671                        | \$63,862         | \$178,533 |

The following table shows the balance in the allowance for loan losses and the related loan balance at June 30, 2013 and December 31, 2012, 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 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 | Outstanding | Allowance for Loan Losses | Outstanding  |
| June 30, 2013     |                           |             |                           |              |
| Commercial        | \$7,548                   | \$76,511    | \$91,051                  | \$5,947,735  |
| Personal Banking  | 2,288                     | 28,906      | 65,145                    | 4,317,003    |
| Total             | \$9,836                   | \$105,417   | \$156,196                 | \$10,264,738 |
| December 31, 2012 |                           |             |                           |              |
| Commercial        | \$5,434                   | \$80,807    | \$100,291                 | \$5,624,965  |
| Personal Banking  | 2,051                     | 36,111      | 64,756                    | 4,089,501    |
| Total             | \$7,485                   | \$116,918   | \$165,047                 | \$9,714,466  |

## Impaired loans

The table below shows the Company's investment in impaired loans at June 30, 2013 and December 31, 2012. 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 under ASC 310-40. 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 13.

(In thousands) June 30, 2013 Dec. 31, 2012

|                               |           |           |
|-------------------------------|-----------|-----------|
| Non-accrual loans             | \$39,092  | \$51,410  |
| Restructured loans (accruing) | 66,325    | 65,508    |
| Total impaired loans          | \$105,417 | \$116,918 |



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The following table provides additional information about impaired loans held by the Company at June 30, 2013 and December 31, 2012, 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<br>Investment | Unpaid<br>Principal<br>Balance | Related<br>Allowance |
|-------------------------------------|------------------------|--------------------------------|----------------------|
| June 30, 2013                       |                        |                                |                      |
| With no related allowance recorded: |                        |                                |                      |
| Business                            | \$7,969                | \$9,000                        | \$—                  |
| Real estate – construction and land | 8,763                  | 16,862                         | —                    |
| Real estate – business              | 6,040                  | 8,802                          | —                    |
| Real estate – personal              | 603                    | 666                            | —                    |
|                                     | \$23,375               | \$35,330                       | \$—                  |
| With an allowance recorded:         |                        |                                |                      |
| Business                            | \$20,185               | \$23,609                       | \$3,054              |
| Real estate – construction and land | 22,395                 | 24,007                         | 2,459                |
| Real estate – business              | 11,159                 | 16,871                         | 2,035                |
| Real estate – personal              | 10,032                 | 12,684                         | 1,183                |
| Consumer                            | 4,418                  | 4,418                          | 86                   |
| Revolving home equity               | 717                    | 717                            | 14                   |
| Consumer credit card                | 13,136                 | 13,136                         | 1,005                |
|                                     | \$82,042               | \$95,442                       | \$9,836              |
| Total                               | \$105,417              | \$130,772                      | \$9,836              |
| December 31, 2012                   |                        |                                |                      |
| With no related allowance recorded: |                        |                                |                      |
| Business                            | \$9,964                | \$12,697                       | \$—                  |
| Real estate – construction and land | 8,440                  | 15,102                         | —                    |
| Real estate – business              | 5,484                  | 8,200                          | —                    |
| Real estate – personal              | 1,166                  | 1,380                          | —                    |
| Revolving home equity               | 510                    | 843                            | —                    |
|                                     | \$25,564               | \$38,222                       | \$—                  |
| With an allowance recorded:         |                        |                                |                      |
| Business                            | \$19,358               | \$22,513                       | \$1,888              |
| Real estate – construction and land | 20,446                 | 25,808                         | 1,762                |
| Real estate – business              | 17,115                 | 23,888                         | 1,784                |
| Real estate – personal              | 14,157                 | 17,304                         | 857                  |
| Consumer                            | 4,779                  | 4,779                          | 93                   |
| Revolving home equity               | 779                    | 779                            | 18                   |
| Consumer credit card                | 14,720                 | 14,720                         | 1,083                |
|                                     | \$91,354               | \$109,791                      | \$7,485              |
| Total                               | \$116,918              | \$148,013                      | \$7,485              |



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Total average impaired loans for the three and six months periods ended June 30, 2013 and 2012, respectively, are shown in the table below.

| (In thousands)                           | Commercial | Personal Banking | Total     |
|------------------------------------------|------------|------------------|-----------|
| Average Impaired Loans:                  |            |                  |           |
| For the three months ended June 30, 2013 |            |                  |           |
| Non-accrual loans                        | \$36,384   | \$4,949          | \$41,333  |
| Restructured loans (accruing)            | 41,053     | 25,141           | 66,194    |
| Total                                    | \$77,437   | \$30,090         | \$107,527 |
| For the six months ended June 30, 2013   |            |                  |           |
| Non-accrual loans                        | \$38,733   | \$5,501          | \$44,234  |
| Restructured loans (accruing)            | 39,854     | 26,210           | 66,064    |
| Total                                    | \$78,587   | \$31,711         | \$110,298 |
| For the three months ended June 30, 2012 |            |                  |           |
| Non-accrual loans                        | \$58,662   | \$7,165          | \$65,827  |
| Restructured loans (accruing)            | 50,102     | 20,324           | 70,426    |
| Total                                    | \$108,764  | \$27,489         | \$136,253 |
| For the six months ended June 30, 2012   |            |                  |           |
| Non-accrual loans                        | \$63,113   | \$7,287          | \$70,400  |
| Restructured loans (accruing)            | 45,164     | 21,939           | 67,103    |
| Total                                    | \$108,277  | \$29,226         | \$137,503 |

The table below shows interest income recognized during the three and six month periods ended June 30, 2013 and 2012 for impaired loans held at the end of each respective period. This interest all relates to accruing restructured loans, as discussed in the "Troubled debt restructurings" section on page 13.

| (In thousands)                                | For the Three Months Ended June 30 |       | For the Six Months Ended June 30 |         |
|-----------------------------------------------|------------------------------------|-------|----------------------------------|---------|
|                                               | 2013                               | 2012  | 2013                             | 2012    |
| Interest income recognized on impaired loans: |                                    |       |                                  |         |
| Business                                      | \$141                              | \$236 | \$282                            | \$471   |
| Real estate – construction and land           | 215                                | 249   | 430                              | 498     |
| Real estate – business                        | 50                                 | 105   | 100                              | 210     |
| Real estate – personal                        | 70                                 | 9     | 139                              | 17      |
| Consumer                                      | 91                                 | 19    | 182                              | 38      |
| Revolving home equity                         | 10                                 | 1     | 19                               | 1       |
| Consumer credit card                          | 253                                | 321   | 506                              | 642     |
| Total                                         | \$830                              | \$940 | \$1,658                          | \$1,877 |



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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, 2013 and December 31, 2012.

| (In thousands)                      | Current or<br>Less Than 30<br>Days Past Due | 30 – 89<br>Days Past<br>Due | 90 Days<br>Past Due<br>and Still<br>Accruing | Non-accrual | Total        |
|-------------------------------------|---------------------------------------------|-----------------------------|----------------------------------------------|-------------|--------------|
| June 30, 2013                       |                                             |                             |                                              |             |              |
| Commercial:                         |                                             |                             |                                              |             |              |
| Business                            | \$3,397,158                                 | \$6,244                     | \$629                                        | \$ 11,330   | \$3,415,361  |
| Real estate – construction and land | 386,625                                     | 1,759                       | 84                                           | 10,157      | 398,625      |
| Real estate – business              | 2,160,535                                   | 36,841                      | 138                                          | 12,746      | 2,210,260    |
| Personal Banking:                   |                                             |                             |                                              |             |              |
| Real estate – personal              | 1,681,776                                   | 10,893                      | 2,532                                        | 4,859       | 1,700,060    |
| Consumer                            | 1,431,476                                   | 17,709                      | 1,596                                        | —           | 1,450,781    |
| Revolving home equity               | 420,727                                     | 1,642                       | 533                                          | —           | 422,902      |
| Consumer credit card                | 744,876                                     | 8,639                       | 6,997                                        | —           | 760,512      |
| Overdrafts                          | 11,283                                      | 371                         | —                                            | —           | 11,654       |
| Total                               | \$10,234,456                                | \$84,098                    | \$12,509                                     | \$ 39,092   | \$10,370,155 |
| December 31, 2012                   |                                             |                             |                                              |             |              |
| Commercial:                         |                                             |                             |                                              |             |              |
| Business                            | \$3,110,403                                 | \$10,054                    | \$1,288                                      | \$ 13,056   | \$3,134,801  |
| Real estate – construction and land | 325,541                                     | 16,721                      | 56                                           | 13,678      | 355,996      |
| Real estate – business              | 2,194,395                                   | 3,276                       | —                                            | 17,304      | 2,214,975    |
| Personal Banking:                   |                                             |                             |                                              |             |              |
| Real estate – personal              | 1,564,281                                   | 10,862                      | 2,854                                        | 6,862       | 1,584,859    |
| Consumer                            | 1,273,581                                   | 13,926                      | 2,143                                        | —           | 1,289,650    |
| Revolving home equity               | 433,437                                     | 2,121                       | 1,499                                        | 510         | 437,567      |
| Consumer credit card                | 786,081                                     | 10,657                      | 7,507                                        | —           | 804,245      |
| Overdrafts                          | 8,925                                       | 366                         | —                                            | —           | 9,291        |
| Total                               | \$9,696,644                                 | \$67,983                    | \$15,347                                     | \$ 51,410   | \$9,831,384  |

## 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, 2013     |             |                          |                      |             |
| Pass              | \$3,302,856 | \$ 356,347               | \$2,092,071          | \$5,751,274 |
| Special mention   | 62,000      | 2,462                    | 50,982               | 115,444     |
| Substandard       | 39,175      | 29,659                   | 54,461               | 123,295     |
| Non-accrual       | 11,330      | 10,157                   | 12,746               | 34,233      |
| Total             | \$3,415,361 | \$ 398,625               | \$2,210,260          | \$6,024,246 |
| December 31, 2012 |             |                          |                      |             |
| Pass              | \$3,018,062 | \$ 297,156               | \$2,103,913          | \$5,419,131 |
| Special mention   | 58,793      | 11,400                   | 38,396               | 108,589     |
| Substandard       | 44,890      | 33,762                   | 55,362               | 134,014     |
| Non-accrual       | 13,056      | 13,678                   | 17,304               | 44,038      |
| Total             | \$3,134,801 | \$ 355,996               | \$2,214,975          | \$5,705,772 |

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 Banking loans for which FICO scores are not obtained because they generally pertain to commercial customer activities and are often underwritten with other collateral considerations. At June 30, 2013, these were comprised of \$228.6 million in personal real estate loans and \$76.1 million in consumer loans, or 7.0% of the Personal Banking portfolio. At December 31, 2012, these were comprised of \$224.5 million in personal real estate loans and \$87.4 million in consumer loans, or 7.6% 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, 2013 and December 31, 2012 by FICO score.

## Personal Banking Loans

|                   | % of Loan Category     |          |                       |                      |   |
|-------------------|------------------------|----------|-----------------------|----------------------|---|
|                   | Real Estate - Personal | Consumer | Revolving Home Equity | Consumer Credit Card |   |
| June 30, 2013     |                        |          |                       |                      |   |
| FICO score:       |                        |          |                       |                      |   |
| Under 600         | 2.0                    | %5.6     | %2.0                  | %4.0                 | % |
| 600 - 659         | 3.1                    | 10.9     | 4.9                   | 11.6                 |   |
| 660 - 719         | 9.8                    | 24.0     | 16.0                  | 33.1                 |   |
| 720 - 779         | 25.6                   | 27.4     | 28.7                  | 28.5                 |   |
| 780 and Over      | 59.5                   | 32.1     | 48.4                  | 22.8                 |   |
| Total             | 100.0                  | %100.0   | %100.0                | %100.0               | % |
| December 31, 2012 |                        |          |                       |                      |   |
| FICO score:       |                        |          |                       |                      |   |
| Under 600         | 2.3                    | %6.7     | %2.6                  | %4.4                 | % |
| 600 - 659         | 3.2                    | 11.3     | 5.3                   | 11.7                 |   |
| 660 - 719         | 10.4                   | 24.4     | 15.2                  | 32.1                 |   |
| 720 - 779         | 26.6                   | 26.4     | 30.0                  | 28.2                 |   |
| 780 and Over      | 57.5                   | 31.2     | 46.9                  | 23.6                 |   |
| Total             | 100.0                  | %100.0   | %100.0                | %100.0               | % |

#### Troubled debt restructurings

As mentioned previously, the Company's impaired loans include loans which have been classified as troubled debt restructurings. Total restructured loans amounted to \$89.5 million at June 30, 2013. 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, and those non-accrual loans totaled \$23.1 million at June 30, 2013. Other performing restructured loans totaled \$66.3 million at June 30, 2013. These are primarily comprised of certain business, construction and business real estate loans classified as substandard. Upon maturity,



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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 commercial loans totaled \$43.5 million at June 30, 2013. 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 \$13.1 million at June 30, 2013. 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 has classified additional loans as troubled debt restructurings because they were not reaffirmed by the borrower in bankruptcy proceedings. At June 30, 2013, these loans totaled \$9.7 million in 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 under the terms of the loan agreements.

The following table shows the outstanding balances of loans classified as troubled debt restructurings at June 30, 2013, 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, 2013 | Balance 90 days<br>past due at any<br>time during<br>previous 12<br>months |
|-------------------------------------|---------------|----------------------------------------------------------------------------|
| Commercial:                         |               |                                                                            |
| Business                            | \$24,929      | \$—                                                                        |
| Real estate - construction and land | 29,946        | 4,403                                                                      |
| Real estate - business              | 8,979         | 3,753                                                                      |
| Personal Banking:                   |               |                                                                            |
| Real estate - personal              | 7,343         | —                                                                          |
| Consumer                            | 4,418         | 104                                                                        |
| Revolving home equity               | 718           | 49                                                                         |
| Consumer credit card                | 13,136        | 789                                                                        |
| Total restructured loans            | \$89,469      | \$9,098                                                                    |

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 \$1.5 million 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 \$11.4 million at June 30, 2013 to lend additional funds to borrowers with restructured loans.

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The Company's holdings of foreclosed real estate totaled \$13.4 million and \$13.5 million at June 30, 2013 and December 31, 2012, respectively. Personal property acquired in repossession, generally autos and marine and recreational vehicles, totaled \$2.3 million and \$3.5 million at June 30, 2013 and December 31, 2012, respectively. These assets are carried at the lower of the amount recorded at acquisition date or the current fair value less estimated costs to sell.

## 4. Investment Securities

Investment securities, at fair value, consisted of the following at June 30, 2013 and December 31, 2012.

| (In thousands)              | June 30, 2013 | Dec. 31,<br>2012 |
|-----------------------------|---------------|------------------|
| Available for sale          | \$8,927,815   | \$9,522,248      |
| Trading                     | 14,670        | 28,837           |
| Non-marketable              | 113,470       | 118,650          |
| Total investment securities | \$9,055,955   | \$9,669,735      |

Most of the Company's investment securities are classified as available for sale, and this portfolio is discussed in more detail below. Securities which are classified as non-marketable include Federal Home Loan Bank (FHLB) stock and Federal Reserve Bank stock held for debt and regulatory purposes, which totaled \$45.4 million at both June 30, 2013 and December 31, 2012. Investment in Federal Reserve Bank 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. Non-marketable securities also include private equity investments, which amounted to \$68.0 million at June 30, 2013 and \$73.2 million at December 31, 2012.

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A summary of the available for sale investment securities by maturity groupings as of June 30, 2013 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. 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. The Company does not have exposure to subprime originated mortgage-backed or collateralized debt obligation instruments.

| (In thousands)                                       | Amortized<br>Cost | Fair Value  |
|------------------------------------------------------|-------------------|-------------|
| U.S. government and federal agency obligations:      |                   |             |
| After 1 but within 5 years                           | \$247,531         | \$265,394   |
| After 5 but within 10 years                          | 80,681            | 86,284      |
| After 10 years                                       | 72,863            | 62,179      |
| Total U.S. government and federal agency obligations | 401,075           | 413,857     |
| Government-sponsored enterprise obligations:         |                   |             |
| Within 1 year                                        | 20,177            | 20,323      |
| After 1 but within 5 years                           | 89,693            | 92,140      |
| After 5 but within 10 years                          | 169,719           | 161,361     |
| After 10 years                                       | 146,967           | 140,994     |
| Total government-sponsored enterprise obligations    | 426,556           | 414,818     |
| State and municipal obligations:                     |                   |             |
| Within 1 year                                        | 103,698           | 104,485     |
| After 1 but within 5 years                           | 698,390           | 716,807     |
| After 5 but within 10 years                          | 564,173           | 554,505     |
| After 10 years                                       | 259,367           | 245,397     |
| Total state and municipal obligations                | 1,625,628         | 1,621,194   |
| Mortgage and asset-backed securities:                |                   |             |
| Agency mortgage-backed securities                    | 2,889,382         | 2,937,002   |
| Non-agency mortgage-backed securities                | 230,729           | 242,432     |
| Asset-backed securities                              | 3,094,715         | 3,088,148   |
| Total mortgage and asset-backed securities           | 6,214,826         | 6,267,582   |
| Other debt securities:                               |                   |             |
| Within 1 year                                        | 38,193            | 38,961      |
| After 1 but within 5 years                           | 45,751            | 45,826      |
| After 5 but within 10 years                          | 86,319            | 80,948      |
| Total other debt securities                          | 170,263           | 165,735     |
| Equity securities                                    | 11,921            | 44,629      |
| Total available for sale investment securities       | \$8,850,269       | \$8,927,815 |

Investments in U.S. government securities are comprised mainly of U.S. Treasury inflation-protected securities (TIPS), which totaled \$413.7 million, at fair value, at June 30, 2013. 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 \$126.8 million, at fair value, of auction rate securities, which were purchased from bank customers in 2008. Included in equity securities is common stock held by the holding company, Commerce Bancshares, Inc. (the Parent), with a fair value of \$35.9 million at June 30, 2013.



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

| (In thousands)                                 | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair Value  |
|------------------------------------------------|-------------------|------------------------------|-------------------------------|-------------|
| June 30, 2013                                  |                   |                              |                               |             |
| U.S. government and federal agency obligations | \$401,075         | \$23,466                     | \$(10,684)                    | \$413,857   |
| Government-sponsored enterprise obligations    | 426,556           | 2,597                        | (14,335)                      | 414,818     |
| State and municipal obligations                | 1,625,628         | 29,529                       | (33,963)                      | 1,621,194   |
| Mortgage and asset-backed securities:          |                   |                              |                               |             |
| Agency mortgage-backed securities              | 2,889,382         | 67,921                       | (20,301)                      | 2,937,002   |
| Non-agency mortgage-backed securities          | 230,729           | 13,400                       | (1,697)                       | 242,432     |
| Asset-backed securities                        | 3,094,715         | 6,742                        | (13,309)                      | 3,088,148   |
| Total mortgage and asset-backed securities     | 6,214,826         | 88,063                       | (35,307)                      | 6,267,582   |
| Other debt securities                          | 170,263           | 1,251                        | (5,779)                       | 165,735     |
| Equity securities                              | 11,921            | 32,708                       | —                             | 44,629      |
| Total                                          | \$8,850,269       | \$177,614                    | \$(100,068)                   | \$8,927,815 |
| December 31, 2012                              |                   |                              |                               |             |
| U.S. government and federal agency obligations | \$399,971         | \$40,395                     | \$(1,607)                     | \$438,759   |
| Government-sponsored enterprise obligations    | 467,063           | 5,188                        | (677)                         | 471,574     |
| State and municipal obligations                | 1,585,926         | 46,076                       | (16,295)                      | 1,615,707   |
| Mortgage and asset-backed securities:          |                   |                              |                               |             |
| Agency mortgage-backed securities              | 3,248,007         | 132,953                      | (5)                           | 3,380,955   |
| Non-agency mortgage-backed securities          | 224,223           | 12,906                       | (118)                         | 237,011     |
| Asset-backed securities                        | 3,152,913         | 15,848                       | (1,367)                       | 3,167,394   |
| Total mortgage and asset-backed securities     | 6,625,143         | 161,707                      | (1,490)                       | 6,785,360   |
| Other debt securities                          | 174,727           | 3,127                        | (102)                         | 177,752     |
| Equity securities                              | 5,695             | 27,401                       | —                             | 33,096      |
| Total                                          | \$9,258,525       | \$283,894                    | \$(20,171)                    | \$9,522,248 |

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/A-, whose fair values have fallen more than 20% below purchase price for an extended period of time, or have been identified based on management's judgment. These securities are placed on a watch list, and for all such securities, 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, 2013, the fair value of securities on this watch list was \$221.8 million compared to \$220.7 million at December 31, 2012.

As of June 30, 2013, 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 \$86.2 million. The cumulative credit-related portion of the impairment initially recorded on these securities totaled \$12.5 million and was recorded in earnings. 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 included the following:

| Significant Inputs           | Range     |
|------------------------------|-----------|
| Prepayment CPR               | 0% - 33%  |
| Projected cumulative default | 16% - 61% |
| Credit support               | 0% - 15%  |
| Loss severity                | 17% - 81% |

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The following table shows changes in the credit losses recorded in earnings during the during the six months ended June 30, 2013 and 2012, for which a portion of an OTTI was recognized in other comprehensive income.

| (In thousands)                                                                      | For the Six Months<br>Ended June 30 |          |
|-------------------------------------------------------------------------------------|-------------------------------------|----------|
|                                                                                     | 2013                                | 2012     |
| Balance at January 1                                                                | \$11,306                            | \$9,931  |
| Credit losses on debt securities for which impairment was previously recognized     | 930                                 | 670      |
| Increase in expected cash flows that are recognized over remaining life of security | (40                                 | )(70     |
| Balance at June 30                                                                  | \$12,196                            | \$10,531 |

Securities with unrealized losses recorded in accumulated other comprehensive income 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, 2013                                  |                     |                   |                     |                   |             |                   |
| U.S. government and federal agency obligations | \$62,179            | \$ 10,684         | \$—                 | \$—               | \$62,179    | \$ 10,684         |
| Government-sponsored enterprise obligations    | 297,058             | 14,335            | —                   | —                 | 297,058     | 14,335            |
| State and municipal obligations                | 580,175             | 21,019            | 81,599              | 12,944            | 661,774     | 33,963            |
| Mortgage and asset-backed securities:          |                     |                   |                     |                   |             |                   |
| Agency mortgage-backed securities              | 609,376             | 20,301            | —                   | —                 | 609,376     | 20,301            |
| Non-agency mortgage-backed securities          | 45,788              | 1,650             | 2,257               | 47                | 48,045      | 1,697             |
| Asset-backed securities                        | 1,832,777           | 11,702            | 104,962             | 1,607             | 1,937,739   | 13,309            |
| Total mortgage and asset-backed securities     | 2,487,941           | 33,653            | 107,219             | 1,654             | 2,595,160   | 35,307            |
| Other debt securities                          | 99,895              | 5,779             | —                   | —                 | 99,895      | 5,779             |
| Total                                          | \$3,527,248         | \$ 85,470         | \$188,818           | \$14,598          | \$3,716,066 | \$100,068         |
| December 31, 2012                              |                     |                   |                     |                   |             |                   |
| U.S. government and federal agency obligations | \$71,464            | \$ 1,607          | \$—                 | \$—               | \$71,464    | \$ 1,607          |
| Government-sponsored enterprise obligations    | 102,082             | 677               | —                   | —                 | 102,082     | 677               |
| State and municipal obligations                | 173,600             | 2,107             | 80,530              | 14,188            | 254,130     | 16,295            |
| Mortgage and asset-backed securities:          |                     |                   |                     |                   |             |                   |
| Agency mortgage-backed securities              | 5,874               | 5                 | —                   | —                 | 5,874       | 5                 |
| Non-agency mortgage-backed securities          | —                   | —                 | 12,609              | 118               | 12,609      | 118               |
| Asset-backed securities                        | 338,007             | 976               | 78,684              | 391               | 416,691     | 1,367             |
| Total mortgage and asset-backed securities     | 343,881             | 981               | 91,293              | 509               | 435,174     | 1,490             |
| Other debt securities                          | 39,032              | 102               | —                   | —                 | 39,032      | 102               |
| Total                                          | \$730,059           | \$ 5,474          | \$171,823           | \$14,697          | \$901,882   | \$20,171          |

The total available for sale portfolio consisted of approximately 1,700 individual securities at June 30, 2013. The portfolio included 507 securities, having an aggregate fair value of \$3.7 billion, that were in an unrealized loss position at June 30, 2013, compared to 144 securities, with a fair value of \$901.9 million, at December 31, 2012. The total amount of unrealized loss on these securities increased \$79.9 million to \$100.1 million at June 30, 2013, which was mainly due to a recent rise in interest rates. At June 30, 2013, the fair value of securities in an unrealized loss position for 12 months or longer with temporary impairment totaled \$186.6 million, or 2.1% of the total portfolio value, and the fair value of other securities with other-than-temporary impairment totaled \$2.3 million.





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The Company's holdings of state and municipal obligations included gross unrealized losses of \$34.0 million at June 30, 2013. Of these losses, \$12.9 million related to auction rate securities and \$21.0 million related to other state and municipal obligations. This portfolio, exclusive of ARS, totaled \$1.5 billion at fair value, or 16.7% of total available for sale securities. The average credit quality of the portfolio, excluding ARS, is Aa2 as rated by Moody's. The portfolio is diversified in order to reduce risk, and information about the top five largest holdings, by state and economic sector, is shown in the table below. The Company does not have exposure to obligations of Detroit, Michigan, which recently filed for Chapter 9 bankruptcy. The Company has processes and procedures in place to monitor its holdings, identify signs of financial distress and, if necessary, exit its positions in a timely manner.

|                    | % of Portfolio | Average Life (in years) | Average Rating (Moody's) |
|--------------------|----------------|-------------------------|--------------------------|
| At June 30, 2013   |                |                         |                          |
| Texas              | 9.8            | 5.3                     | Aa1                      |
| Florida            | 9.4            | 4.8                     | Aa2                      |
| Ohio               | 5.7            | 5.3                     | Aa2                      |
| Washington         | 5.5            | 4.8                     | Aa2                      |
| New York           | 5.1            | 6.7                     | Aa2                      |
| General obligation | 31.7           | 4.8                     | Aa2                      |
| Housing            | 17.5           | 6.4                     | Aa1                      |
| Lease              | 16.7           | 4.9                     | Aa2                      |
| Transportation     | 13.5           | 4.5                     | Aa3                      |
| Limited tax        | 5.1            | 5.5                     | Aa1                      |

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

| (In thousands)                                                | For the Six Months Ended June 30 |          |
|---------------------------------------------------------------|----------------------------------|----------|
|                                                               | 2013                             | 2012     |
| Proceeds from sales of available for sale securities          | \$—                              | \$4,951  |
| Proceeds from sales of non-marketable securities              | 4,096                            | 9,165    |
| Total proceeds                                                | \$4,096                          | \$14,116 |
| Available for sale:                                           |                                  |          |
| Gains realized on sales                                       | \$—                              | \$342    |
| Gain realized on donation                                     | 1,375                            | —        |
| Other-than-temporary impairment recognized on debt securities | (930)                            | (670)    |
| Non-marketable:                                               |                                  |          |
| Gains realized on sales                                       | 603                              | 304      |
| Losses realized on sales                                      | (2,979)                          | (200)    |
| Fair value adjustments, net                                   | (1,802)                          | 5,600    |
| Investment securities gains (losses), net                     | \$(3,733)                        | \$5,376  |

At June 30, 2013, securities totaling \$4.6 billion in fair value were pledged to secure public fund deposits, securities sold under agreements to repurchase, trust funds, and borrowings at the Federal Reserve Bank and FHLB. Securities pledged under agreements pursuant to which the collateral may be sold or re-pledged by the secured parties approximated \$746.1 million, while the remaining securities were pledged under agreements pursuant to which the secured parties may not sell or re-pledge the collateral. Except for obligations of various government-sponsored enterprises such as FNMA, FHLB and FHLMC, no investment in a single issuer exceeded 10% of stockholders' equity.



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## 5. Goodwill and Other Intangible Assets

The following table presents information about the Company's intangible assets which have estimable useful lives.

| (In thousands)                 | June 30, 2013         |                          |                     |            | December 31, 2012     |                          |                     |            |
|--------------------------------|-----------------------|--------------------------|---------------------|------------|-----------------------|--------------------------|---------------------|------------|
|                                | Gross Carrying Amount | Accumulated Amortization | Valuation Allowance | Net Amount | Gross Carrying Amount | Accumulated Amortization | Valuation Allowance | Net Amount |
| Amortizable intangible assets: |                       |                          |                     |            |                       |                          |                     |            |
| Core deposit premium           | \$25,720              | \$(21,805)               | \$—                 | \$3,915    | \$25,720              | \$(20,892)               | \$—                 | \$4,828    |
| Mortgage servicing rights      | 3,251                 | (2,443)                  | (206)               | 602        | 3,132                 | (2,267)                  | (393)               | 472        |
| Total                          | \$28,971              | \$(24,248)               | \$(206)             | \$4,517    | \$28,852              | \$(23,159)               | \$(393)             | \$5,300    |

Aggregate amortization expense on intangible assets was \$532 thousand and \$669 thousand, respectively, for the three month periods ended June 30, 2013 and 2012 and \$1.1 million and \$1.4 million, respectively, for the six month periods ended June 30, 2013 and 2012. The following table shows the estimated annual amortization expense for the next five fiscal years. This expense is based on existing asset balances and the interest rate environment as of June 30, 2013. The Company's actual amortization expense in any given period may be different from the estimated amounts depending upon the acquisition of intangible assets, changes in mortgage interest rates, prepayment rates and other market conditions.

(In thousands)

|      |         |
|------|---------|
| 2013 | \$1,730 |
| 2014 | 1,265   |
| 2015 | 928     |
| 2016 | 619     |
| 2017 | 349     |

Changes in the carrying amount of goodwill and net other intangible assets for the six month period ended June 30, 2013 is as follows.

| (In thousands)          | Goodwill  | Core Deposit Premium | Mortgage Servicing Rights |
|-------------------------|-----------|----------------------|---------------------------|
| Balance January 1, 2013 | \$125,585 | \$4,828              | \$472                     |
| Originations            | —         | —                    | 119                       |
| Amortization            | —         | (913)                | (176)                     |
| Impairment reversal     | —         | —                    | 187                       |
| Balance June 30, 2013   | \$125,585 | \$3,915              | \$602                     |

Goodwill allocated to the Company's operating segments at June 30, 2013 and December 31, 2012 is shown below.

(In thousands)

|                    |           |
|--------------------|-----------|
| Consumer segment   | \$67,765  |
| Commercial segment | 57,074    |
| Wealth segment     | 746       |
| Total goodwill     | \$125,585 |

## 6. Guarantees

The Company, as a provider of financial services, routinely issues financial guarantees in the form of financial and performance standby letters of credit. Standby letters of credit are contingent commitments issued by the Company generally to guarantee the payment or performance obligation of a customer to a third party. While these represent a potential outlay by the Company, a significant amount of the commitments may expire without being drawn upon. The Company has recourse against the customer for any amount it is required to pay to a third party under a standby letter of credit. The letters of credit are subject to the same credit policies, underwriting standards and approval process as loans made by the Company. Most of the standby letters of credit are secured, and in the event of nonperformance by customers, the Company has rights to the underlying collateral, which could include commercial real estate, physical plant and property, inventory, receivables, cash and marketable securities.

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Upon issuance of standby letters of credit, the Company recognizes a liability for the fair value of the obligation undertaken, which is estimated to be equivalent to the amount of fees received from the customer over the life of the agreement. At June 30, 2013 that net liability was \$3.9 million, which will be accreted into income over the remaining life of the respective commitments. The contractual amount of these letters of credit, which represents the maximum potential future payments guaranteed by the Company, was \$330.0 million at June 30, 2013.

The Company periodically enters into risk participation agreements (RPAs) as a guarantor to other financial institutions, in order to mitigate those institutions' credit risk associated with interest rate swaps with third parties. The RPA stipulates that, in the event of default by the third party on the interest rate swap, the Company will reimburse a portion of the loss borne by the financial institution. These interest rate swaps are normally collateralized (generally with real property, inventories and equipment) by the third party, which limits the credit risk associated with the Company's RPAs. The third parties usually have other borrowing relationships with the Company. The Company monitors overall borrower collateral, and at June 30, 2013, believes sufficient collateral is available to cover potential swap losses. The RPAs are carried at fair value throughout their term, with all changes in fair value, including those due to a change in the third party's creditworthiness, recorded in current earnings. The terms of the RPAs, which correspond to the terms of the underlying swaps, range from 4 to 10 years. At June 30, 2013, the liability recorded for guarantor RPAs was \$98 thousand, and the notional amount of the underlying swaps was \$42.3 million. The maximum potential future payment guaranteed by the Company cannot be readily estimated but is dependent upon the fair value of the interest rate swaps at the time of default.

## 7. Pension

The amount of net pension cost is shown in the table below:

| (In thousands)                                   | For the Three<br>Months Ended June<br>30 |         | For the Six Months<br>Ended June 30 |         |
|--------------------------------------------------|------------------------------------------|---------|-------------------------------------|---------|
|                                                  | 2013                                     | 2012    | 2013                                | 2012    |
| Service cost - benefits earned during the period | \$131                                    | \$104   | \$263                               | \$207   |
| Interest cost on projected benefit obligation    | 1,123                                    | 1,286   | 2,245                               | 2,573   |
| Expected return on plan assets                   | (1,608)                                  | (1,645) | (3,217)                             | (3,290) |
| Amortization of unrecognized net loss            | 766                                      | 730     | 1,533                               | 1,460   |
| Net periodic pension cost                        | \$412                                    | \$475   | \$824                               | \$950   |

Substantially all benefits accrued under the Company's defined benefit pension plan were frozen effective January 1, 2005, and the remaining benefits were frozen effective January 1, 2011. During 2012, the Company made a discretionary contribution of \$1.5 million to its defined benefit pension plan in order to reduce pension guarantee premiums but has made no subsequent contributions to the defined benefit plan in 2013. The Company also made minimal funding contributions to a supplemental executive retirement plan (the CERP), which carries no segregated assets. The Company has no plans to make any further contributions, other than those related to the CERP, during the remainder of 2013.

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## 8. Common Stock

Presented below is a summary of the components used to calculate basic and diluted income per share. The Company applies the two-class method of computing income per share, as nonvested share-based awards that contain nonforfeitable rights to dividends are considered securities which participate in undistributed earnings with common stock. The two-class method requires the calculation of separate income per share amounts for the nonvested share-based awards and for common stock. Income per share attributable to common stock is shown in the table below. Nonvested share-based awards are further discussed in Note 13.

|                                                                                                                                                         | For the Three<br>Months Ended<br>June 30 |          | For the Six Months<br>Ended June 30 |           |
|---------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------|----------|-------------------------------------|-----------|
|                                                                                                                                                         | 2013                                     | 2012     | 2013                                | 2012      |
| (In thousands, except per share data)                                                                                                                   |                                          |          |                                     |           |
| Basic income per common share:                                                                                                                          |                                          |          |                                     |           |
| Net income attributable to Commerce Bancshares, Inc.                                                                                                    | \$65,805                                 | \$70,733 | \$126,822                           | \$136,532 |
| Less income allocated to nonvested restricted stock                                                                                                     | 750                                      | 666      | 1,344                               | 1,228     |
| Net income allocated to common stock                                                                                                                    | \$65,055                                 | \$70,067 | \$125,478                           | \$135,304 |
| Weighted average common shares outstanding                                                                                                              | 89,784                                   | 91,774   | 89,996                              | 92,203    |
| Basic income per common share                                                                                                                           | \$.72                                    | \$.77    | \$1.39                              | \$1.47    |
| Diluted income per common share:                                                                                                                        |                                          |          |                                     |           |
| Net income attributable to Commerce Bancshares, Inc.                                                                                                    | \$65,805                                 | \$70,733 | \$126,822                           | \$136,532 |
| Less income allocated to nonvested restricted stock                                                                                                     | 747                                      | 665      | 1,340                               | 1,226     |
| Net income allocated to common stock                                                                                                                    | \$65,058                                 | \$70,068 | \$125,482                           | \$135,306 |
| Weighted average common shares outstanding                                                                                                              | 89,784                                   | 91,774   | 89,996                              | 92,203    |
| Net effect of the assumed exercise of stock-based awards - based on the treasury stock method using the average market price for the respective periods | 375                                      | 282      | 305                                 | 317       |
| Weighted average diluted common shares outstanding                                                                                                      | 90,159                                   | 92,056   | 90,301                              | 92,520    |
| Diluted income per common share                                                                                                                         | \$.72                                    | \$.76    | \$1.39                              | \$1.46    |

Nearly all unexercised stock options and stock appreciation rights were included in the computations of diluted income per share for the six month periods ended June 30, 2013 and 2012.

## 9. Accumulated Other Comprehensive Income

The table below shows the activity and accumulated balances for components of other comprehensive income. The largest component is the unrealized holding gains and losses on available for sale securities. Unrealized gains and losses on debt securities for which an other-than-temporary impairment (OTTI) has been recorded in current earnings are shown separately below. The other component is the amortization from other comprehensive income of losses associated with pension benefits, which occurs as the losses are included in current net periodic pension cost.

| (In thousands)                                                   | Unrealized Gains (Losses)<br>on Securities (1) |            | Pension Loss<br>(2) | Total<br>Accumulated<br>Other<br>Comprehensive<br>Income |
|------------------------------------------------------------------|------------------------------------------------|------------|---------------------|----------------------------------------------------------|
|                                                                  | OTTI                                           | Other      |                     |                                                          |
| Balance January 1, 2013                                          | \$3,245                                        | \$160,263  | \$(27,164)          | )\$136,344                                               |
| Other comprehensive income before reclassifications              | 710                                            | (186,443)  | )—                  | (185,733)                                                |
| Amounts reclassified from accumulated other comprehensive income | 930                                            | (1,375)    | )1,533              | 1,088                                                    |
| Current period other comprehensive income (loss), before tax     | 1,640                                          | (187,818)  | )1,533              | (184,645)                                                |
| Income tax (expense) benefit                                     | (623)                                          | )71,371    | (583)               | )70,165                                                  |
| Current period other comprehensive income (loss), net of tax     | 1,017                                          | (116,447)  | )950                | (114,480)                                                |
| Balance June 30, 2013                                            | \$4,262                                        | \$43,816   | \$(26,214)          | )\$21,864                                                |
| Balance January 1, 2012                                          | \$(4,321)                                      | )\$136,137 | \$(21,278)          | )\$110,538                                               |
| Other comprehensive income before reclassifications              | 5,616                                          | 34,845     | —                   | 40,461                                                   |
| Amounts reclassified from accumulated other comprehensive income | 670                                            | (342)      | )1,460              | 1,788                                                    |
| Current period other comprehensive income, before tax            | 6,286                                          | 34,503     | 1,460               | 42,249                                                   |
| Income tax expense                                               | (2,389)                                        | ) (13,111) | ) (555)             | ) (16,055)                                               |
| Current period other comprehensive income, net of tax            | 3,897                                          | 21,392     | 905                 | 26,194                                                   |
| Balance June 30, 2012                                            | \$(424)                                        | )\$157,529 | \$(20,373)          | )\$136,732                                               |

(1) The pre-tax amounts reclassified from accumulated other comprehensive income are included in "investment securities gains (losses), net" in the consolidated statements of income.

(2) The pre-tax amounts reclassified from accumulated other comprehensive income are included in the computation of net periodic pension cost as "amortization of unrecognized net loss" (see Note 7).

## 10. Segments

The Company segregates financial information for use in assessing its performance and allocating resources among three operating segments: Consumer, Commercial and Wealth. The Consumer segment includes the consumer portion of the retail branch network (loans, deposits, and other personal banking services), indirect and other consumer financing, and consumer debit and credit bank cards. The Commercial segment provides corporate lending (including the Small Business Banking product line within the branch network), leasing, international services, and business, government deposit, and related commercial cash management services, as well as merchant and commercial bank card products. The Commercial segment includes the Capital Markets Group, which sells fixed income securities and provides investment safekeeping and bond accounting services. The Wealth segment provides traditional trust and estate tax planning, advisory and discretionary investment management, and brokerage services, and includes the Private Banking product portfolio.



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The following table presents selected financial information by segment and reconciliations of combined segment totals to consolidated totals. There were no material intersegment revenues among the three segments. Management periodically makes changes to methods of assigning costs and income to its business segments to better reflect operating results. If appropriate, these changes are reflected in prior year information presented below.

| (In thousands)                          | Consumer  | Commercial | Wealth   | Segment<br>Totals | Other/<br>Elimination | Consolidated<br>Totals |
|-----------------------------------------|-----------|------------|----------|-------------------|-----------------------|------------------------|
| <b>Three Months Ended June 30, 2013</b> |           |            |          |                   |                       |                        |
| Net interest income                     | \$66,883  | \$ 69,098  | \$9,781  | \$145,762         | \$ 13,696             | \$ 159,458             |
| Provision for loan losses               | (8,670)   | (617)      | (92)     | (9,379)           | 2,000                 | (7,379)                |
| Non-interest income                     | 28,405    | 45,105     | 29,630   | 103,140           | (464)                 | 102,676                |
| Investment securities losses, net       | —         | —          | —        | —                 | (1,568)               | (1,568)                |
| Non-interest expense                    | (68,965)  | (59,076)   | (23,649) | (151,690)         | (5,276)               | (156,966)              |
| Income before income taxes              | \$17,653  | \$ 54,510  | \$15,670 | \$87,833          | \$ 8,388              | \$ 96,221              |
| <b>Six Months Ended June 30, 2013</b>   |           |            |          |                   |                       |                        |
| Net interest income                     | \$134,096 | \$ 140,057 | \$20,111 | \$294,264         | \$ 15,537             | \$ 309,801             |
| Provision for loan losses               | (16,881)  | (128)      | (140)    | (17,149)          | 6,485                 | (10,664)               |
| Non-interest income                     | 55,130    | 89,611     | 58,333   | 203,074           | (521)                 | 202,553                |
| Investment securities losses, net       | —         | —          | —        | —                 | (3,733)               | (3,733)                |
| Non-interest expense                    | (136,876) | (117,983)  | (47,957) | (302,816)         | (9,187)               | (312,003)              |
| Income before income taxes              | \$35,469  | \$ 111,557 | \$30,347 | \$177,373         | \$ 8,581              | \$ 185,954             |
| <b>Three Months Ended June 30, 2012</b> |           |            |          |                   |                       |                        |
| Net interest income                     | \$68,561  | \$ 72,746  | \$9,708  | \$151,015         | \$ 14,090             | \$ 165,105             |
| Provision for loan losses               | (9,153)   | (1,543)    | (510)    | (8,120)           | 2,905                 | (5,215)                |
| Non-interest income                     | 28,259    | 44,944     | 27,221   | 100,424           | 392                   | 100,816                |
| Investment securities gains, net        | —         | —          | —        | —                 | 1,336                 | 1,336                  |
| Non-interest expense                    | (67,148)  | (56,082)   | (22,244) | (145,474)         | (10,866)              | (156,340)              |
| Income before income taxes              | \$20,519  | \$ 63,151  | \$14,175 | \$97,845          | \$ 7,857              | \$ 105,702             |
| <b>Six Months Ended June 30, 2012</b>   |           |            |          |                   |                       |                        |
| Net interest income                     | \$137,654 | \$ 144,275 | \$19,465 | \$301,394         | \$ 23,448             | \$ 324,842             |
| Provision for loan losses               | (18,460)  | (288)      | (552)    | (19,300)          | 5,920                 | (13,380)               |
| Non-interest income                     | 55,447    | 87,838     | 53,376   | 196,661           | (1,262)               | 195,399                |
| Investment securities gains, net        | —         | —          | —        | —                 | 5,376                 | 5,376                  |
| Non-interest expense                    | (133,263) | (112,051)  | (45,011) | (290,325)         | (16,476)              | (306,801)              |
| Income before income taxes              | \$41,378  | \$ 119,774 | \$27,278 | \$188,430         | \$ 17,006             | \$ 205,436             |

The information presented above was derived from the internal profitability reporting system used by management to monitor and manage the financial performance of the Company. This information is based on internal management accounting policies, which have been developed to reflect the underlying economics of the businesses. The policies address the methodologies applied in connection with funds transfer pricing and assignment of overhead costs among segments. Funds transfer pricing was used in the determination of net interest income by assigning a standard cost (credit) for funds used (provided) by assets and liabilities based on their maturity, prepayment and/or repricing characteristics.

The segment activity, as shown above, includes both direct and allocated items. Amounts in the “Other/Elimination” column include activity not related to the segments, such as that relating to administrative functions, the investment securities portfolio, and the effect of certain expense allocations to the segments. The provision for loan losses in this category contains the difference between net loan charge-offs assigned directly to the segments and the recorded provision for loan loss expense. Included in this category’s net interest income are earnings of the investment portfolio, which are not allocated to a segment.

The performance measurement of the operating segments is based on the management structure of the Company and is not necessarily comparable with similar information for any other financial institution. The information is also not necessarily indicative of the segments' financial condition and results of operations if they were independent entities.

#### 11. Derivative Instruments

The notional amounts of the Company's derivative instruments are shown in the table below. These contractual amounts, along with other terms of the derivative, are used to determine amounts to be exchanged between counterparties and are not a measure of loss exposure. The largest group of notional amounts relate to interest rate swaps, which are discussed in more detail

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below. The Company also contracts with other financial institutions, as a guarantor or beneficiary, to share credit risk associated with certain interest rate swaps through risk participation agreements. The Company's risks and responsibilities as guarantor are further discussed in Note 6 on Guarantees.

Through its International Department, the Company enters into foreign exchange contracts consisting mainly of contracts to purchase or deliver foreign currencies for customers at specific future dates. This activity increased in 2013 due to higher customer demand. Also, the Company's past practice of originating and selling fixed rate personal real estate loans to other institutions historically resulted in mortgage loan commitments and forward sales contracts. In late 2011, the Company curtailed the sales of these types of loans and did not hold such loans for sale at June 30, 2013 or December 31, 2012.

| (In thousands)                       | June 30,<br>2013 | December 31,<br>2012 |
|--------------------------------------|------------------|----------------------|
| Interest rate swaps                  | \$431,485        | \$435,542            |
| Interest rate caps                   | 10,736           | 27,736               |
| Credit risk participation agreements | 45,551           | 43,243               |
| Foreign exchange contracts           | 99,256           | 47,897               |
| Total notional amount                | \$587,028        | \$554,418            |

The Company's interest rate risk management strategy includes the ability to modify the repricing characteristics of certain assets and liabilities so that changes in interest rates do not adversely affect the net interest margin and cash flows. Interest rate swaps are used on a limited basis as part of this strategy. At June 30, 2013, the Company had entered into three interest rate swaps with a notional amount of \$12.5 million, included in the table above, which are designated as fair value hedges of certain fixed rate loans. Gains and losses on these derivative instruments, as well as the offsetting loss or gain on the hedged loans attributable to the hedged risk, are recognized in current earnings. These gains and losses are reported in interest and fees on loans in the accompanying statements of income. The table below shows gains and losses related to fair value hedges.

| (In thousands)                     | For the Three<br>Months Ended<br>June 30 |      | For the Six Months<br>Ended June 30 |       |
|------------------------------------|------------------------------------------|------|-------------------------------------|-------|
|                                    | 2013                                     | 2012 | 2013                                | 2012  |
| Gain (loss) on interest rate swaps | \$105                                    | \$57 | \$230                               | \$145 |
| Gain (loss) on loans               | (102)                                    | (50) | (224)                               | (135) |
| Amount of hedge ineffectiveness    | \$3                                      | \$7  | \$6                                 | \$10  |

The Company's other derivative instruments are accounted for as free-standing derivatives, and changes in their fair value are recorded in current earnings. These instruments include interest rate swap contracts sold to customers who wish to modify their interest rate sensitivity. These swaps are offset by matching contracts purchased by the Company from other financial institutions. Because of the matching terms of the offsetting contracts, in addition to collateral provisions which mitigate the impact of non-performance risk, changes in fair value subsequent to initial recognition have a minimal effect on earnings. The notional amount of these types of swaps at June 30, 2013 was \$419.0 million. The Company is party to master netting arrangements with many of its derivative counterparties; however, the Company does not offset assets and liabilities under these arrangements for balance sheet presentation, as the effect of offsetting is not significant. Additional information about the potential effects of offsetting and collateral amounts pledged by the Company is provided in Note 12 on Balance Sheet Offsetting.

Many of the Company's interest rate swap contracts with large financial institutions contain contingent features relating to debt ratings or capitalization levels. Under these provisions, if the Company's debt rating falls below investment grade or if the Company ceases to be "well-capitalized" under risk-based capital guidelines, certain counterparties can require immediate and ongoing collateralization on interest rate swaps in net liability positions or

can require instant settlement of the contracts. The Company maintains debt ratings and capital well above these minimum requirements.

The banking customer counterparties are engaged in a variety of businesses, including real estate, building materials, education, financial services, communications, consumer products, and manufacturing. At June 30, 2013, the largest loss exposures were in the groups related to education, real estate, and manufacturing. If the counterparties in these groups failed to perform, and if the underlying collateral proved to be of no value, the Company estimates that it would incur losses of \$2.8 million (education), \$2.5 million (real estate and building materials) and \$1.7 million (manufacturing) at June 30, 2013.

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The fair values of the Company's derivative instruments, whose notional amounts are listed above, are shown in the table below. Information about the valuation methods used to determine fair value is provided in Note 14 on Fair Value Measurements.

| (In thousands)                                          | Asset Derivatives      |                          |                          | Liability Derivatives  |                          |                          |
|---------------------------------------------------------|------------------------|--------------------------|--------------------------|------------------------|--------------------------|--------------------------|
|                                                         | Balance Sheet Location | June 30, 2013 Fair Value | Dec. 31, 2012 Fair Value | Balance Sheet Location | June 30, 2013 Fair Value | Dec. 31, 2012 Fair Value |
| Derivatives designated as hedging instruments:          |                        |                          |                          |                        |                          |                          |
| Interest rate swaps                                     | Other assets           | \$—                      | \$—                      | Other liabilities      | \$(492)                  | \$(723)                  |
| Total derivatives designated as hedging instruments     |                        | \$—                      | \$—                      |                        | \$(492)                  | \$(723)                  |
| Derivatives not designated as hedging instruments:      |                        |                          |                          |                        |                          |                          |
| Interest rate swaps                                     | Other assets           | \$11,767                 | \$16,334                 | Other liabilities      | \$(11,769)               | \$(16,337)               |
| Interest rate caps                                      | Other assets           | 1                        | 1                        | Other liabilities      | (1)                      | (1)                      |
| Credit risk participation agreements                    | Other assets           | 5                        | 9                        | Other liabilities      | (98)                     | (196)                    |
| Foreign exchange contracts                              | Other assets           | 909                      | 396                      | Other liabilities      | (889)                    | (461)                    |
| Total derivatives not designated as hedging instruments |                        | \$12,682                 | \$16,740                 |                        | \$(12,757)               | \$(16,995)               |
| Total derivatives                                       |                        | \$12,682                 | \$16,740                 |                        | \$(13,249)               | \$(17,718)               |

The effects of derivative instruments on the consolidated statements of income are shown in the table below.

| (In thousands)                                     | Location of Gain or (Loss) Recognized in Income on Derivatives | Amount of Gain or (Loss) Recognized in Income on Derivatives |       |                                  |       |
|----------------------------------------------------|----------------------------------------------------------------|--------------------------------------------------------------|-------|----------------------------------|-------|
|                                                    |                                                                | For the Three Months Ended June 30                           |       | For the Six Months Ended June 30 |       |
|                                                    |                                                                | 2013                                                         | 2012  | 2013                             | 2012  |
| Derivatives in fair value hedging relationships:   |                                                                |                                                              |       |                                  |       |
| Interest rate swaps                                | Interest and fees on loans                                     | \$105                                                        | \$57  | \$230                            | \$145 |
| Total                                              |                                                                | \$105                                                        | \$57  | \$230                            | \$145 |
| Derivatives not designated as hedging instruments: |                                                                |                                                              |       |                                  |       |
| Interest rate swaps                                | Other non-interest income                                      | \$155                                                        | \$81  | \$294                            | \$198 |
| Credit risk participation agreements               | Other non-interest income                                      | 69                                                           | 7     | 125                              | 5     |
| Foreign exchange contracts                         | Other non-interest income                                      | (62)                                                         | 147   | 85                               | 7     |
| Mortgage loan commitments                          | Loan fees and sales                                            | —                                                            | —     | —                                | (20)  |
| Mortgage loan forward sale contracts               | Loan fees and sales                                            | —                                                            | —     | —                                | 11    |
| Total                                              |                                                                | \$162                                                        | \$235 | \$504                            | \$201 |

## 12. Balance Sheet Offsetting

The following tables show the extent to which assets and liabilities relating to derivative instruments, securities purchased under agreements to resell (resell agreements), and securities sold under agreements to repurchase (repurchase agreements) have been offset in the consolidated balance sheets. They also provide information about these instruments which are subject to an enforceable master netting arrangement, irrespective of whether they are offset, and the extent to which the instruments could potentially be offset. Also shown is collateral received or pledged in the form of other financial instruments, which are generally marketable securities. The collateral amounts in these tables are limited to the outstanding balances of the related asset or liability (after netting is applied); thus instances of overcollateralization are not shown. Most of the assets and liabilities in the following tables were transacted under master netting arrangements that contain a conditional right of offset, such as close-out netting, upon default.

The financial collateral securing these arrangements consists of marketable securities. These are valued daily, and adjustments to amounts received and pledged by the Company are made as appropriate to maintain proper collateralization for these transactions. Collateral posted by the Company to financial institution counterparties under derivative contracts is generally subject to thresholds and transfer minimums. By contract, it may be sold or re-pledged by the secured party until recalled at a subsequent valuation date by the pledging party. Derivative transactions with customers are generally secured by non-financial collateral, such as real and personal property, which is not shown in the table below. Collateral accepted or pledged in resell and repurchase agreements with other financial institutions also may be sold or re-pledged by the secured party, but is usually delivered to and held by third party trustees. The Company generally retains custody of securities pledged for repurchase agreements with customers.

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| (In thousands)                                                      | Gross Amount Recognized | Gross Amounts Offset in the Balance Sheet | Net Amounts Presented in the Balance Sheet | Gross Amounts Not Offset in the Balance Sheet |                                        |            |
|---------------------------------------------------------------------|-------------------------|-------------------------------------------|--------------------------------------------|-----------------------------------------------|----------------------------------------|------------|
|                                                                     |                         |                                           |                                            | Financial Instruments                         | Securities Collateral Received/Pledged | Net Amount |
| June 30, 2013                                                       |                         |                                           |                                            |                                               |                                        |            |
| Assets:                                                             |                         |                                           |                                            |                                               |                                        |            |
| Derivatives subject to master netting agreements                    | \$12,334                | \$—                                       | \$12,334                                   | \$(1,022                                      | ) \$ —                                 | \$11,312   |
| Derivatives not subject to master netting agreements                | 348                     | —                                         | 348                                        |                                               |                                        |            |
| Total derivatives                                                   | 12,682                  | —                                         | 12,682                                     |                                               |                                        |            |
| Total resell agreements, subject to master netting arrangements     | 1,500,000               | (300,000                                  | ) 1,200,000                                | —                                             | (1,200,000                             | ) —        |
| Liabilities:                                                        |                         |                                           |                                            |                                               |                                        |            |
| Derivatives subject to master netting agreements                    | 12,738                  | —                                         | 12,738                                     | (1,022                                        | ) (10,493                              | ) 1,223    |
| Derivatives not subject to master netting agreements                | 511                     | —                                         | 511                                        |                                               |                                        |            |
| Total derivatives                                                   | 13,249                  | —                                         | 13,249                                     |                                               |                                        |            |
| Total repurchase agreements, subject to master netting arrangements | 1,284,334               | (300,000                                  | ) 984,334                                  | —                                             | (984,334                               | ) —        |
| December 31, 2012                                                   |                         |                                           |                                            |                                               |                                        |            |
| Assets:                                                             |                         |                                           |                                            |                                               |                                        |            |
| Derivatives subject to master netting agreements                    | \$16,475                | \$—                                       | \$16,475                                   | \$(603                                        | ) \$ —                                 | \$15,872   |
| Derivatives not subject to master netting agreements                | 265                     | —                                         | 265                                        |                                               |                                        |            |
| Total derivatives                                                   | 16,740                  | —                                         | 16,740                                     |                                               |                                        |            |
| Total resell agreements, subject to master netting arrangements     | 1,500,000               | (300,000                                  | ) 1,200,000                                | —                                             | (1,200,000                             | ) —        |
| Liabilities:                                                        |                         |                                           |                                            |                                               |                                        |            |
| Derivatives subject to master netting agreements                    | 17,315                  | —                                         | 17,315                                     | (603                                          | ) (16,017                              | ) 695      |
| Derivatives not subject to master netting agreements                | 403                     | —                                         | 403                                        |                                               |                                        |            |
| Total derivatives                                                   | 17,718                  | —                                         | 17,718                                     |                                               |                                        |            |
| Total repurchase agreements, subject to master netting arrangements | 1,359,040               | (300,000                                  | ) 1,059,040                                | —                                             | (1,059,040                             | ) —        |

The Company is party to several agreements commonly known as collateral swaps. These agreements involve the exchange of collateral under simultaneous repurchase and resell agreements with the same financial institution

counterparty. These repurchase and resell agreements have the same principal amounts, inception dates, and maturity dates and have been offset against each other in the balance sheet, as permitted under the netting provisions of ASC 210-20-45. The collateral swaps totaled \$300.0 million at both June 30, 2013 and December 31, 2012. At June 30, 2013, the Company had posted collateral consisting of \$313.7 million in agency mortgage-backed securities and accepted \$341.2 million in investment grade asset-backed, commercial mortgage-backed, and corporate bonds.

In June 2013, the Company became subject to new trade and clearing regulations authorized under the Dodd-Frank Wall Street Reform and Consumer Protection Act. The new rules require certain derivative transactions to be cleared through a clearing house, which the Company accesses through a designated clearing member. Under the new rules, initial and ongoing maintenance margin, in the form of cash and marketable securities, is required of both of the original counterparties to the contract, which is maintained by the clearing house. Once the trade is cleared, the clearing house assumes the performance risk of the original dealer counterparty. As of June 30, 2013, the Company had not executed any transactions subject to the new regulations.



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## 13. Stock-Based Compensation

The Company has historically issued stock-based compensation in the form of nonvested restricted stock, stock options and stock appreciation rights (SARs). During the first six months of 2013, stock-based compensation was issued in the form of nonvested stock and SARs. The stock-based compensation expense that has been charged against income was \$1.5 million and \$1.1 million in the three month periods ended June 30, 2013 and 2012, respectively, and \$2.7 million and \$2.6 million in the six months ended June 30, 2013 and 2012, respectively.

Nonvested stock awards generally vest in 4 to 7 years and contain restrictions as to transferability, sale, pledging, or assigning, among others, prior to the end of the vesting period. Dividend and voting rights are conferred upon grant. A summary of the status of the Company's nonvested share awards as of June 30, 2013, and changes during the six month period then ended, is presented below.

|                              | Shares    | Weighted<br>Average<br>Grant Date<br>Fair Value |
|------------------------------|-----------|-------------------------------------------------|
| Nonvested at January 1, 2013 | 882,803   | \$34.62                                         |
| Granted                      | 344,587   | 37.70                                           |
| Vested                       | (37,316)  | ) 34.70                                         |
| Forfeited                    | (15,313)  | ) 33.96                                         |
| Canceled                     | (115,497) | ) 35.32                                         |
| Nonvested at June 30, 2013   | 1,059,264 | \$35.55                                         |

SARs and stock options are granted with exercise prices equal to the market price of the Company's stock at the date of grant. SARs vest ratably over 4 years of continuous service and have 10-year contractual terms. All SARs must be settled in stock under provisions of the plan. Stock options, which have not been granted since 2005, vested ratably over 3 years of continuous service and also have 10-year contractual terms. In determining compensation cost, the Black-Scholes option-pricing model is used to estimate the fair value of SARs and options on date of grant. The current year per share average fair value and the model assumptions are shown in the table below.

|                                                     |           |
|-----------------------------------------------------|-----------|
| Weighted per share average fair value at grant date | \$7.16    |
| Assumptions:                                        |           |
| Dividend yield                                      | 2.3 %     |
| Volatility                                          | 23.2 %    |
| Risk-free interest rate                             | 1.2 %     |
| Expected term                                       | 7.3 years |

A summary of option activity during the first six months of 2013 is presented below.

|                                               | Shares    | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Term | Aggregate<br>Intrinsic<br>Value |
|-----------------------------------------------|-----------|------------------------------------------|---------------------------------------------------------|---------------------------------|
| (Dollars in thousands, except per share data) |           |                                          |                                                         |                                 |
| Outstanding at January 1, 2013                | 768,773   | \$31.51                                  |                                                         |                                 |
| Granted                                       | —         | —                                        |                                                         |                                 |
| Forfeited                                     | —         | —                                        |                                                         |                                 |
| Expired                                       | —         | —                                        |                                                         |                                 |
| Exercised                                     | (227,000) | ) 30.11                                  |                                                         |                                 |
| Outstanding at June 30, 2013                  | 541,773   | \$32.10                                  | 1.3 years                                               | \$6,203                         |



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A summary of SAR activity during the first six months of 2013 is presented below.

|                                               | Rights    | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Term | Aggregate<br>Intrinsic<br>Value |
|-----------------------------------------------|-----------|------------------------------------------|---------------------------------------------------------|---------------------------------|
| (Dollars in thousands, except per share data) |           |                                          |                                                         |                                 |
| Outstanding at January 1, 2013                | 1,787,376 | \$36.07                                  |                                                         |                                 |
| Granted                                       | 213,721   | 39.03                                    |                                                         |                                 |
| Forfeited                                     | (1,521)   | )31.31                                   |                                                         |                                 |
| Expired                                       | —         | —                                        |                                                         |                                 |
| Exercised                                     | (146,429) | )36.13                                   |                                                         |                                 |
| Outstanding at June 30, 2013                  | 1,853,147 | \$36.41                                  | 4.4 years                                               | \$13,230                        |

## 14. Fair Value Measurements

The Company uses fair value measurements to record fair value adjustments to certain financial and nonfinancial assets and liabilities and to determine fair value disclosures. Various financial instruments such as available for sale and trading securities, certain non-marketable securities relating to private equity activities, and derivatives are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets and liabilities on a nonrecurring basis, such as loans held for sale, mortgage servicing rights and certain other investment securities. These nonrecurring fair value adjustments typically involve lower of cost or fair value accounting or write-downs of individual assets.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Depending on the nature of the asset or liability, the Company uses various valuation techniques and assumptions when estimating fair value. For accounting disclosure purposes, a three-level valuation hierarchy of fair value measurements has been established. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

Level 1 – inputs to the valuation methodology are quoted prices for identical assets or liabilities in active markets.  
 Level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, and inputs that are observable for the assets or liabilities, either directly or indirectly (such as interest rates, yield curves, and prepayment speeds).  
 Level 3 – inputs to the valuation methodology are unobservable and significant to the fair value. These may be internally developed, using the Company's best information and assumptions that a market participant would consider. When determining the fair value measurements for assets and liabilities required or permitted to be recorded or disclosed at fair value, the Company considers the principal or most advantageous market in which it would transact and considers assumptions that market participants would use when pricing the asset or liability. When possible, the Company looks to active and observable markets to price identical assets or liabilities. When identical assets and liabilities are not traded in active markets, the Company looks to observable market data for similar assets and liabilities. Nevertheless, certain assets and liabilities are not actively traded in observable markets, and the Company must use alternative valuation techniques to derive an estimated fair value measurement.

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## Instruments Measured at Fair Value on a Recurring Basis

The table below presents the June 30, 2013 and December 31, 2012 carrying values of assets and liabilities measured at fair value on a recurring basis. There were no transfers among levels during the first six months of 2013 or the year ended December 31, 2012.

| (In thousands)                                 | Total Fair Value | Fair Value Measurements Using                                  |                                               |                                           |
|------------------------------------------------|------------------|----------------------------------------------------------------|-----------------------------------------------|-------------------------------------------|
|                                                |                  | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| June 30, 2013                                  |                  |                                                                |                                               |                                           |
| Assets:                                        |                  |                                                                |                                               |                                           |
| Available for sale securities:                 |                  |                                                                |                                               |                                           |
| U.S. government and federal agency obligations | \$413,857        | \$413,857                                                      | \$—                                           | \$—                                       |
| Government-sponsored enterprise obligations    | 414,818          | —                                                              | 414,818                                       | —                                         |
| State and municipal obligations                | 1,621,194        | —                                                              | 1,494,441                                     | 126,753                                   |
| Agency mortgage-backed securities              | 2,937,002        | —                                                              | 2,937,002                                     | —                                         |
| Non-agency mortgage-backed securities          | 242,432          | —                                                              | 242,432                                       | —                                         |
| Asset-backed securities                        | 3,088,148        | —                                                              | 3,088,148                                     | —                                         |
| Other debt securities                          | 165,735          | —                                                              | 165,735                                       | —                                         |
| Equity securities                              | 44,629           | 26,018                                                         | 18,611                                        | —                                         |
| Trading securities                             | 14,670           | —                                                              | 14,670                                        | —                                         |
| Private equity investments                     | 63,279           | —                                                              | —                                             | 63,279                                    |
| Derivatives *                                  | 12,682           | —                                                              | 12,677                                        | 5                                         |
| Assets held in trust                           | 6,652            | 6,652                                                          | —                                             | —                                         |
| Total assets                                   | \$9,025,098      | \$446,527                                                      | \$8,388,534                                   | \$190,037                                 |
| Liabilities:                                   |                  |                                                                |                                               |                                           |
| Derivatives *                                  | \$13,249         | \$—                                                            | \$13,151                                      | \$98                                      |
| Total liabilities                              | \$13,249         | \$—                                                            | \$13,151                                      | \$98                                      |
| December 31, 2012                              |                  |                                                                |                                               |                                           |
| Assets:                                        |                  |                                                                |                                               |                                           |
| Available for sale securities:                 |                  |                                                                |                                               |                                           |
| U.S. government and federal agency obligations | \$438,759        | \$438,759                                                      | \$—                                           | \$—                                       |
| Government-sponsored enterprise obligations    | 471,574          | —                                                              | 471,574                                       | —                                         |
| State and municipal obligations                | 1,615,707        | —                                                              | 1,489,293                                     | 126,414                                   |
| Agency mortgage-backed securities              | 3,380,955        | —                                                              | 3,380,955                                     | —                                         |
| Non-agency mortgage-backed securities          | 237,011          | —                                                              | 237,011                                       | —                                         |
| Asset-backed securities                        | 3,167,394        | —                                                              | 3,167,394                                     | —                                         |
| Other debt securities                          | 177,752          | —                                                              | 177,752                                       | —                                         |
| Equity securities                              | 33,096           | 17,835                                                         | 15,261                                        | —                                         |
| Trading securities                             | 28,837           | —                                                              | 28,837                                        | —                                         |
| Private equity investments                     | 68,167           | —                                                              | —                                             | 68,167                                    |
| Derivatives *                                  | 16,740           | —                                                              | 16,731                                        | 9                                         |
| Assets held in trust                           | 5,440            | 5,440                                                          | —                                             | —                                         |
| Total assets                                   | \$9,641,432      | \$462,034                                                      | \$8,984,808                                   | \$194,590                                 |
| Liabilities:                                   |                  |                                                                |                                               |                                           |
| Derivatives *                                  | \$17,718         | \$—                                                            | \$17,522                                      | \$196                                     |

|                   |          |     |          |       |
|-------------------|----------|-----|----------|-------|
| Total liabilities | \$17,718 | \$— | \$17,522 | \$196 |
|-------------------|----------|-----|----------|-------|

\* The fair value of each class of derivative is shown in Note 11.

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Valuation methods for instruments measured at fair value on a recurring basis

Following is a description of the Company's valuation methodologies used for instruments measured at fair value on a recurring basis:

Available for sale investment securities

For available for sale securities, changes in fair value, including that portion of other-than-temporary impairment unrelated to credit loss, are recorded in other comprehensive income. As mentioned in Note 4 on Investment Securities, the Company records the credit-related portion of other-than-temporary impairment in current earnings. This portfolio comprises the majority of the assets which the Company records at fair value. Most of the portfolio, which includes government-sponsored enterprise, mortgage-backed and asset-backed securities, are priced utilizing industry-standard models that consider various assumptions, including time value, yield curves, volatility factors, prepayment speeds, default rates, loss severity, current market and contractual prices for the underlying financial instruments, as well as other relevant economic measures. Substantially all of these assumptions are observable in the marketplace, can be derived from observable data, or are supported by observable levels at which transactions are executed in the marketplace. These measurements are classified as Level 2 in the fair value hierarchy. Where quoted prices are available in an active market, the measurements are classified as Level 1. Most of the Level 1 measurements apply to common stock and U.S. Treasury obligations.

The fair values of Level 1 and 2 securities (excluding equity securities) in the available for sale portfolio are prices provided by a third-party pricing service. The prices provided by the third-party pricing service are based on observable market inputs, as described in the sections below. On a quarterly basis, the Company compares a sample of these prices to other independent sources for the same and similar securities. Variances are analyzed, and, if appropriate, additional research is conducted with the third-party pricing service. Based on this research, the pricing service may affirm or revise its quoted price. No significant adjustments have been made to the prices provided by the pricing service. The pricing service also provides documentation on an ongoing basis that includes reference data, inputs and methodology by asset class, which is reviewed to ensure that security placement within the fair value hierarchy is appropriate.

Valuation methods and inputs, by class of security:

U.S. government and federal agency obligations

U.S. treasury bills, bonds and notes, including TIPS, are valued using live data from active market makers and inter-dealer brokers. Valuations for stripped coupon and principal issues are derived from yield curves generated from various dealer contacts and live data sources.

Government-sponsored enterprise obligations

Government-sponsored enterprise obligations are evaluated using cash flow valuation models. Inputs used are live market data, cash settlements, Treasury market yields, and floating rate indices such as LIBOR, CMT, and Prime.

State and municipal obligations, excluding auction rate securities

A yield curve is generated and applied to bond sectors, and individual bond valuations are extrapolated. Inputs used to generate the yield curve are bellwether issue levels, established trading spreads between similar issuers or credits, historical trading spreads over widely accepted market benchmarks, new issue scales, and verified bid information. Bid information is verified by corroborating the data against external sources such as broker-dealers, trustees/paying agents, issuers, or non-affiliated bondholders.

Mortgage and asset-backed securities

Collateralized mortgage obligations and other asset-backed securities are valued at the tranche level. For each tranche valuation, the process generates predicted cash flows for the tranche, applies a market based (or benchmark) yield/spread for each tranche, and incorporates deal collateral performance and tranche level attributes to determine tranche-specific spreads to adjust the benchmark yield. Tranche cash flows are generated from new deal files and prepayment/default assumptions. Tranche spreads are based on tranche characteristics such as average life, type, volatility, ratings, underlying collateral and performance, and prevailing market conditions. The appropriate tranche spread is applied to the corresponding benchmark, and the resulting value is used to discount the cash flows to generate an evaluated price.

Valuation of agency pass-through securities, typically issued under GNMA, FNMA, FHLMC, and SBA programs, are primarily derived from information from the To Be Announced (TBA) market. This market consists of generic mortgage pools which have not been received for settlement. Snapshots of the TBA market, using live data feeds

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distributed by multiple electronic platforms, and in conjunction with other indices, are used to compute a price based on discounted cash flow models.

### Other debt securities

Other debt securities are valued using active markets and inter-dealer brokers as well as bullet spread scales and option adjusted spreads. The spreads and models use yield curves, terms and conditions of the bonds, and any special features (i.e., call or put options, redemption features, etc.).

### Equity securities

Equity securities are priced using the market prices for each security from the major stock exchanges or other electronic quotation systems. These are generally classified as Level 1 measurements. Stocks which trade infrequently are classified as Level 2.

The available for sale portfolio includes certain auction rate securities. The auction process by which auction rate securities are normally priced has not functioned since 2008, and due to the illiquidity in the market, the fair value of these securities cannot be based on observable market prices. The fair values of the auction rate securities are estimated using a discounted cash flows analysis which is discussed more fully in the Level 3 Inputs section of this note. Because several of the inputs significant to the measurement are not observable, these measurements are classified as Level 3 measurements.

### Trading securities

The securities in the Company's trading portfolio are priced by averaging several broker quotes for similar instruments and are classified as Level 2 measurements.

### Private equity investments

These securities are held by the Company's private equity subsidiaries and are included in non-marketable investment securities in the consolidated balance sheets. Due to the absence of quoted market prices, valuation of these nonpublic investments requires significant management judgment. These fair value measurements, which are discussed in the Level 3 Inputs section of this note, are classified as Level 3.

### Derivatives

The Company's derivative instruments include interest rate swaps, foreign exchange forward contracts, commitments and sales contracts related to personal mortgage loan origination activity, and certain credit risk guarantee agreements. When appropriate, the impact of credit standing, as well as any potential credit enhancements such as collateral, has been considered in the fair value measurement.

Valuations for interest rate swaps are derived from a proprietary model whose significant inputs are readily observable market parameters, primarily yield curves used to calculate current exposure. Counterparty credit risk is incorporated into the model and calculated by applying a net credit spread over LIBOR to the swap's total expected exposure over time. The net credit spread is comprised of spreads for both the Company and its counterparty, derived from probability of default and other loss estimate information obtained from a third party credit data provider or from the Company's Credit Department when not otherwise available. The credit risk component is not significant compared to the overall fair value of the swaps. The results of the model are constantly validated through comparison to active trading in the marketplace. These fair value measurements are classified as Level 2.

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Fair value measurements for foreign exchange contracts are derived from a model whose primary inputs are quotations from global market makers and are classified as Level 2.

The fair values of mortgage loan commitments and forward sales contracts on the associated loans are based on quoted prices for similar loans in the secondary market. However, these prices are adjusted by a factor which considers the likelihood that a commitment will ultimately result in a closed loan. This estimate is based on the Company's historical data and its judgment about future economic trends. Based on the unobservable nature of this adjustment, these measurements are classified as Level 3.

- The Company's contracts related to credit risk guarantees are valued under a proprietary model which uses unobservable inputs and assumptions about the creditworthiness of the counterparty (generally a Bank customer). Customer credit spreads, which are based on probability of default and other loss estimates, are calculated internally by the Company's

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Credit Department, as mentioned above, and are based on the Company's internal risk rating for each customer. Because these inputs are significant to the measurements, they are classified as Level 3.

Assets held in trust

Assets held in an outside trust for the Company's deferred compensation plan consist of investments in mutual funds. The fair value measurements are based on quoted prices in active markets and classified as Level 1. The Company has recorded an asset representing the total investment amount. The Company has also recorded a corresponding nonfinancial liability, representing the Company's liability to the plan participants.

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The changes in Level 3 assets and liabilities measured at fair value on a recurring basis are summarized as follows:

|                                                                                                                                                                               | Fair Value Measurements Using<br>Significant Unobservable Inputs<br>(Level 3) |                                  |             |             |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------|----------------------------------|-------------|-------------|
|                                                                                                                                                                               | State and<br>Municipal<br>Obligation                                          | Private<br>Equity<br>Investments | Derivatives | Total       |
| (In thousands)                                                                                                                                                                |                                                                               |                                  |             |             |
| For the three months ended June 30, 2013                                                                                                                                      |                                                                               |                                  |             |             |
| Balance March 31, 2013                                                                                                                                                        | \$ 128,143                                                                    | \$ 68,103                        | \$ (131 )   | \$ 196,115  |
| Total gains or losses (realized/unrealized):                                                                                                                                  |                                                                               |                                  |             |             |
| Included in earnings                                                                                                                                                          | —                                                                             | 298                              | 69          | 367         |
| Included in other comprehensive income *                                                                                                                                      | (1,072 )                                                                      | —                                | —           | (1,072 )    |
| Investment securities called                                                                                                                                                  | (375 )                                                                        | —                                | —           | (375 )      |
| Discount accretion                                                                                                                                                            | 57                                                                            | —                                | —           | 57          |
| Purchases of private equity investments                                                                                                                                       | —                                                                             | 2,000                            | —           | 2,000       |
| Sale/pay down of private equity investments                                                                                                                                   | —                                                                             | (7,184 )                         | —           | (7,184 )    |
| Capitalized interest/dividends                                                                                                                                                | —                                                                             | 62                               | —           | 62          |
| Sale of risk participation agreement                                                                                                                                          | —                                                                             | —                                | (31 )       | (31 )       |
| Balance June 30, 2013                                                                                                                                                         | \$ 126,753                                                                    | \$ 63,279                        | \$ (93 )    | \$ 189,939  |
| Total gains or losses for the three months included in earnings<br>attributable to the change in unrealized gains or losses relating to assets<br>still held at June 30, 2013 | \$—                                                                           | \$ 298                           | \$ 69       | \$ 367      |
| For the six months ended June 30, 2013                                                                                                                                        |                                                                               |                                  |             |             |
| Balance January 1, 2013                                                                                                                                                       | \$ 126,414                                                                    | \$ 68,167                        | \$ (187 )   | \$ 194,394  |
| Total gains or losses (realized/unrealized):                                                                                                                                  |                                                                               |                                  |             |             |
| Included in earnings                                                                                                                                                          | —                                                                             | (1,477 )                         | 125         | (1,352 )    |
| Included in other comprehensive income *                                                                                                                                      | 1,116                                                                         | —                                | —           | 1,116       |
| Investment securities called                                                                                                                                                  | (900 )                                                                        | —                                | —           | (900 )      |
| Discount accretion                                                                                                                                                            | 123                                                                           | —                                | —           | 123         |
| Purchase of private equity securities                                                                                                                                         | —                                                                             | 3,650                            | —           | 3,650       |
| Sale/pay down of private equity investments                                                                                                                                   | —                                                                             | (7,184 )                         | —           | (7,184 )    |
| Capitalized interest/dividends                                                                                                                                                | —                                                                             | 123                              | —           | 123         |
| Sale of risk participation agreement                                                                                                                                          | —                                                                             | —                                | (31 )       | (31 )       |
| Balance June 30, 2013                                                                                                                                                         | \$ 126,753                                                                    | \$ 63,279                        | \$ (93 )    | \$ 189,939  |
| Total gains or losses for the six months included in earnings attributable<br>to the change in unrealized gains or losses relating to assets still held at<br>June 30, 2013   | \$—                                                                           | \$ (1,477 )                      | \$ 125      | \$ (1,352 ) |
| For the three months ended June 30, 2012                                                                                                                                      |                                                                               |                                  |             |             |
| Balance March 31, 2012                                                                                                                                                        | \$ 129,873                                                                    | \$ 72,121                        | \$ (106 )   | \$ 201,888  |
| Total gains or losses (realized/unrealized):                                                                                                                                  |                                                                               |                                  |             |             |
| Included in earnings                                                                                                                                                          | —                                                                             | 1,475                            | 7           | 1,482       |
| Included in other comprehensive income *                                                                                                                                      | 520                                                                           | —                                | —           | 520         |
| Investment securities called                                                                                                                                                  | (3,000 )                                                                      | —                                | —           | (3,000 )    |
| Discount accretion                                                                                                                                                            | 147                                                                           | —                                | —           | 147         |
| Sale/pay down of private equity securities                                                                                                                                    | —                                                                             | (7,845 )                         | —           | (7,845 )    |
| Capitalized interest/dividends                                                                                                                                                | —                                                                             | 15                               | —           | 15          |
| Balance June 30, 2012                                                                                                                                                         | \$ 127,540                                                                    | \$ 65,766                        | \$ (99 )    | \$ 193,207  |
| Total gains or losses for the three months included in earnings<br>attributable to the change in unrealized gains or losses relating to assets                                | \$—                                                                           | \$ 600                           | \$ 7        | \$ 607      |

still held at June 30, 2012

For the six months ended June 30, 2012

|                                                                                                                                                                       |           |           |           |           |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------|-----------|-----------|-----------|
| Balance January 1, 2012                                                                                                                                               | \$135,621 | \$ 66,978 | \$ (123 ) | \$202,476 |
| Total gains or losses (realized/unrealized):                                                                                                                          |           |           |           |           |
| Included in earnings                                                                                                                                                  | —         | 5,600     | (4 )      | 5,596     |
| Included in other comprehensive income *                                                                                                                              | (4,938 )  | —         | —         | (4,938 )  |
| Investment securities called                                                                                                                                          | (3,350 )  | —         | —         | (3,350 )  |
| Discount accretion                                                                                                                                                    | 207       | —         | —         | 207       |
| Purchase of private equity investments                                                                                                                                | —         | 3,275     | —         | 3,275     |
| Sale/pay down of private equity securities                                                                                                                            | —         | (10,279 ) | —         | (10,279 ) |
| Capitalized interest/dividends                                                                                                                                        | —         | 192       | —         | 192       |
| Purchase of risk participation agreement                                                                                                                              | —         | —         | 28        | 28        |
| Balance June 30, 2012                                                                                                                                                 | \$127,540 | \$ 65,766 | \$ (99 )  | \$193,207 |
| Total gains or losses for the six months included in earnings attributable to the change in unrealized gains or losses relating to assets still held at June 30, 2012 | \$—       | \$ 4,575  | \$ 5      | \$4,580   |

\* Included in "net unrealized gains (losses) on other securities" in the consolidated statements of comprehensive income.

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Gains and losses included in earnings for the Level 3 assets and liabilities in the previous table are reported in the following line items in the consolidated statements of income:

| (In thousands)                                                                      | Loan Fees<br>and Sales | Other<br>Non-Interest<br>Income | Investment<br>Securities<br>Gains<br>(Losses),<br>Net | Total      |
|-------------------------------------------------------------------------------------|------------------------|---------------------------------|-------------------------------------------------------|------------|
| For the three months ended June 30, 2013                                            |                        |                                 |                                                       |            |
| Total gains or losses included in earnings                                          | \$—                    | \$ 69                           | \$ 298                                                | \$ 367     |
| Change in unrealized gains or losses relating to assets still held at June 30, 2013 | \$—                    | \$ 69                           | \$ 298                                                | \$ 367     |
| For the six months ended June 30, 2013                                              |                        |                                 |                                                       |            |
| Total gains or losses included in earnings                                          | \$—                    | \$ 125                          | \$(1,477 )                                            | \$(1,352 ) |
| Change in unrealized gains or losses relating to assets still held at June 30, 2013 | \$—                    | \$ 125                          | \$(1,477 )                                            | \$(1,352 ) |
| For the three months ended June 30, 2012                                            |                        |                                 |                                                       |            |
| Total gains or losses included in earnings                                          | \$—                    | \$ 7                            | \$ 1,475                                              | \$ 1,482   |
| Change in unrealized gains or losses relating to assets still held at June 30, 2012 | \$—                    | \$ 7                            | \$ 600                                                | \$ 607     |
| For the six months ended June 30, 2012                                              |                        |                                 |                                                       |            |
| Total gains or losses included in earnings                                          | \$(9 )                 | \$ 5                            | \$ 5,600                                              | \$ 5,596   |
| Change in unrealized gains or losses relating to assets still held at June 30, 2012 | \$—                    | \$ 5                            | \$ 4,575                                              | \$ 4,580   |

## Level 3 Inputs

As shown above, the Company's significant Level 3 measurements which employ unobservable inputs that are readily quantifiable pertain to auction rate securities (ARS) held by the Bank and investments in portfolio concerns held by the Company's private equity subsidiaries. ARS are included in state and municipal securities and totaled \$126.8 million at June 30, 2013, while private equity investments, included in non-marketable securities, totaled \$63.3 million.

Information about these inputs is presented in the table and discussions below.

## Quantitative Information about Level 3 Fair Value Measurements

|                            | Valuation Technique         | Unobservable Input               | Range       |
|----------------------------|-----------------------------|----------------------------------|-------------|
| Auction rate securities    | Discounted cash flow        | Estimated market recovery period | 5 years     |
|                            |                             | Estimated market rate            | 2.3% - 3.5% |
| Private equity investments | Market comparable companies | EBITDA multiple                  | 4.0 - 5.5   |

The fair values of ARS are estimated using a discounted cash flows analysis in which estimated cash flows are based on mandatory interest rates paid under failing auctions and projected over an estimated market recovery period. Under normal conditions, ARS traded in weekly auctions and were considered liquid investments. The Company's estimate of when these auctions might resume is highly judgmental and subject to variation depending on current and projected market conditions. Few auctions of these securities have been held since 2008, and most sales have been privately arranged. Estimated cash flows during the period over which the Company expects to hold the securities are discounted at an estimated market rate. These securities are comprised of bonds issued by various states and municipalities for healthcare and student lending purposes, and market rates are derived for each type. Market rates are calculated at each valuation date using a LIBOR or Treasury based rate plus spreads representing adjustments for liquidity premium and nonperformance risk. The spreads are developed internally by employees in the Company's

bond department. An increase in the holding period alone would result in a higher fair value measurement, while an increase in the estimated market rate (the discount rate) alone would result in a lower fair value measurement. The valuation of ARS is regularly reviewed by members of the Company's Asset/Liability Committee.

The fair values of the Company's private equity investments are based on a determination of fair value of the investee company less exit costs and preference payments assuming the sale of the investee company. Investee companies are normally non-public entities. The fair value of the investee company is determined by reference to the investee's total earnings before interest, depreciation/amortization, and income taxes (EBITDA) multiplied by an EBITDA factor. EBITDA is normally determined based on a trailing prior period adjusted for specific factors including current economic outlook, investee management, and specific unique circumstances such as sales order information, major customer status, regulatory changes, etc. The EBITDA multiple is based on management's review of published trading multiples for recent private equity transactions and other judgments and is derived for each individual investee. The value of the investee company is then reduced to reflect appropriate assumed selling and liquidation costs. The fair value of the Company's investment (which is usually a partial interest in the investee company) is

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then calculated based on its ownership percentage in the investee company. On a quarterly basis, these fair value analyses are reviewed by a valuation committee consisting of investment managers and senior Company management.

## Instruments Measured at Fair Value on a Nonrecurring Basis

For assets measured at fair value on a nonrecurring basis during the first six months of 2013 and 2012, and still held as of June 30, 2013 and 2012, the following table provides the adjustments to fair value recognized during the respective periods, the level of valuation inputs used to determine each adjustment, and the carrying value of the related individual assets or portfolios at June 30, 2013 and 2012.

| (In thousands)                      | Fair Value | Fair Value Measurements Using                                                    |                                                           |                                                    | Total Gains<br>(Losses)<br>Recognized<br>During the<br>Six Months<br>Ended June<br>30 |
|-------------------------------------|------------|----------------------------------------------------------------------------------|-----------------------------------------------------------|----------------------------------------------------|---------------------------------------------------------------------------------------|
|                                     |            | Quoted<br>Prices in<br>Active<br>Markets for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |                                                                                       |
| June 30, 2013                       |            |                                                                                  |                                                           |                                                    |                                                                                       |
| Collateral dependent impaired loans | \$6,731    | \$—                                                                              | \$—                                                       | \$ 6,731                                           | \$(1,967 )                                                                            |
| Private equity investments          | 675        | —                                                                                | —                                                         | 675                                                | (325 )                                                                                |
| Mortgage servicing rights           | 602        | —                                                                                | —                                                         | 602                                                | 187                                                                                   |
| Foreclosed assets                   | 291        | —                                                                                | —                                                         | 291                                                | (135 )                                                                                |
| June 30, 2012                       |            |                                                                                  |                                                           |                                                    |                                                                                       |
| Collateral dependent impaired loans | \$27,176   | \$—                                                                              | \$—                                                       | \$ 27,176                                          | \$(5,918 )                                                                            |
| Mortgage servicing rights           | 574        | —                                                                                | —                                                         | 574                                                | 20                                                                                    |
| Foreclosed assets                   | 1,550      | —                                                                                | —                                                         | 1,550                                              | (425 )                                                                                |
| Long-lived assets                   | 5,397      | —                                                                                | —                                                         | 5,397                                              | (3,398 )                                                                              |

## Valuation methods for instruments measured at fair value on a nonrecurring basis

Following is a description of the Company's valuation methodologies used for other financial and nonfinancial instruments measured at fair value on a nonrecurring basis.

## Collateral dependent impaired loans

While the overall loan portfolio is not carried at fair value, the Company periodically records nonrecurring adjustments to the carrying value of loans based on fair value measurements for partial charge-offs of the uncollectible portions of those loans. Nonrecurring adjustments also include certain impairment amounts for collateral dependent loans when establishing the allowance for loan losses. Such amounts are generally based on the fair value of the underlying collateral supporting the loan. In determining the value of real estate collateral, the Company relies on external and internal appraisals of property values depending on the size and complexity of the real estate collateral. The Company maintains a staff of qualified appraisers who also review third party appraisal reports for reasonableness. In the case of non-real estate collateral, reliance is placed on a variety of sources, including external estimates of value and judgments based on the experience and expertise of internal specialists. Values of all loan collateral are regularly reviewed by credit administration. Unobservable inputs to these measurements, which include estimates and judgments often used in conjunction with appraisals, are not readily quantifiable. These measurements are classified as Level 3. Changes in fair value recognized for partial charge-offs of loans and loan impairment reserves on loans held by the Company at June 30, 2013 and 2012 are shown in the table above.

Loans held for sale

Loans held for sale are carried at the lower of cost or fair value. At June 30, 2013, this portfolio consisted of student loans. Most of the portfolio is under contract to an agency which has been unable to consistently purchase loans under existing contractual terms. These loans have been evaluated using a fair value measurement method based on a discounted cash flows analysis, which is classified as Level 3. The fair value of these loans was \$5.6 million at June 30, 2013, net of an impairment reserve of \$141 thousand. The measurement of fair value for other student loans is based on the specific prices mandated in the underlying sale contracts and the estimated exit price and is classified as Level 2.



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### Private equity investments and restricted stock

These assets are included in non-marketable investment securities in the consolidated balance sheets. They include certain investments in private equity concerns held by the Parent company which are carried at cost, reduced by other-than-temporary impairment. These investments are periodically evaluated for impairment based on their estimated fair value as determined by review of available information, most of which is provided as monthly or quarterly internal financial statements, annual audited financial statements, investee tax returns, and in certain situations, through research into and analysis of the assets and investments held by those private equity concerns.

Restricted stock consists of stock issued by the Federal Reserve Bank and FHLB and is held by the bank subsidiary as required for regulatory purposes. Generally, there are restrictions on the sale and/or liquidation of these investments, and they are carried at cost, reduced by other-than-temporary impairment. Fair value measurements for these securities are classified as Level 3.

### Mortgage servicing rights

The Company initially measures its mortgage servicing rights at fair value and amortizes them over the period of estimated net servicing income. They are periodically assessed for impairment based on fair value at the reporting date. Mortgage servicing rights do not trade in an active market with readily observable prices. Accordingly, the fair value is estimated based on a valuation model which calculates the present value of estimated future net servicing income. The model incorporates assumptions that market participants use in estimating future net servicing income, including estimates of prepayment speeds, market discount rates, cost to service, float earnings rates, and other ancillary income, including late fees. The fair value measurements are classified as Level 3.

### Goodwill and core deposit premium

Valuation of goodwill to determine impairment is performed on an annual basis, or more frequently if there is an event or circumstance that would indicate impairment may have occurred. The process involves calculations to determine the fair value of each reporting unit on a stand-alone basis. A combination of formulas using current market multiples, based on recent sales of financial institutions within the Company's geographic marketplace, is used to estimate the fair value of each reporting unit. That fair value is compared to the carrying amount of the reporting unit, including its recorded goodwill. Impairment is considered to have occurred if the fair value of the reporting unit is lower than the carrying amount of the reporting unit. The fair value of the Company's common stock relative to its computed book value per share is also considered as part of the overall evaluation. These measurements are classified as Level 3.

Core deposit premiums are recognized at the time a portfolio of deposits is acquired. Core deposit premiums are recognized using valuation techniques which calculate the present value of the estimated net cost savings attributable to the core deposit base, relative to alternative costs of funds and tax benefits, if applicable, over the expected remaining economic life of the depositors. Subsequent evaluations are made when facts or circumstances indicate potential impairment may have occurred. The Company uses estimates of discounted future cash flows, comparisons with alternative sources for deposits, consideration of income potential generated in other product lines by current customers, geographic parameters, and other demographics to estimate a current fair value of a specific deposit base. If the calculated fair value is less than the carrying value, impairment is considered to have occurred. This measurement is classified as Level 3.

### Foreclosed assets

Foreclosed assets consist of loan collateral which has been repossessed through foreclosure. This collateral is comprised of commercial and residential real estate and other non-real estate property, including auto, marine and

recreational vehicles. Foreclosed assets are recorded as held for sale initially at the lower of the loan balance or fair value of the collateral less estimated selling costs. Subsequent to foreclosure, valuations are updated periodically, and the assets may be marked down further, reflecting a new cost basis. Fair value measurements may be based upon appraisals, third-party price opinions, or internally developed pricing methods. These measurements are classified as Level 3.

#### Long-lived assets

In accordance with ASC 360-10-35, investments in branch facilities and various office buildings are written down to estimated fair value, or estimated fair value less cost to sell if the property is held for sale. Fair value is estimated in a process which considers current local commercial real estate market conditions and the judgment of the sales agent and often involves obtaining third party appraisals from certified real estate appraisers. The carrying amounts of these real estate holdings are regularly monitored by real estate professionals employed by the Company. These fair value measurements are classified as Level 3. Unobservable inputs to these measurements, which include estimates and judgments often used in conjunction with appraisals, are not readily quantifiable.

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## 15. Fair Value of Financial Instruments

The carrying amounts and estimated fair values of financial instruments held by the Company are set forth below. Fair value estimates are made at a specific point in time based on relevant market information. They do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for many of the Company's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, risk characteristics and economic conditions. These estimates are subjective, involve uncertainties, and cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

The methods and inputs used in the estimation of fair value for the financial instruments in the table below are discussed in the preceding Fair Value Measurements note and in the Fair Value of Financial Instruments note in the Company's 2012 Annual Report on Form 10-K. There have been no significant changes in these methods and inputs since December 31, 2012.

The estimated fair values of the Company's financial instruments and the classification of their fair value measurement within the valuation hierarchy are as follows:

| (In thousands)                                       | Fair Value June 30, 2013 |                 | December 31, 2012    |                 |                      |
|------------------------------------------------------|--------------------------|-----------------|----------------------|-----------------|----------------------|
|                                                      | Hierarchy Level          | Carrying Amount | Estimated Fair Value | Carrying Amount | Estimated Fair Value |
| <b>Financial Assets</b>                              |                          |                 |                      |                 |                      |
| <b>Loans:</b>                                        |                          |                 |                      |                 |                      |
| Business                                             | Level 3                  | \$3,415,361     | \$3,407,477          | \$3,134,801     | \$3,144,989          |
| Real estate - construction and land                  | Level 3                  | 398,625         | 400,990              | 355,996         | 352,547              |
| Real estate - business                               | Level 3                  | 2,210,260       | 2,225,420            | 2,214,975       | 2,240,796            |
| Real estate - personal                               | Level 3                  | 1,700,060       | 1,717,425            | 1,584,859       | 1,642,820            |
| Consumer                                             | Level 3                  | 1,450,781       | 1,463,829            | 1,289,650       | 1,309,403            |
| Revolving home equity                                | Level 3                  | 422,902         | 428,011              | 437,567         | 441,651              |
| Consumer credit card                                 | Level 3                  | 760,512         | 775,469              | 804,245         | 823,560              |
| Overdrafts                                           | Level 3                  | 11,654          | 11,654               | 9,291           | 9,291                |
| Loans held for sale                                  | Level 2                  | 3,382           | 3,382                | 3,017           | 3,030                |
| Loans held for sale                                  | Level 3                  | 5,559           | 5,559                | 5,810           | 5,810                |
| <b>Investment securities:</b>                        |                          |                 |                      |                 |                      |
| Available for sale                                   | Level 1                  | 439,875         | 439,875              | 456,594         | 456,594              |
| Available for sale                                   | Level 2                  | 8,361,187       | 8,361,187            | 8,939,240       | 8,939,240            |
| Available for sale                                   | Level 3                  | 126,753         | 126,753              | 126,414         | 126,414              |
| Trading                                              | Level 2                  | 14,670          | 14,670               | 28,837          | 28,837               |
| Non-marketable                                       | Level 3                  | 113,470         | 113,470              | 118,650         | 118,650              |
| Federal funds sold                                   | Level 1                  | 22,990          | 22,990               | 27,595          | 27,595               |
| Securities purchased under agreements to resell      | Level 3                  | 1,200,000       | 1,202,506            | 1,200,000       | 1,215,234            |
| Interest earning deposits with banks                 | Level 1                  | 6,816           | 6,816                | 179,164         | 179,164              |
| Cash and due from banks                              | Level 1                  | 399,687         | 399,687              | 573,066         | 573,066              |
| Derivative instruments                               | Level 2                  | 12,677          | 12,677               | 16,731          | 16,731               |
| Derivative instruments                               | Level 3                  | 5               | 5                    | 9               | 9                    |
| <b>Financial Liabilities</b>                         |                          |                 |                      |                 |                      |
| Non-interest bearing deposits                        | Level 1                  | \$5,811,473     | \$5,811,473          | \$6,299,903     | \$6,299,903          |
| Savings, interest checking and money market deposits | Level 1                  | 9,573,390       | 9,573,390            | 9,817,943       | 9,817,943            |
| Time open and certificates of deposit                | Level 3                  | 2,512,075       | 2,515,492            | 2,230,807       | 2,239,595            |
| Federal funds purchased                              | Level 1                  | 636,360         | 636,360              | 24,510          | 24,510               |

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|                                                |         |         |         |           |           |
|------------------------------------------------|---------|---------|---------|-----------|-----------|
| Securities sold under agreements to repurchase | Level 3 | 984,334 | 983,893 | 1,059,040 | 1,057,462 |
| Other borrowings                               | Level 3 | 102,766 | 113,341 | 103,710   | 117,527   |
| Derivative instruments                         | Level 2 | 13,151  | 13,151  | 17,522    | 17,522    |
| Derivative instruments                         | Level 3 | 98      | 98      | 196       | 196       |

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## 16. Legal Proceedings

On July 13, 2012, Visa and MasterCard each announced a preliminary settlement to resolve the plaintiffs' claims in the multi-district interchange litigation and also announced an agreement in principle to resolve the claims brought against them by certain individual retailers in that same litigation. The proposed settlement includes a cash payment to certain merchants of \$6.6 billion, of which Visa is responsible for \$4.4 billion, and a provision which would reduce credit card interchange income by 10 basis points over an 8 month period beginning in September 2013. Other provisions include the ability for merchants to surcharge customers for credit card usage, the ability for merchant buying groups to negotiate together with Visa and MasterCard, and the ability to cancel this proposed agreement if more than 25% of all affected merchants opt out of the agreement. The Company estimates that the pre-tax cost of the future reduction of 10 basis points in interchange income for an 8 month period, which is part of the above settlement, would amount to approximately \$5.2 million. Accordingly, the Company established a liability in 2012 for these anticipated costs.

In December 2011, the Bank reached a class-wide settlement in a class action lawsuit captioned *Wolfgeher v. Commerce Bank*, Case No. 1:10-cv-22017 (MDL 2036, S.D. Fla.) which alleged that the Bank had improperly charged overdraft fees on certain debit card transactions and claimed refunds for the plaintiff individually and on behalf of other customers as a class. A formal Settlement Agreement and Release related to this lawsuit was signed by the Bank on July 26, 2012. The Bank, while admitting no wrongdoing, agreed to the settlement in order to resolve the litigation and avoid further expense. The settlement provided for a payment of \$18.3 million into a class settlement fund, the proceeds of which will be used to issue refunds to class members and to pay attorneys' fees, administrative and other costs, in exchange for a complete release of all claims asserted against the Bank. The Bank also agreed to post debit card transactions in chronological order, which was implemented on February 21, 2013. As a result of the change in the posting order of debit card transactions, the Company currently estimates that overdraft income will be reduced on an annual basis by \$3.5 million to \$5.5 million. A second suit alleging the same facts and also seeking class-action status was filed on June 4, 2010 in Missouri state court; however, the second suit was resolved by agreement on July 18, 2013, and will be dismissed.

On January 4, 2013, the Company was named in a petition by Patrick J. Malloy III, Bankruptcy Trustee for the Bankruptcy Estate of George David Gordon Jr. ("Gordon"). The petition was filed in the District Court in and for Tulsa County, State of Oklahoma and removed to the United States District Court for the Northern District of Oklahoma, and subsequently remanded back to the District Court on May 7, 2013. On May 10, 2013, the Company was served with an amended petition in the case. The amended petition alleges that Gordon was involved in securities fraud and that Bank South, an Oklahoma bank that was subsequently acquired by the Company, together with a lending officer employed by Bank South, are jointly and severally liable, as aiders and abettors of the fraudulent scheme, for losses suffered by defrauded investors. The losses suffered by investors who have assigned their claims to the Trustee are alleged to be in excess of \$9 million. The claim alleges that Commerce Bank is liable as a successor by merger to Bank South. Based on facts available to the Company and after discussion with outside counsel handling the matter, it is not possible to determine at this time whether this litigation presents a loss contingency that is probable or estimable. The Company believes it has substantial defenses to this matter and anticipates the matter will be resolved without material loss. No liability has been recorded at this time, in accordance with accounting guidance at ASC 450-20. This matter will continue to be evaluated on an ongoing basis and if further developments result in a loss contingency related to this claim being both probable and estimable, the Company will establish an accrued liability with respect to such loss contingency and record it accordingly.

The Company has various other lawsuits pending at June 30, 2013, arising in the normal course of business. While some matters pending against the Company specify damages claimed by plaintiffs, others do not seek a specified amount of damages or are at very early stages of the legal process. The Company records a loss accrual for all legal matters for which it deems a loss is probable and can be reasonably estimated. Some legal matters, which are at early stages in the legal process, have not yet progressed to the point where a loss amount can be estimated.



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

The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes and with the statistical information and financial data appearing in this report as well as the Company's 2012 Annual Report on Form 10-K. Results of operations for the three and six month periods ended June 30, 2013 are not necessarily indicative of results to be attained for any other period.

Forward-Looking Information

This report may contain "forward-looking statements" that are subject to risks and uncertainties and include information about possible or assumed future results of operations. Many possible events or factors could affect the future financial results and performance of the Company. This could cause results or performance to differ materially from those expressed in the forward-looking statements. Words such as "expects", "anticipates", "believes", "estimates", variations of such words and other similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in, or implied by, such forward-looking statements. Readers should not rely solely on the forward-looking statements and should consider all uncertainties and risks discussed throughout this report. Forward-looking statements speak only as of the date they are made. The Company does not undertake to update forward-looking statements to reflect circumstances or events that occur after the date the forward-looking statements are made or to reflect the occurrence of unanticipated events. Such possible events or factors include: changes in economic conditions in the Company's market area, changes in policies by regulatory agencies, governmental legislation and regulation, fluctuations in interest rates, changes in liquidity requirements, demand for loans in the Company's market area, failure of litigation settlement agreements to become final in accordance with their terms, and competition with other entities that offer financial services.

Critical Accounting Policies

The Company has identified several policies as being critical because they require management to make particularly difficult, subjective and/or complex judgments about matters that are inherently uncertain and because of the likelihood that materially different amounts would be reported under different conditions or using different assumptions. These policies relate to the allowance for loan losses, the valuation of certain investment securities, and accounting for income taxes. A discussion of these policies can be found in the sections captioned "Critical Accounting Policies" and "Allowance for Loan Losses" in Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's 2012 Annual Report on Form 10-K. There have been no changes in the Company's application of critical accounting policies since December 31, 2012.

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## Selected Financial Data

|                                                       | Three Months Ended |           | Six Months Ended |           |
|-------------------------------------------------------|--------------------|-----------|------------------|-----------|
|                                                       | June 30            |           | June 30          |           |
|                                                       | 2013               | 2012      | 2013             | 2012      |
| <b>Per Share Data</b>                                 |                    |           |                  |           |
| Net income per common share — basic                   | \$ .72             | \$ .77    | \$ 1.39          | \$ 1.47   |
| Net income per common share — diluted                 | .72                | .76       | 1.39             | 1.46      |
| Cash dividends                                        | .225               | .219      | .450             | .438      |
| Book value                                            |                    |           | 23.23            | 24.26     |
| Market price                                          |                    |           | 43.55            | 36.10     |
| <b>Selected Ratios</b>                                |                    |           |                  |           |
| (Based on average balance sheets)                     |                    |           |                  |           |
| Loans to deposits <sup>(1)</sup>                      | 56.68              | % 55.26 % | 55.66            | % 55.39 % |
| Non-interest bearing deposits to total deposits       | 32.30              | 32.29     | 32.55            | 31.61     |
| Equity to loans <sup>(1)</sup>                        | 21.60              | 24.04     | 21.80            | 23.95     |
| Equity to deposits                                    | 12.24              | 13.28     | 12.13            | 13.27     |
| Equity to total assets                                | 9.97               | 10.82     | 9.95             | 10.78     |
| Return on total assets                                | 1.20               | 1.38      | 1.17             | 1.34      |
| Return on total equity                                | 12.07              | 12.80     | 11.73            | 12.42     |
| (Based on end-of-period data)                         |                    |           |                  |           |
| Non-interest income to revenue <sup>(2)</sup>         | 39.17              | 37.91     | 39.53            | 37.56     |
| Efficiency ratio <sup>(3)</sup>                       | 59.73              | 58.53     | 60.72            | 58.72     |
| Tier I risk-based capital ratio                       |                    |           | 13.58            | 14.80     |
| Total risk-based capital ratio                        |                    |           | 14.85            | 16.13     |
| Tangible common equity to assets ratio <sup>(4)</sup> |                    |           | 9.06             | 10.16     |
| Tier I leverage ratio                                 |                    |           | 9.08             | 9.73      |

(1) Includes loans held for sale.

(2) Revenue includes net interest income and non-interest income.

(3) The efficiency ratio is calculated as non-interest expense (excluding intangibles amortization) as a percent of revenue.

(4) The tangible common equity ratio is calculated as stockholders' equity reduced by goodwill and other intangible assets (excluding mortgage servicing rights) divided by total assets reduced by goodwill and other intangible assets (excluding mortgage servicing rights).



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## Results of Operations

## Summary

| (Dollars in thousands)                               | Three Months Ended June 30 |            |          | Six Months Ended June 30 |            |          |
|------------------------------------------------------|----------------------------|------------|----------|--------------------------|------------|----------|
|                                                      | 2013                       | 2012       | % change | 2013                     | 2012       | % change |
| Net interest income                                  | \$159,458                  | \$165,105  | (3.4 )%  | \$309,801                | \$324,842  | (4.6 )%  |
| Provision for loan losses                            | (7,379 )                   | (5,215 )   | 41.5     | (10,664 )                | (13,380 )  | (20.3 )  |
| Non-interest income                                  | 102,676                    | 100,816    | 1.8      | 202,553                  | 195,399    | 3.7      |
| Investment securities gains (losses), net            | (1,568 )                   | 1,336      | N.M.     | (3,733 )                 | 5,376      | N.M.     |
| Non-interest expense                                 | (156,966 )                 | (156,340 ) | .4       | (312,003 )               | (306,801 ) | 1.7      |
| Income taxes                                         | (30,182 )                  | (34,466 )  | (12.4 )  | (59,107 )                | (67,386 )  | (12.3 )  |
| Non-controlling interest expense                     | (234 )                     | (503 )     | (53.5 )  | (25 )                    | (1,518 )   | (98.4 )  |
| Net income attributable to Commerce Bancshares, Inc. | \$65,805                   | \$70,733   | (7.0 )%  | \$126,822                | \$136,532  | (7.1 )%  |

For the quarter ended June 30, 2013, net income attributable to Commerce Bancshares, Inc. (net income) amounted to \$65.8 million, a decrease of \$4.9 million, or 7.0%, compared to the second quarter of the previous year, and an increase of \$4.8 million, or 7.8%, compared to the previous quarter. For the current quarter, the annualized return on average assets was 1.20%, the annualized return on average equity was 12.07%, and the efficiency ratio was 59.73%. Diluted earnings per share was \$.72, a decrease of 5.3% compared to \$.76 per share in the second quarter of 2012, and an increase of 7.5% compared to \$.67 in the previous quarter.

Compared to the second quarter of last year, net interest income decreased \$5.6 million, or 3.4%, partly due to a decrease of \$4.3 million in interest on investment securities (mainly in mortgage-backed securities). This decline was partly offset by the reclassification of \$2.6 million of interest received on the sale of a private equity investment which had been previously recorded as securities gains. Interest income on loans decreased \$4.2 million (mainly in business and business real estate loans). These declines in interest income were partly offset by a decrease of \$1.8 million in interest expense on deposits. The provision for loan losses totaled \$7.4 million for the current quarter, representing an increase of \$2.2 million, or 41.5%, over the second quarter of 2012. Non-interest income increased \$1.9 million, or 1.8%, due to continued growth in bank card and trust fee income, while non-interest expense remained flat. Net investment securities losses for the second quarter of 2013 amounted to \$1.6 million compared to net gains of \$1.3 million during the second quarter of last year. The current quarter losses included the previously mentioned reclassification, partly offset by a gain of \$1.4 million resulting from the donation of appreciated securities.

Net income for the first six months of 2013 was \$126.8 million, a decrease of \$9.7 million, or 7.1%, from the same period last year. Diluted earnings per share was \$1.39, a decrease of 4.8% compared to \$1.46 per share in the same period last year. For the first six months of 2013, the annualized return on average assets was 1.17%, the annualized return on average equity was 11.73%, and the efficiency ratio was 60.72%. Net interest income declined \$15.0 million, or 4.6%, from the same period last year due to lower earnings on the loan and investment securities portfolios of \$8.2 million and \$13.1 million, respectively. These declines in income were partially offset by an increase of \$2.8 million in interest income on long-term resell agreements and a decline of \$3.5 million in deposit interest expense. The provision for loan losses was \$10.7 million for the first six months of 2013, down \$2.7 million from the same period last year. Non-interest income increased by \$7.2 million, or 3.7%, over the same period as last year due to continued growth bank card and trust fee income. Non-interest expense increased by \$5.2 million due to increases in salaries and employee benefits expense and data processing and software costs. Net investment securities losses were \$3.7 million in the first six months of 2013 compared to net securities gains of \$5.4 million in the first six months of 2012. The higher losses were largely due to lower gains in fair value on private equity securities and the interest reclassification mentioned above, partly offset by the securities donation gain.



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## Net Interest Income

The following table summarizes the changes in net interest income on a fully taxable equivalent basis, by major category of interest earning assets and interest bearing liabilities, identifying changes related to volumes and rates. Changes not solely due to volume or rate changes are allocated to rate.

## Analysis of Changes in Net Interest Income

| (In thousands)                                               | Three Months Ended June 30,<br>2013 vs. 2012 |                 |            | Six Months Ended June 30,<br>2013 vs. 2012 |                 |             |
|--------------------------------------------------------------|----------------------------------------------|-----------------|------------|--------------------------------------------|-----------------|-------------|
|                                                              | Change due to<br>Average Volume              | Average<br>Rate | Total      | Change due to<br>Average Volume            | Average<br>Rate | Total       |
| Interest income, fully taxable equivalent basis:             |                                              |                 |            |                                            |                 |             |
| Loans                                                        | \$ 10,631                                    | \$(14,752)      | \$(4,121 ) | \$ 19,008                                  | \$(27,050 )     | \$(8,042 )  |
| Loans held for sale                                          | —                                            | 3               | 3          | (28 )                                      | 11              | (17 )       |
| Investment securities:                                       |                                              |                 |            |                                            |                 |             |
| U.S. government and federal agency securities                | 1,311                                        | (2,404 )        | (1,093 )   | 1,674                                      | (5,050 )        | (3,376 )    |
| Government-sponsored enterprise obligations                  | 891                                          | (347 )          | 544        | 1,804                                      | (530 )          | 1,274       |
| State and municipal obligations                              | 3,124                                        | (1,651 )        | 1,473      | 6,613                                      | (3,273 )        | 3,340       |
| Mortgage-backed securities                                   | (5,315 )                                     | (913 )          | (6,228 )   | (10,074 )                                  | (3,349 )        | (13,423 )   |
| Asset-backed securities                                      | 843                                          | (1,684 )        | (841 )     | 2,104                                      | (3,579 )        | (1,475 )    |
| Other securities                                             | 624                                          | 1,483           | 2,107      | 954                                        | 256             | 1,210       |
| Total interest on investment securities                      | 1,478                                        | (5,516 )        | (4,038 )   | 3,075                                      | (15,525 )       | (12,450 )   |
| Short-term federal funds sold and securities purchased under |                                              |                 |            |                                            |                 |             |
| agreements to resell                                         | 2                                            | (3 )            | (1 )       | (5 )                                       | (4 )            | (9 )        |
| Long-term securities purchased under agreements to resell    | 1,894                                        | (666 )          | 1,228      | 3,533                                      | (751 )          | 2,782       |
| Interest earning deposits with banks                         | (33 )                                        | (4 )            | (37 )      | (3 )                                       | (12 )           | (15 )       |
| Total interest income                                        | 13,972                                       | (20,938 )       | (6,966 )   | 25,580                                     | (43,331 )       | (17,751 )   |
| Interest expense:                                            |                                              |                 |            |                                            |                 |             |
| Deposits:                                                    |                                              |                 |            |                                            |                 |             |
| Savings                                                      | 17                                           | (24 )           | (7 )       | 38                                         | (71 )           | (33 )       |
| Interest checking and money market                           | 273                                          | (1,525 )        | (1,252 )   | 759                                        | (3,142 )        | (2,383 )    |
| Time open & C.D.'s of less than \$100,000                    | (127 )                                       | (221 )          | (348 )     | (272 )                                     | (433 )          | (705 )      |
| Time open & C.D.'s of \$100,000 and over                     | 105                                          | (266 )          | (161 )     | (22 )                                      | (351 )          | (373 )      |
| Total interest on deposits                                   | 268                                          | (2,036 )        | (1,768 )   | 503                                        | (3,997 )        | (3,494 )    |
| Federal funds purchased and securities sold under            |                                              |                 |            |                                            |                 |             |
| agreements to repurchase                                     | 155                                          | (62 )           | 93         | 108                                        | (22 )           | 86          |
| Other borrowings                                             | 41                                           | (88 )           | (47 )      | 61                                         | (202 )          | (141 )      |
| Total interest expense                                       | 464                                          | (2,186 )        | (1,722 )   | 672                                        | (4,221 )        | (3,549 )    |
| Net interest income, fully taxable equivalent basis          | \$ 13,508                                    | \$(18,752)      | \$(5,244 ) | \$ 24,908                                  | \$(39,110 )     | \$(14,202 ) |

Net interest income for the second quarter of 2013 was \$159.5 million, a \$5.6 million decline from the second quarter of 2012. On a tax equivalent (T/E) basis, net interest income totaled \$165.9 million in the second quarter of 2013, up \$9.2 million over the previous quarter and down \$5.2 million from the second quarter of 2012. The decline from the same period last year was mainly the result of lower yields on loans and investment securities in the current quarter, which were partly offset by lower rates paid on deposits and higher loan balances. The Company's net interest rate margin was 3.21% in the second quarter of 2013, compared to 3.07% in the previous quarter and 3.55% in the second

quarter of 2012.

Total interest income (T/E) decreased \$7.0 million, or 3.9%, from the second quarter of 2012. Interest income on loans, including loans held for sale, declined \$4.1 million due to a 61 basis point decrease in average rates earned, while average loan balances increased 9.5%. The higher balances contributed \$10.6 million to interest income and occurred mainly in business, consumer and personal real estate loans. The overall average rate earned on total loans declined to 4.34% during the current quarter compared to 4.95% in the second quarter of 2012, which resulted in a \$14.8 million decrease in interest income. Most of the rate impact occurred in business, consumer, business real estate and personal real estate loans. The average rate earned on business real estate loans decreased 51 basis points, with a minor increase in average balances. The average yield on personal real estate loans declined 49 basis points, while the average balance increased \$189.1 million, or 12.8%. Average business loans increased \$358.4 million,

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or 12.4%, which was offset by a decline of 51 basis points in rates earned. Average consumer loans increased \$296.0 million, while the average yield fell 104 basis points. Most of the increase in consumer loan balances resulted from higher auto and fixed-rate home equity loans, which were partly offset by a decrease of \$84.5 million in marine and RV loans as that portfolio continues to pay down (since the Company no longer originates these types of loans). Average consumer credit card loans increased \$29.1 million compared to the second quarter of 2012, while the average rate earned on these balances decreased to 11.20% from 11.87%.

Interest income on investment securities (T/E) was \$58.2 million during the second quarter of 2013 compared to \$62.2 million during the same period last year, which was a decrease of \$4.0 million. This decline included a \$1.1 million decrease in inflation interest on the Company's inflation-protected securities (TIPS) as a result of the lower consumer Price Indices published this quarter, on which this interest is based. Also, lower average rates were earned on the remainder of the available for sale portfolio, especially in state and municipal and asset-backed securities with rate declines of 42 and 22 basis points, respectively. These declines were partly offset by the recognition of \$2.6 million in interest income upon the sale of a private equity investment (classified as non-marketable in the accompanying consolidated balance sheet) which had been recorded in previous periods as securities gains. The average balance of the total portfolio (excluding fair value adjustments) increased \$163.8 million, or 1.8%, compared to the second quarter of 2012. This growth mainly occurred in state and municipal obligations, asset-backed securities, and government sponsored obligations, which increased by \$311.2 million, \$299.3 million and \$173.5 million, respectively, while the average balance of mortgage-backed securities declined \$737.7 million. The effect of the higher average total portfolio balance was offset by a lower overall average yield, which declined to 2.52% compared to 2.75% during the second quarter of 2012.

Interest income on long-term securities purchased under agreements to resell increased \$1.2 million over the second quarter of 2012. This increase included \$265 thousand of interest on collateral swaps, which are discussed in Note 12 to the consolidated financial statements. The remainder of the increase was due to higher average balances of other resell agreements, which increased \$350.0 million, or 41.2%.

The average tax equivalent yield on total interest earning assets was 3.36% in the second quarter of 2013 compared to 3.75% in the second quarter of 2012.

Total interest expense decreased \$1.7 million, or 18.1%, compared to the second quarter of 2012, mainly due to a \$1.8 million decrease in interest expense on interest bearing deposits. The decrease in interest expense on deposits resulted primarily from declines of 7 basis points in average rates paid on money market accounts and 12 basis point in rates paid on certificates of deposit. Total average interest bearing deposits increased \$757.3 million, or 6.7%, over the second quarter of 2012, as money market account balances increased \$490.0 million, or 6.1%, and certificate of deposit balances increased \$138.1 million, or 5.8% (mainly in short-term jumbo certificates of deposit). The overall average rate incurred on all interest bearing liabilities decreased to .23% in the second quarter of 2013 compared to .30% in the second quarter of 2012.

Net interest income (T/E) for the first six months of 2013 was \$322.7 million compared to \$336.9 million for the same period in 2012. For the first six months of 2013, the net yield on total interest earning assets on a tax equivalent basis was 3.14% compared to 3.50% in the first six months of 2012.

Total interest income (T/E) for the first six months of 2013 decreased \$17.8 million from the same period last year, due to lower loan and investment securities yields offset by lower rates paid on deposits and higher loan balances. Loan interest income (T/E) fell \$8.1 million overall due to 53 basis point decrease in the average rate earned, partly offset by a \$770.8 million, or 8.3%, increase in total average loan balances. Investment securities interest income (T/E) fell \$12.5 million overall due to a 34 basis point decline in the average yield (including a decline of \$3.1 million in TIPS income), offset by an increase in average balances of \$277.1 million, or 3.0%. In addition, income on long-term resell agreements rose \$2.8 million over the prior period, largely due to higher average balances and higher collateral swap income included in this category.

Total interest expense for the first six months of 2013 declined \$3.5 million compared to last year, largely due to lower rates paid on interest bearing deposits. Interest expense on money market accounts decreased \$2.4 million (mainly due to a decline of 7 basis points in rates paid), while interest expense on certificates of deposits declined \$1.1 million (due to a decline of 9 basis points). The overall cost of total interest bearing liabilities decreased to .24%

compared to .31% in the same period in the prior year.

Summaries of average assets and liabilities and the corresponding average rates earned/paid appear on the last page of this discussion.

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## Non-Interest Income

| (Dollars in thousands)                       | Three Months Ended June 30 |           |          | Six Months Ended June 30 |           |          |
|----------------------------------------------|----------------------------|-----------|----------|--------------------------|-----------|----------|
|                                              | 2013                       | 2012      | % change | 2013                     | 2012      | % change |
| Bank card transaction fees                   | \$40,700                   | \$38,434  | 5.9 %    | \$79,250                 | \$73,167  | 8.3 %    |
| Trust fees                                   | 25,734                     | 23,833    | 8.0      | 50,903                   | 46,647    | 9.1      |
| Deposit account charges and other fees       | 19,602                     | 19,975    | (1.9 )   | 38,314                   | 39,311    | (2.5 )   |
| Capital market fees                          | 3,305                      | 5,010     | (34.0 )  | 7,696                    | 11,881    | (35.2 )  |
| Consumer brokerage services                  | 2,853                      | 2,576     | 10.8     | 5,539                    | 5,102     | 8.6      |
| Loan fees and sales                          | 1,314                      | 1,706     | (23.0 )  | 2,787                    | 3,267     | (14.7 )  |
| Other                                        | 9,168                      | 9,282     | (1.2 )   | 18,064                   | 16,024    | 12.7     |
| Total non-interest income                    | \$102,676                  | \$100,816 | 1.8 %    | \$202,553                | \$195,399 | 3.7 %    |
| Non-interest income as a % of total revenue* | 39.2                       | %37.9     | %        | 39.5                     | %37.6     | %        |

\* Total revenue includes net interest income and non-interest income.

For the second quarter of 2013, total non-interest income amounted to \$102.7 million compared with \$100.8 million in the same quarter last year, which was an increase of \$1.9 million, or 1.8%. Bank card fees for the quarter increased \$2.3 million, or 5.9%, over the second quarter of last year, as a result of an 8.6% increase in corporate card fees, which totaled \$19.3 million this quarter. Credit card fees also grew by 5.8% and totaled \$5.9 million this quarter, while debit card fees grew 3.2% and totaled \$9.0 million. Trust fees for the quarter increased \$1.9 million, or 8.0%, over the same quarter last year, resulting mainly from growth in personal (up 9.3%) and institutional (up 7.9%) trust fees. Deposit account fees declined \$373 thousand, or 1.9%, compared to last year as overdraft fees declined by \$1.2 million, but were partly offset by combined growth in corporate cash management fees and other deposit fees of \$847 thousand, or 7.5%. Capital market fees for the current quarter decreased \$1.7 million, to \$3.3 million, as demand from correspondent banks and other customers slowed later in the second quarter of 2013. Consumer brokerage services revenue increased \$277 thousand, or 10.8%, while loan fees and sales revenue was down \$392 thousand, or 23.0%.

Non-interest income for the first six months of 2013 was \$202.6 million compared to \$195.4 million in the first six months of 2012, resulting in an increase of \$7.2 million, or 3.7%. Bank card fees increased \$6.1 million, or 8.3%, as a result of growth in corporate card fees of \$4.6 million, or 13.7%. In addition, higher transaction volumes resulted in growth of 6.9% in merchant fees, while credit card fees increased by 5.7%. Trust fee income increased \$4.3 million, or 9.1%, as a result of growth in both personal and institutional trust fees. Deposit account fees decreased \$997 thousand, or 2.5%, mainly due to a decline in overdraft and return item fees of \$2.2 million. This decline was mainly the result of a new posting routine on debit transactions which took effect in February. The change is currently expected to reduce overdraft fees by \$3.3 million to \$5.5 million on an annualized basis, which is a lower impact than originally estimated. Helping to offset this effect was an increase in various other deposit fees and cash management fees of \$1.2 million. Capital market fees decreased \$4.2 million, or 35.2%, and were impacted by rising rates and loan demand at correspondent banks. Consumer brokerage services revenue increased by \$437 thousand, or 8.6%, mainly due to growth in advisory fees, partly offset by lower fixed annuity fees. Loan fees and sales decreased \$480 thousand, or 14.7%, due to declines in student loan sales gains and loan commitment fees. Other non-interest income increased by \$2.0 million, or 12.7%, as a result of a \$3.0 million fair value loss recorded last year on an office building which was held for sale, partly offset by declines in the current period in tax credit sales income and lease syndication revenue.

## Investment Securities Gains (Losses), Net

Net gains and losses on investment securities which were recognized in earnings during the three months and six months ended June 30, 2013 and 2012 are shown in the table below. Net securities losses amounted to \$1.6 million in the second quarter of 2013, while net securities losses of \$3.7 million were recorded in the first six months of 2013. Included in these net losses are credit-related impairment losses on certain non-agency guaranteed mortgage-backed

securities which have been identified as other-than-temporarily impaired. These identified securities had a total fair value of \$86.2 million at June 30, 2013. During the current quarter, additional credit-related impairment losses of \$488 thousand were recorded, bringing the total credit-related impairment losses for the first six months of 2013 to \$930 thousand. The cumulative credit-related impairment loss initially recorded on these securities amounted to \$12.5 million. Also shown below are net gains and losses relating to non-marketable private equity investments, which are primarily held by the Parent's majority-owned private equity subsidiaries. These include fair value adjustments, in addition to gains and losses realized upon disposition. Most of the current quarter loss resulted from a \$2.6 million reclassification to interest income recorded upon the sale of a private equity investment, as mentioned above. The portion of the private equity activity attributable to minority interests is reported as non-controlling interest in the consolidated statements of income, and resulted in income of \$855 thousand during the first six months of 2013 and expense of \$1.2 million during the same period last year. Partly offsetting the current quarter losses was a \$1.4 million gain recorded by the Parent upon the donation of appreciated common stock.



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| (In thousands)                                  | Three Months Ended June 30 |           | Six Months Ended June 30 |           |
|-------------------------------------------------|----------------------------|-----------|--------------------------|-----------|
|                                                 | 2013                       | 2012      | 2013                     | 2012      |
| Available for sale:                             |                            |           |                          |           |
| Common stock                                    | \$1,375                    | \$—       | \$1,375                  | \$—       |
| Agency mortgage-backed bonds                    | —                          | —         | —                        | 342       |
| OTTI losses on non-agency mortgage-backed bonds | (488                       | ) (350    | ) (930                   | ) (670    |
| Non-marketable:                                 |                            |           |                          |           |
| Private equity investments                      | (2,455                     | ) 1,686   | (4,178                   | ) 5,704   |
| Total investment securities gains (losses), net | \$(1,568                   | ) \$1,336 | \$(3,733                 | ) \$5,376 |

## Non-Interest Expense

| (Dollars in thousands)         | Three Months Ended June 30 |           |          | Six Months Ended June 30 |           |          |
|--------------------------------|----------------------------|-----------|----------|--------------------------|-----------|----------|
|                                | 2013                       | 2012      | % change | 2013                     | 2012      | % change |
| Salaries and employee benefits | \$89,569                   | \$87,511  | 2.4 %    | \$180,450                | \$177,054 | 1.9 %    |
| Net occupancy                  | 11,234                     | 11,105    | 1.2      | 22,469                   | 22,365    | .5       |
| Equipment                      | 4,680                      | 4,999     | (6.4 )   | 9,363                    | 10,188    | (8.1 )   |
| Supplies and communication     | 5,797                      | 5,667     | 2.3      | 11,386                   | 11,280    | .9       |
| Data processing and software   | 19,584                     | 18,282    | 7.1      | 38,535                   | 35,751    | 7.8      |
| Marketing                      | 4,048                      | 4,469     | (9.4 )   | 7,407                    | 8,291     | (10.7 )  |
| Deposit insurance              | 2,790                      | 2,618     | 6.6      | 5,557                    | 5,138     | 8.2      |
| Other                          | 19,264                     | 21,689    | (11.2 )  | 36,836                   | 36,734    | .3       |
| Total non-interest expense     | \$156,966                  | \$156,340 | .4 %     | \$312,003                | \$306,801 | 1.7 %    |

Non-interest expense for the second quarter of 2013 amounted to \$157.0 million, an increase of \$626 thousand, or .4%, compared with \$156.3 million in the second quarter of last year. Salaries and benefits expense increased \$2.1 million, or 2.4%, mainly due to an increase in salary costs of \$2.5 million, or 4.2%, partly offset by lower medical costs of \$988 thousand. Growth in salaries expense resulted from added staffing mainly in the areas of commercial banking, wealth and commercial card. Full-time equivalent employees totaled 4,720 at June 30, 2013 compared to 4,702 at June 30, 2012. Equipment expense declined \$319 thousand due to lower depreciation expense, while a reduction in marketing expenditures resulted in a decline of \$421 thousand in expense. Data processing and software costs increased \$1.3 million, or 7.1%, partly due to higher variable processing costs related to commercial card revenues. Occupancy and supplies and communication costs increased a total of \$259 thousand, or 1.5%, and deposit insurance expense changed slightly, increasing \$172 thousand. Other non-interest expense decreased \$2.4 million compared to the second quarter of last year, mainly due to a \$5.7 million charge last year related to certain Visa litigation that did not reoccur in 2013. This decline was partly offset by a \$1.2 million increase in legal, loan collection and professional fees in the current quarter. Other non-interest expense also included a provision of \$898 thousand on a letter of credit exposure, in addition to donation expense of \$1.5 million related to appreciated stock, as mentioned above.

For the first six months of 2013, non-interest expense amounted to \$312.0 million, an increase of \$5.2 million, or 1.7%, compared with \$306.8 million in the same period last year. Salaries and benefits expense increased by \$3.4 million, or 1.9%, mainly due to higher salaries expense, partly offset by lower medical and incentives expense. Occupancy expense increased \$104 thousand, or .5%, while supplies and communication expense increased \$106 thousand, or .9%. Equipment expense decreased \$825 thousand, or 8.1%, due to lower depreciation expense. Data processing and software expense increased \$2.8 million, or 7.8%, mainly due to higher bank card processing expense. Marketing expense declined \$884 thousand, or 10.7%, while deposit insurance increased by \$419 thousand, or 8.2%. Other non-interest expense increased slightly over the prior period, resulting from provisions of \$1.9 million on letter

of credit exposures, the stock donation expense mentioned above, higher legal and professional fees, and card network incentives of \$1.1 million received in 2012 upon contract renegotiations. These expense increases were partly offset by higher gains on sales of foreclosed property in the current period, in addition to the prior year Visa litigation charge of \$5.7 million.

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## Provision and Allowance for Loan Losses

| (In thousands)                     | Three Months Ended |                  |                  | Six Months Ended |                 |
|------------------------------------|--------------------|------------------|------------------|------------------|-----------------|
|                                    | June 30,<br>2013   | Mar. 31,<br>2013 | June 30,<br>2012 | June 30<br>2013  | June 30<br>2012 |
| Provision for loan losses          | \$7,379            | \$3,285          | \$5,215          | \$10,664         | \$13,380        |
| Net loan charge-offs (recoveries): |                    |                  |                  |                  |                 |
| Business                           | (87                | )(50             | )(3,600          | (137             | )(3,490         |
| Real estate-construction and land  | (744               | )(532            | )116             | (1,276           | )336            |
| Real estate-business               | 1,253              | (104             | )1,839           | 1,149            | 3,334           |
| Consumer credit card               | 6,935              | 6,048            | 5,930            | 12,983           | 12,103          |
| Consumer                           | 1,452              | 1,709            | 1,974            | 3,161            | 4,605           |
| Revolving home equity              | 156                | 139              | 943              | 295              | 1,303           |
| Real estate-personal               | 172                | 373              | 679              | 545              | 748             |
| Overdrafts                         | 242                | 202              | 333              | 444              | 440             |
| Total net loan charge-offs         | \$9,379            | \$7,785          | \$8,214          | \$17,164         | \$19,379        |

|                                                | Three Months Ended |                  |                  | Six Months Ended |                 |
|------------------------------------------------|--------------------|------------------|------------------|------------------|-----------------|
|                                                | June 30,<br>2013   | Mar. 31,<br>2013 | June 30,<br>2012 | June 30<br>2013  | June 30<br>2012 |
| Annualized net loan charge-offs (recoveries)*: |                    |                  |                  |                  |                 |
| Business                                       | (.01               | )%(.01           | )%(.50           | )%(.01           | )%(.24          |
| Real estate-construction and land              | (.80               | )(.61            | ) .13            | (.71             | ) .18           |
| Real estate-business                           | .23                | (.02             | ) .34            | .10              | .31             |
| Consumer credit card                           | 3.75               | 3.25             | 3.35             | 3.50             | 3.37            |
| Consumer                                       | .41                | .52              | .70              | .46              | .83             |
| Revolving home equity                          | .15                | .13              | .84              | .14              | .58             |
| Real estate-personal                           | .04                | .09              | .19              | .07              | .10             |
| Overdrafts                                     | 15.24              | 15.15            | 23.65            | 15.20            | 13.36           |
| Total annualized net loan charge-offs          | .37                | % .32            | % .36            | % .35            | % .42           |

\* as a percentage of average loans (excluding loans held for sale)

The Company has an established process to determine the amount of the allowance for loan losses, which assesses the risks and losses inherent in its portfolio. This process provides an allowance consisting of a specific allowance component based on certain individually evaluated loans and a general component based on estimates of allowances for pools of loans.

Loans subject to individual evaluation generally consist of business, construction, business real estate and personal real estate loans on non-accrual status and include troubled debt restructurings that are on non-accrual status. These non-accrual loans are evaluated individually for impairment based on factors such as payment history, borrower financial condition, collateral, current economic conditions and loss experience. For collateral dependent loans, appraisals of collateral (including exit costs) are normally obtained annually but discounted based on date last received and market conditions. From these evaluations of expected cash flows and collateral values, specific allowances are determined.

Loans which are not individually evaluated are segregated by loan type and sub-type and are collectively evaluated. These loans include commercial loans (business, construction and business real estate) which have been graded pass, special mention or substandard and all personal banking loans, except personal real estate loans on non-accrual status.

Collectively-evaluated loans include certain troubled debt restructurings with similar risk characteristics. Allowances determined for personal banking loans, which are generally smaller balance homogeneous type loans, use consistent methodologies which consider historical and current loss trends, delinquencies and current economic conditions.

Allowances for commercial type loans, which are generally larger and more complex in structure with more unpredictable loss characteristics, use methods which consider historical and current loss trends, current loan grades, delinquencies, industry concentrations, economic conditions throughout the Company's markets as monitored by Company credit officers, and general economic conditions.

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The Company's estimate of the allowance for loan losses and the corresponding provision for loan losses is based upon various judgments and assumptions made by management. Factors that influence these judgments include past loan loss experience, current loan portfolio composition and characteristics, trends in delinquencies, portfolio risk ratings, levels of non-performing assets, and prevailing regional and national economic conditions. The Company has internal credit administration and loan review staffs that continuously review loan quality and report the results of their reviews and examinations to the Company's senior management and Board of Directors. Such reviews also assist management in establishing the level of the allowance. In using this process and the information available, management must consider various assumptions and exercise considerable judgment to determine the overall level of the allowance for loan losses. Because of these subjective factors, actual outcomes of inherent losses can differ from original estimates. The Company's subsidiary bank continues to be subject to examination by several regulatory agencies, and examinations are conducted throughout the year, targeting various segments of the loan portfolio for review. Note 1 in the 2012 Annual Report on Form 10-K contains additional discussion on the allowance and charge-off policies.

Net loan charge-offs in the second quarter of 2013 amounted to \$9.4 million, compared with \$7.8 million in the prior quarter and \$8.2 million in the second quarter of last year. Compared to the previous quarter, net charge-offs increased in the business real estate and consumer credit card categories by \$1.4 million and \$887 thousand, respectively. Most of the increase in business real estate charge-offs related to a single borrower. These increases were partially offset by lower net charge-offs recorded in the consumer and personal real estate categories, which declined \$257 thousand and \$201 thousand, respectively. Additionally, net recoveries on construction and land loans increased \$212 thousand. For the three months ended June 30, 2013, the ratio of annualized total net loan charge-offs to total average loans was .37%, compared to .32% in the previous quarter and .36% in the same quarter last year.

For the second quarter of 2013, annualized net charge-offs on average consumer credit card loans amounted to 3.75%, compared with 3.25% in the previous quarter and 3.35% in the same period last year. Consumer loan net charge-offs for the quarter amounted to .41% of average consumer loans, compared to .52% in the previous quarter and .70% in the same quarter last year. Annualized net charge-offs on business real estate loans increased to .23% compared to net recoveries of .02% in the previous quarter, but decreased from net charge-offs of .34% in the same period last year.

The provision for loan losses for the current quarter totaled \$7.4 million, an increase of \$4.1 million over the previous quarter and \$2.2 million over the same period last year. The current quarter provision for loan losses was \$2.0 million less than net loan charge-offs for the current quarter, thereby reducing the allowance for loan losses to \$166.0 million. At June 30, 2013, the allowance was 1.60% of total loans, excluding loans held for sale, and was 425% of total non-accrual loans.

Net charge-offs during the first six months of 2013 were \$17.2 million compared to \$19.4 million in the same period of 2012. The \$2.2 million decrease was due to lower net charge-offs in the current period in most loan categories except business loans, where net recoveries were significantly lower in 2013 as a result of two large recoveries in the second quarter of 2012.

#### Risk Elements of Loan Portfolio

The following table presents non-performing assets and loans which are past due 90 days and still accruing interest. Non-performing assets include non-accruing loans and foreclosed real estate. Loans are placed on non-accrual status when management does not expect to collect payments consistent with acceptable and agreed upon terms of repayment. Loans that are 90 days past due as to principal and/or interest payments are generally placed on non-accrual, unless they are both well-secured and in the process of collection, or they are personal banking loans that are exempt under regulatory rules from being classified as non-accrual.

(Dollars in thousands)

|                                                          | June 30,<br>2013 | December 31,<br>2012 |   |
|----------------------------------------------------------|------------------|----------------------|---|
| Non-accrual loans                                        | \$39,092         | \$51,410             |   |
| Foreclosed real estate                                   | 13,434           | 13,453               |   |
| Total non-performing assets                              | \$52,526         | \$64,863             |   |
| Non-performing assets as a percentage of total loans     | .51              | %.66                 | % |
| Non-performing assets as a percentage of total assets    | .24              | %.29                 | % |
| Total loans past due 90 days and still accruing interest | \$12,509         | \$15,347             |   |

Non-accrual loans, which are also classified as impaired, totaled \$39.1 million at June 30, 2013, and decreased \$12.3 million from December 31, 2012. The decline from December 31, 2012 occurred mainly in business real estate and construction and land non-accrual loans, which decreased \$4.6 million and \$3.5 million, respectively. At June 30, 2013, non-accrual loans were comprised mainly of business real estate (32.6%), business (29.0%), and construction and land (26.0%) loans. Foreclosed real estate totaled \$13.4 million at June 30, 2013, a decrease of \$19 thousand when compared to December 31, 2012. Total loans past due 90 days

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or more and still accruing interest were \$12.5 million as of June 30, 2013, a decrease of \$2.8 million when compared to December 31, 2012. Balances by class for loans non-accrual loans and loans past due 90 days and still accruing interest is shown in the "Delinquent and non-accrual loans" section in Note 3 to the consolidated financial statements.

In addition to the non-performing and past due loans mentioned above, the Company also has identified loans for which management has concerns about the ability of the borrowers to meet existing repayment terms. They are classified as substandard under the Company's internal rating system. The loans are generally secured by either real estate or other borrower assets, reducing the potential for loss should they become non-performing. Although these loans are generally identified as potential problem loans, they may never become non-performing. Such loans totaled \$127.0 million at June 30, 2013 compared with \$141.9 million at December 31, 2012, resulting in a decrease of \$14.9 million, or 10.5%. The change in potential problem loans was largely due to decreases of \$5.7 million in business loans, \$4.2 million in personal real estate loans, and \$4.1 million in construction and land loans.

| (In thousands)                      | June 30,<br>2013 | December 31,<br>2012 |
|-------------------------------------|------------------|----------------------|
| Potential problem loans:            |                  |                      |
| Business                            | \$39,175         | \$ 44,881            |
| Real estate – construction and land | 29,659           | 33,762               |
| Real estate – business              | 54,461           | 55,362               |
| Real estate – personal              | 3,668            | 7,891                |
| Total potential problem loans       | \$126,963        | \$ 141,896           |

At June 30, 2013, the Company had \$89.5 million of loans whose terms have been modified or restructured under a troubled debt restructuring. These loans have been extended to borrowers who are experiencing financial difficulty and who have been granted a concession, as defined by accounting guidance. Of this balance, \$23.1 million have been placed on non-accrual status. Of the remaining \$66.3 million, approximately \$43.5 million were commercial loans (business, construction and business real estate) classified as substandard, which were renewed at interest rates that were not judged to be market rates for new debt with similar risk. These loans are performing under their modified terms, and the Company believes it probable that all amounts due under the modified terms of the agreements will be collected. However, because of their substandard classification, they are included as potential problem loans in the table above. An additional \$13.1 million in troubled debt restructurings were composed of certain credit card loans under various debt management and assistance programs. Other restructured loans include \$9.7 million of personal banking loans which were not reaffirmed in bankruptcy, on which the borrowers are continuing to make payments.

#### Loans with Special Risk Characteristics

Management relies primarily on an internal risk rating system, in addition to delinquency status, to assess risk in the loan portfolio, and these statistics are presented in Note 3 to the consolidated financial statements. However, certain types of loans are considered at high risk of loss due to their terms, location, or special conditions. Additional information about the major types of loans in these categories and their risk features are provided below. Information based on loan-to-value (LTV) ratios was generally calculated with valuations at loan origination date. The Company does not attempt to obtain updated appraisals or valuations unless the loans become significantly delinquent or are in the process of being foreclosed upon.

#### Real Estate – Construction and Land Loans

The Company's portfolio of construction and land loans, as shown in the table below, amounted to 3.8% of total loans outstanding at June 30, 2013.

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| (Dollars in thousands)                          | June 30,<br>2013 | % of<br>Total<br>Loans | % of<br>Total<br>Loans | December 31,<br>2012 | % of<br>Total<br>Loans | % of<br>Total<br>Loans | % |
|-------------------------------------------------|------------------|------------------------|------------------------|----------------------|------------------------|------------------------|---|
| Residential land and land development           | \$67,956         | 17.0                   | %.7                    | %\$ 61,794           | 17.4                   | %.6                    | % |
| Residential construction                        | 76,651           | 19.2                   | .7                     | 68,590               | 19.2                   | .7                     |   |
| Commercial land and land development            | 85,568           | 21.5                   | .8                     | 83,491               | 23.5                   | .9                     |   |
| Commercial construction                         | 168,450          | 42.3                   | 1.6                    | 142,121              | 39.9                   | 1.4                    |   |
| Total real estate - construction and land loans | \$398,625        | 100.0                  | %3.8                   | %\$ 355,996          | 100.0                  | %3.6                   | % |



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## Real Estate – Business Loans

Total business real estate loans were \$2.2 billion at June 30, 2013 and comprised 21.3% of the Company's total loan portfolio. These loans include properties such as manufacturing and warehouse buildings, small office and medical buildings, churches, hotels and motels, shopping centers, and other commercial properties. At June 30, 2013, 46.9% of business real estate loans were for owner-occupied real estate properties, which present lower risk profiles.

| (Dollars in thousands)             | June 30,    |            | % of<br>Total<br>Loans | December 31,   |            | % of<br>Total<br>Loans |   |
|------------------------------------|-------------|------------|------------------------|----------------|------------|------------------------|---|
|                                    | 2013        | % of Total |                        | 2012           | % of Total |                        |   |
| Owner-occupied                     | \$1,037,297 | 46.9       | % 10.0                 | % \$ 1,035,407 | 46.7       | % 10.5                 | % |
| Office                             | 266,647     | 12.1       | 2.6                    | 269,756        | 12.2       | 2.7                    |   |
| Retail                             | 249,051     | 11.3       | 2.5                    | 245,021        | 11.1       | 2.5                    |   |
| Multi-family                       | 181,014     | 8.2        | 1.7                    | 184,208        | 8.3        | 1.9                    |   |
| Hotels                             | 150,108     | 6.8        | 1.4                    | 155,392        | 7.0        | 1.6                    |   |
| Farm                               | 128,267     | 5.8        | 1.2                    | 123,613        | 5.6        | 1.3                    |   |
| Industrial                         | 102,021     | 4.6        | 1.0                    | 110,645        | 5.0        | 1.1                    |   |
| Other                              | 95,855      | 4.3        | .9                     | 90,933         | 4.1        | .9                     |   |
| Total real estate - business loans | \$2,210,260 | 100.0      | % 21.3                 | % \$ 2,214,975 | 100.0      | % 22.5                 | % |

## Real Estate – Personal Loans

The Company's \$1.7 billion personal real estate loan portfolio is composed mainly of residential first mortgage real estate loans. As shown on page 47, recent loss rates have remained low, and at June 30, 2013, past due loans declined slightly and non-accrual loans declined \$2.0 million compared to December 31, 2012. Also, as shown in Note 3, only 5.1% of this portfolio has FICO scores of less than 660. Approximately \$16.3 million of personal real estate loans were structured with interest only payments. These loans are typically made to high net-worth borrowers and generally have low LTV ratios or have additional collateral pledged to secure the loan, and therefore, they are not perceived to represent above normal credit risk. At June 30, 2013, the Company had loans with no mortgage insurance and an original LTV higher than 80% totaling \$140.3 million compared to \$136.2 million at December 31, 2012.

## Revolving Home Equity Loans

The Company has \$422.9 million in revolving home equity loans at June 30, 2013 that are generally collateralized by residential real estate. Most of these loans (93.9%) are written with terms requiring interest only monthly payments. These loans are offered in three main product lines: LTV up to 80%, 80% to 90%, and 90% to 100%. As of June 30, 2013, the outstanding principal of loans with an original LTV higher than 80% was \$55.6 million, or 13% of the portfolio, compared to \$61.0 million as of December 31, 2012. Total revolving home equity loan balances over 30 days past due were \$2.2 million at June 30, 2013 compared to \$4.1 million at December 31, 2012. The weighted average FICO score for the total current portfolio balance is 765. At maturity, the accounts are re-underwritten and if they qualify under the Company's credit, collateral and capacity policies, the borrower is given the option to renew the line of credit, or to convert the outstanding balance to an amortizing loan. If criteria are not met, amortization is required, or the borrower may pay off the loan. During 2013 through 2016, approximately 53% of the Company's current outstanding balances are expected to mature. Of these balances, 84% have a FICO score above 700. The Company does not expect a significant increase in losses as these loans mature, due to their high FICO scores, low LTVs, and low historical loss levels.

## Fixed Rate Home Equity Loans

In addition to the residential real estate mortgage and the revolving home equity products mentioned above, the Company offers a third choice to those consumers desiring a fixed rate home equity loan with a fixed maturity date and a determined amortization schedule. The fixed rate home equity loan is typically used to finance a specific home repair or remodeling project. This portfolio of loans approximated \$257.7 million and \$210.1 million at June 30, 2013 and December 31, 2012, respectively. At the end of the second quarter of 2013, \$65.9 million of this portfolio had an LTV higher than 80%, up from a balance of \$54.0 million at the end of 2012.

At times, these loans are written with interest only monthly payments and a balloon payoff at maturity; however, such loans totaled less than 2% of the outstanding balance of fixed rate home equity loans at June 30, 2013. The Company has limited the offering of fixed rate home equity loans with LTV ratios over 90% during the past several years, and only \$5.5 million in new fixed rate home equity loans were written with these LTV ratios during the first half of 2013.

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Management does not believe these loans collateralized by real estate (personal real estate, revolving home equity, and fixed rate home equity) represent any unusual concentrations of risk, as evidenced by net charge-offs on these loans in the first half of 2013 of \$545 thousand, \$295 thousand, and \$124 thousand, respectively. The amount of any increased potential loss on high LTV agreements relates mainly to amounts advanced that are in excess of the 80% collateral calculation, not the entire approved line. The Company currently offers no subprime first mortgage or home equity loans. These are characterized as new loans to customers with FICO scores below 650 for home equity loans, 660 for government-insured first mortgages, and 680 for all other conventional first mortgages. The Company does not purchase brokered loans.

### Other Consumer Loans

Within the consumer loan portfolio are several direct and indirect product lines, comprised mainly of loans secured by automobiles, marine and RVs. Outstanding balances for these loans were \$990.0 million and \$897.5 million at June 30, 2013 and December 31, 2012, respectively. The balances over 30 days past due amounted to \$13.9 million at June 30, 2013 compared to \$11.8 million at the end of 2012. For the six months ended June 30, 2013, \$280.0 million of new automobile loans were originated, compared to \$440.2 million during the full year of 2012. The Company has curtailed new marine and RV loans since 2008, and at June 30, 2013, outstanding balances totaled \$287.6 million. The loss ratios experienced for marine and RV loans have been higher than other consumer loan products in recent years, and the annualized ratios were 1.0% and 2.0% in the first six months of 2013 and 2012, respectively.

Additionally, the Company offers low introductory rates on selected consumer credit card products. Out of a portfolio at June 30, 2013 of \$760.5 million in consumer credit card loans outstanding, approximately \$117.0 million, or 15.4%, carried a low introductory rate. Within the next six months, \$54.0 million of these loans are scheduled to convert to the ongoing higher contractual rate. To mitigate some of the risk involved with this credit card product, the Company performs credit checks and detailed analysis of the customer borrowing profile before approving the loan application. Management believes that the risks in the consumer loan portfolio are reasonable and the anticipated loss ratios are within acceptable parameters.

### Shared National Credits

The Company participates in credits of large, publicly traded companies which are defined by regulation as shared national credits, or SNCs. Regulations define SNCs as loans exceeding \$20 million that are shared by three or more financial institutions. The Company typically participates in these loans when business operations are maintained in the local communities or regional markets and opportunities to provide other banking services are present. The balance of SNC loans totaled \$445.0 million at June 30, 2013, with an additional \$1.1 billion in unfunded commitments.

### Income Taxes

Income tax expense was \$30.2 million in the second quarter of 2013, compared to \$28.9 million in the first quarter of 2013 and \$34.5 million in the second quarter of 2012. The Company's effective tax rate, including the effect of non-controlling interest, was 31.4% in the second quarter of 2013, compared with 32.2% in the first quarter of 2013 and 32.8% in the second quarter of 2012. Income tax expense for the first six months of 2013 was \$59.1 million compared to \$67.4 million for the same period during the previous year, resulting in effective tax rates of 31.8% and 33.0%, respectively. The decrease in the effective tax rate for the first six months of 2013 compared to the same period in 2012 was primarily due to higher tax-exempt interest on state and local municipal obligations.

### Financial Condition

## Balance Sheet

Total assets of the Company were \$21.9 billion at June 30, 2013 and \$22.2 billion at December 31, 2012. Earning assets (excluding fair value adjustments on investment securities) amounted to \$20.6 billion at June 30, 2013, compared to \$20.7 billion at December 31, 2012, and consisted of 50% in loans and 44% in investment securities.

At June 30, 2013, total loans, including loans held for sale, increased \$538.9 million, or 5.5%, compared with balances at December 31, 2012. Business, consumer, and personal real estate loans increased \$280.6 million, \$161.1 million, and \$115.2 million, respectively. Additionally, construction loans increased \$42.6 million. The increase in business loans resulted from growth in a number of lending activities, including tax-advantaged lending, aircraft lending, dealer floor plan and leasing. Demand for automobile and fixed rate home equity lending remained strong as outstanding balances grew by \$132.0 million and \$47.6 million,

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respectively. Marine and RV loans, included in the consumer loan portfolio, continued to run off during the period by \$40.3 million.

Available for sale investment securities (excluding fair value adjustments) decreased by \$408.3 million at June 30, 2013 compared to December 31, 2012. The decline in these securities resulted from a combination of loan growth and a decline in deposits, which bond maturities helped to fund. The largest decrease was in agency mortgage-backed securities, which decreased by \$358.6 million. Additionally, other asset-backed securities decreased \$58.2 million, and government-sponsored enterprise obligations decreased by \$40.5 million. These decreases were partially offset by growth in state and municipal obligations of \$39.7 million. At June 30, 2013, the duration of the investment portfolio was 2.7 years, and maturities and pay downs of approximately \$1.9 billion are expected to occur during the next 12 months.

Deposits at June 30, 2013 totaled \$17.9 billion and decreased \$451.7 million compared to December 31, 2012. Non-interest bearing deposits decreased \$488.4 million, or 7.8%, mainly in business demand deposits, and money market accounts decreased \$258.1 million, or 4.1%. These decreases were offset by an increase of \$316.8 million, or 27.4%, in time open and certificates of deposit over \$100,000.

The Company's short-term borrowings of federal funds purchased and customer repurchase agreements averaged \$973.7 million during the first six months of 2013. These borrowings totaled \$1.2 billion at June 30, 2013 compared to \$683.6 million at December 31, 2012. The growth was due to an increase in federal funds purchased of \$611.9 million, partly offset by a decline of \$74.7 million in repurchase agreements.

## Liquidity and Capital Resources

## Liquidity Management

The Company's most liquid assets are comprised of available for sale investment securities, federal funds sold, securities purchased under agreements to resell (resell agreements), and balances at the Federal Reserve Bank, as follows:

| (In thousands)                                            | June 30, 2013 | March 31,<br>2013 | December 31,<br>2012 |
|-----------------------------------------------------------|---------------|-------------------|----------------------|
| Liquid assets:                                            |               |                   |                      |
| Available for sale investment securities                  | \$8,927,815   | \$9,572,751       | \$9,522,248          |
| Federal funds sold                                        | 22,990        | 7,820             | 27,595               |
| Long-term securities purchased under agreements to resell | 1,200,000     | 1,200,000         | 1,200,000            |
| Balances at the Federal Reserve Bank                      | 6,816         | 199,956           | 179,164              |
| Total                                                     | \$10,157,621  | \$10,980,527      | \$10,929,007         |

Federal funds sold, which are sold to the Company's correspondent bank customers and have overnight maturities, totaled \$23.0 million as of June 30, 2013. Long-term resell agreements, maturing later in 2013 through 2016, totaled \$1.2 billion at June 30, 2013. Under these agreements with upstream financial institutions, the Company holds marketable securities, safekept by a third-party custodian, as collateral. This collateral totaled \$1.3 billion in fair value at June 30, 2013. Interest earning balances at the Federal Reserve Bank, which have overnight maturities and are used for general liquidity purposes, totaled \$6.8 million at June 30, 2013. The fair value of the available for sale investment portfolio was \$8.9 billion at June 30, 2013 and included an unrealized net gain in fair value of \$77.5 million. The total net unrealized gain included net gains of \$52.8 million on mortgage and asset-backed securities and \$12.8 million on U.S. government securities, and net losses of \$11.7 million on government-sponsored enterprise obligations. An additional \$32.7 million unrealized gain was included in the fair value of common stock held by the Parent.



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Approximately \$1.9 billion of the available for sale investment portfolio is expected to mature or pay down during the next 12 months, and these funds offer substantial resources to meet new loan demand or help offset reductions in the Company's deposit funding base. The Company pledges portions of its investment securities portfolio to secure public fund deposits, securities sold under agreements to repurchase, trust funds, letters of credit issued by the FHLB, and borrowing capacity at the Federal Reserve Bank. Total investment securities pledged for these purposes were as follows:

| (In thousands)                                             | June 30, 2013 | March 31, 2013 | December 31, 2012 |
|------------------------------------------------------------|---------------|----------------|-------------------|
| Investment securities pledged for the purpose of securing: |               |                |                   |
| Federal Reserve Bank borrowings                            | \$565,555     | \$580,800      | \$604,121         |
| FHLB borrowings and letters of credit                      | 28,635        | 34,085         | 46,732            |
| Securities sold under agreements to repurchase             | 2,019,283     | 2,209,955      | 2,105,867         |
| Other deposits and swaps                                   | 1,951,631     | 1,933,572      | 1,550,114         |
| Total pledged securities                                   | 4,565,104     | 4,758,412      | 4,306,834         |
| Unpledged and available for pledging                       | 2,798,764     | 3,165,302      | 3,428,781         |
| Ineligible for pledging                                    | 1,563,947     | 1,649,037      | 1,786,633         |
| Total available for sale securities, at fair value         | \$8,927,815   | \$9,572,751    | \$9,522,248       |

Liquidity is also available from the Company's large base of core customer deposits, defined as non-interest bearing, interest checking, savings, and money market deposit accounts. At June 30, 2013, such deposits totaled \$15.4 billion and represented 86.0% of total deposits. These core deposits are normally less volatile, as they are often with customer relationships tied to other products offered by the Company, promoting long lasting relationships and stable funding sources. Time open and certificates of deposit of \$100,000 and over totaled \$1.5 billion at June 30, 2013. These accounts are normally considered more volatile and higher costing and comprised 8.2% of total deposits at June 30, 2013.

| (In thousands)           | June 30, 2013 | March 31, 2013 | December 31, 2012 |
|--------------------------|---------------|----------------|-------------------|
| Core deposit base:       |               |                |                   |
| Non-interest bearing     | \$5,811,473   | \$6,170,274    | \$6,299,903       |
| Interest checking        | 854,141       | 805,960        | 976,144           |
| Savings and money market | 8,719,249     | 8,996,878      | 8,841,799         |
| Total                    | \$15,384,863  | \$15,973,112   | \$16,117,846      |

Other important components of liquidity are the level of borrowings from third party sources and the availability of future credit. The Company's outside borrowings are mainly comprised of federal funds purchased, securities sold under agreements to repurchase, and advances from the FHLB, as follows:

| (In thousands)                                 | June 30, 2013 | March 31, 2013 | December 31, 2012 |
|------------------------------------------------|---------------|----------------|-------------------|
| Borrowings:                                    |               |                |                   |
| Federal funds purchased                        | \$636,360     | \$36,750       | \$24,510          |
| Securities sold under agreements to repurchase | 984,334       | 1,090,108      | 1,059,040         |
| FHLB advances                                  | 102,766       | 102,783        | 103,710           |
| Total                                          | \$1,723,460   | \$1,229,641    | \$1,187,260       |

Federal funds purchased are unsecured overnight borrowings obtained mainly from upstream correspondent banks with which the Company maintains approved lines of credit. Securities sold under agreements to repurchase are secured by a portion of the Company's investment portfolio and are comprised of both non-insured customer funds

totaling \$584.3 million, which generally mature overnight, and structured repurchase agreements of \$400.0 million. The structured repurchase agreements have variable rates and mature later in 2013 and in 2014. The Company also borrows on a secured basis through advances from the FHLB, which totaled \$102.8 million at June 30, 2013. These advances have fixed interest rates and most mature in 2017.



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The Company pledges certain assets, including loans and investment securities, to both the Federal Reserve Bank and the FHLB as security to establish lines of credit and borrow from these entities. Based on the amount and type of collateral pledged, the FHLB establishes a collateral value from which the Company may draw advances against the collateral. Also, this collateral is used to enable the FHLB to issue letters of credit in favor of public fund depositors of the Company. The Federal Reserve Bank also establishes a collateral value of assets pledged to support borrowings from the discount window. The following table reflects the collateral value of assets pledged, borrowings, and letters of credit outstanding, in addition to the estimated future funding capacity available to the Company at June 30, 2013:

June 30, 2013

| (In thousands)                | FHLB        | Federal Reserve | Total       |
|-------------------------------|-------------|-----------------|-------------|
| Collateral value pledged      | \$2,140,518 | \$1,494,025     | \$3,634,543 |
| Advances outstanding          | (102,766)   | )—              | (102,766 )  |
| Letters of credit issued      | (182,010)   | )—              | (182,010 )  |
| Available for future advances | \$1,855,742 | \$1,494,025     | \$3,349,767 |

In addition to those mentioned above, several other sources of liquidity are available. The Bank has strong issuer ratings from Standard & Poor's and Moody's of A and Aa3, respectively. Additionally, the Parent's sound commercial paper rating of P-1 from Moody's would help ensure the ready marketability of its commercial paper, should the need arise. No commercial paper has been issued or outstanding during the past ten years. The Company has no subordinated debt or hybrid instruments which could affect future borrowing capacity. Because of its lack of significant long-term debt, the Company believes that it could generate additional liquidity through its Capital Markets Group from sources such as jumbo certificates of deposit or privately placed corporate debt. Financing may also include the issuance of common or preferred stock.

The cash flows from the operating, investing and financing activities of the Company resulted in a net decrease in cash and cash equivalents of \$350.3 million during the first six months of 2013, as reported in the consolidated statements of cash flows in this report. Operating activities, consisting mainly of net income adjusted for certain non-cash items, provided cash flow of \$167.9 million and has historically been a stable source of funds. Investing activities, which occur mainly in the loan and investment securities portfolios, used cash of \$393.0 million. These activities included \$1.3 billion in purchases of investment securities and a net increase in loans of \$555.9 million, offset by \$1.5 billion in sales, maturities and pay downs of investment securities. Financing activities used cash of \$125.3 million, resulting from a net decrease of \$582.1 million in deposit accounts, purchases of treasury stock of \$45.3 million, and cash dividends paid of \$40.9 million. These decreases in financing activities were partially offset by a net increase in short-term federal funds purchased and securities sold under agreements to repurchase of \$537.1 million. Future short-term liquidity needs arising from daily operations are not expected to vary significantly, and the Company believes it will be able to meet these cash flow needs.

## Capital Management

The Company and its bank subsidiary maintain strong regulatory capital ratios, which exceed the well-capitalized guidelines under federal banking regulations. Information about the Company's risk-based capital is shown below:

| (Dollars in thousands)          | June 30, 2013 | December 31, 2012 | Minimum Ratios for Well-Capitalized Banks |
|---------------------------------|---------------|-------------------|-------------------------------------------|
| Risk-adjusted assets            | \$14,415,319  | \$14,015,648      |                                           |
| Tier I risk-based capital       | 1,957,469     | 1,906,203         |                                           |
| Total risk-based capital        | 2,141,192     | 2,092,141         |                                           |
| Tier I risk-based capital ratio | 13.58         | % 13.60           | % 6.00 %                                  |

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|                                |       |         |         |   |
|--------------------------------|-------|---------|---------|---|
| Total risk-based capital ratio | 14.85 | % 14.93 | % 10.00 | % |
| Tier I leverage ratio          | 9.08  | % 9.14  | % 5.00  | % |

The Company maintains a treasury stock buyback program, and during the quarter ended June 30, 2013, the Company purchased 383,428 shares of stock at an average cost of \$39.90 per share. At June 30, 2013, 936,297 shares remained available for purchase under the current Board authorization. At a July 2013 meeting, the Board of Directors approved the purchase of additional shares, bringing the total shares authorized for future purchase to 4,000,000 shares.

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The Company's common stock dividend policy reflects its earnings outlook, desired payout ratios, the need to maintain adequate capital levels, and alternative investment options. The Company paid a \$.225 per share cash dividend in each of the first two quarters in 2013, which was a 2.7% increase compared to its regular dividend in the fourth quarter of 2012.

## Commitments, Off-Balance Sheet Arrangements and Contingencies

In the normal course of business, various commitments and contingent liabilities arise which are not required to be recorded on the balance sheet. The most significant of these are loan commitments, which at June 30, 2013 totaled \$8.3 billion (including approximately \$3.9 billion in unused approved credit card lines). In addition, the Company enters into standby and commercial letters of credit. These contracts amounted to \$330.0 million and \$8.8 million, respectively, at June 30, 2013. As many commitments expire unused or only partially used, these totals do not necessarily reflect future cash requirements. The carrying value of the guarantee obligations associated with the standby letters of credit, which has been recorded as a liability on the balance sheet, amounted to \$3.9 million at June 30, 2013.

The Company regularly purchases various state tax credits arising from third-party property redevelopment. These credits are either resold to third parties or retained for use by the Company. During the first six months of 2013, purchases and sales of tax credits amounted to \$42.0 million and \$16.7 million, respectively, and at June 30, 2013, outstanding purchase commitments totaled \$169.0 million.

Other significant contingencies related to lawsuits are discussed in Note 16 to the consolidated financial statements.

## Segment Results

The table below is a summary of segment pre-tax income results for the first six months of 2013 and 2012.

| (Dollars in thousands)                                | Consumer   | Commercial | Wealth    | Segment<br>Totals | Other/<br>Elimination | Consolidated<br>Totals |
|-------------------------------------------------------|------------|------------|-----------|-------------------|-----------------------|------------------------|
| Six Months Ended June 30,<br>2013                     |            |            |           |                   |                       |                        |
| Net interest income                                   | \$134,096  | \$140,057  | \$20,111  | \$294,264         | \$15,537              | \$309,801              |
| Provision for loan losses                             | (16,881 )  | (128 )     | (140 )    | (17,149 )         | 6,485                 | (10,664 )              |
| Non-interest income                                   | 55,130     | 89,611     | 58,333    | 203,074           | (521 )                | 202,553                |
| Investment securities losses, net                     | —          | —          | —         | —                 | (3,733 )              | (3,733 )               |
| Non-interest expense                                  | (136,876 ) | (117,983 ) | (47,957 ) | (302,816 )        | (9,187 )              | (312,003 )             |
| Income before income taxes                            | \$35,469   | \$111,557  | \$30,347  | \$177,373         | \$8,581               | \$185,954              |
| Six Months Ended June 30,<br>2012                     |            |            |           |                   |                       |                        |
| Net interest income                                   | \$137,654  | \$144,275  | \$19,465  | \$301,394         | \$23,448              | \$324,842              |
| Provision for loan losses                             | (18,460 )  | (288 )     | (552 )    | (19,300 )         | 5,920                 | (13,380 )              |
| Non-interest income                                   | 55,447     | 87,838     | 53,376    | 196,661           | (1,262 )              | 195,399                |
| Investment securities gains, net                      | —          | —          | —         | —                 | 5,376                 | 5,376                  |
| Non-interest expense                                  | (133,263 ) | (112,051 ) | (45,011 ) | (290,325 )        | (16,476 )             | (306,801 )             |
| Income before income taxes                            | \$41,378   | \$119,774  | \$27,278  | \$188,430         | \$17,006              | \$205,436              |
| Increase (decrease) in income<br>before income taxes: |            |            |           |                   |                       |                        |
| Amount                                                | \$(5,909 ) | \$(8,217 ) | \$3,069   | \$(11,057 )       | \$(8,425 )            | \$(19,482 )            |
| Percent                                               | (14.3 )%   | (6.9 )%    | 11.3 %    | (5.9 )%           | (49.5 )%              | (9.5 )%                |

Consumer

For the six months ended June 30, 2013, income before income taxes for the Consumer segment decreased \$5.9 million, or 14.3%, compared to the first six months of 2012. This decrease was mainly due to a decline of \$3.6 million, or 2.6%, in net interest income coupled with a decline of \$317 thousand, or .6%, in non-interest income and an increase in non-interest expense of \$3.6 million, or 2.7%. These income reductions were partly offset by a decrease of \$1.6 million in the provision for loan losses. Net interest income declined due to a \$2.2 million decrease in loan interest income and a \$3.9 million decrease in net allocated funding credits assigned to the Consumer segment's loan and deposit portfolios, partly offset by a decline of \$2.6 million in deposit interest expense. Non-interest income decreased mainly due to a decline in deposit account fees (mainly overdraft charges), partly offset by higher mortgage banking revenue. Non-interest expense increased over the same period in the previous year due to higher bank card related expense, corporate management fees, occupancy expense and processing costs. The provision for loan losses totaled \$16.9 million, a \$1.6 million decrease from the first six months of 2012, which was due mainly to lower losses on marine and RV loans.

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### Commercial

For the six months ended June 30, 2013, income before income taxes for the Commercial segment decreased \$8.2 million, or 6.9%, compared to the same period in the previous year. This decrease was mainly due to lower net interest income and higher non-interest expense, partly offset by higher non-interest income. Net interest income decreased \$4.2 million, due to a \$7.5 million decline in loan interest income, partly offset by higher net allocated funding credits of \$3.0 million. The provision for loan losses declined \$160 thousand from the same period last year, as business real estate loan charge-offs declined \$2.2 million and construction and land loan charge-offs declined \$1.6 million, while business loan charge-offs increased \$3.1 million. Non-interest income increased by \$1.8 million, or 2.0%, over the previous year due to growth in bank card fees (mainly corporate card and merchant), partly offset by lower capital market fees. Non-interest expense increased \$5.9 million, or 5.3%, over the previous year, mainly due to higher bank card related expense, a provision recorded on a letter of credit exposure and higher salaries and benefits expense. These increases were partly offset by higher gains on sales of foreclosed property and lower corporate management fees.

### Wealth

Wealth segment pre-tax profitability for the six months ended June 30, 2013 increased \$3.1 million, or 11.3%, over the same period in the previous year. Net interest income increased \$646 thousand, or 3.3%, and was impacted by a \$568 thousand decline in deposit interest expense. Non-interest income increased \$5.0 million, or 9.3%, over the prior year due to higher personal and institutional trust fees and brokerage advisory fees. Non-interest expense increased \$2.9 million, or 6.5%, mainly due to higher salary costs, incentive compensation and processing costs. The provision for loan losses declined \$412 thousand, mainly due to lower losses on personal real estate and revolving home equity loans.

The Other/Elimination category in the preceding table includes the activity of various support and overhead operating units of the Company, in addition to the investment securities portfolio and other items not allocated to the segments. In accordance with the Company's transfer pricing policies, the difference between the total provision and total net charge-offs/recoveries is not allocated to a business segment, and is included in this category. The pre-tax profitability of this category was lower than in the same period last year by \$8.4 million. This decrease was mainly due to a \$7.9 million decline in net interest income in this category, related to earnings of the investment portfolio and interest expense on borrowings not allocated to a segment and lower unallocated securities gains of \$9.1 million, partly offset by lower unallocated non-interest expense of \$7.3 million.

### Regulatory Changes Affecting the Banking Industry

In July 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) was signed into law. The Dodd-Frank Act was sweeping legislation intended to overhaul regulation of the financial services industry. Among its many provisions were rules which established a new council of "systemic risk" regulators, created a new consumer protection division within the Federal Reserve, empowered the Federal Reserve to supervise the largest, most complex financial companies, allowed the government to seize and liquidate failing financial companies, and gave regulators new powers to oversee the derivatives market.

Because the Company has maintained a strong balance sheet with solid amounts of capital and has not offered many of the complex financial products that were prevalent in the marketplace, there are a number of provisions within the Dodd-Frank Act, including higher capital standards and improved lending transparency, that management does not expect to negatively affect the Company's future results. New risk-based FDIC rules for insurance assessments have lowered costs for the Company. However, other provisions in the Dodd-Frank Act, such as limitations on debit card interchange fees, have lowered revenues. Higher regulatory and compliance burdens are likely, as evidenced by new

regulations over the derivatives market. In June 2013, new regulations became effective which required the Company to centrally clear specified derivative transactions on an exchange, and to register swap transactions with a central data repository for reporting and recordkeeping. The Company has implemented new processes to achieve this and continues to offer derivative products to customers, who have been largely unaffected by the new regulations.

In October 2012, the Federal Reserve, as required by the Dodd-Frank Act, approved new stress testing regulations applicable to certain financial companies with total consolidated assets of between \$10 billion and \$50 billion. The rule requires that these financial companies conduct stress tests on an annual basis. The stress tests will have an as-of date of September 30, 2013 using three scenarios provided by the Federal Reserve in November 2013 (projected out nine quarters). The Company is required to submit regulatory reports to the Federal Reserve on its stress test results by March 31, 2014. By June 30, 2015, the Company will be required to make public disclosures of the results of the 2015 stress test.

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In July 2013 the Federal Reserve approved a final rule to implement in the United States the Basel III regulatory capital reforms from the Basel Committee on Banking Supervision and certain changes required by the Dodd-Frank Act. The final rule increases minimum requirements for both the quantity and quality of capital held by banking organizations. The rule includes a new minimum ratio of common equity tier 1 capital to risk-weighted assets of 4.5% and a common equity tier 1 capital conservation buffer of 2.5% of risk-weighted assets. The final rule also adjusted the methodology for calculating risk-weighted assets to enhance risk sensitivity. Beginning January 1, 2015, the Company must be compliant with revised minimum regulatory capital ratios and will begin the transitional period for definitions of regulatory capital and regulatory capital adjustments and deductions established under the final rule. Compliance with the risk-weighted asset calculations will be required on January 1, 2015. The Company believes its current capital ratios are higher than those required in the final rule.

On July 31, 2013, a Federal District Court judge ruled that the Federal Reserve inflated debit interchange fees when implementing the Durbin amendment of the Dodd-Frank Act in 2011. The judge ruled that the Federal Reserve erred in using criteria outside of the scope Congress intended to determine the fee cap, which the Federal Reserve set at 21 cents per transaction. The judge also ruled that the network options for both signature and PIN transactions were not set appropriately in accordance with the Dodd-Frank Act. The judge has stayed this decision to give the Federal Reserve time to adopt interim standards and has scheduled a conference with the parties on August 14, 2013. If not overturned on appeal, this ruling could significantly affect debit fees for the banking industry and for the Company. However, these developments are preliminary and the impact on the Company is not determinable at this time.

The many provisions of the Dodd-Frank Act are so extensive that implementation by regulators is still ongoing. Several of the key regulations included in the original law have been delayed since the law's passing, making an assessment of the Dodd Frank Act's full effect on the Company not possible at this time.

### Impact of Recently Issued Accounting Standards

**Other Comprehensive Income** In February 2013, the Financial Accounting Standards Board (FASB) issued ASU 2013-02, "Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income". The amendments require an entity to present, either in the income statement or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income, but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety, an entity is required to cross-reference to other disclosures that provide additional detail about those amounts. This ASU was effective for annual and interim periods beginning January 1, 2013. Adoption of the ASU did not have a significant effect on the Company's consolidated financial statements (see Note 9).

**Balance Sheet** In December 2011, the FASB issued ASU 2011-11, "Disclosures about Offsetting Assets and Liabilities". The ASU is a joint requirement by the FASB and International Accounting Standards Board to enhance current disclosures and increase comparability of GAAP and International Financial Reporting Standards (IFRS) financial statements. Under the ASU, an entity is required to disclose both gross and net information about instruments and transactions eligible for offset in the balance sheet, as well as instruments and transactions subject to an agreement similar to a master netting agreement. ASU 2013-01, "Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities" was issued in January 2013, and amended ASU 2011-11 to specifically include only derivatives accounted for under Topic 815, repurchase and reverse repurchase agreements, and securities borrowing and lending transactions that are either offset or subject to an enforceable master netting arrangement. Both ASUs were effective for annual and interim periods beginning January 1, 2013. Their adoption did not have a significant effect on the Company's consolidated financial statements (see Note 12).

Investment Companies In June 2013, the FASB issued ASU 2013-08, "Amendments to the Scope, Measurement, and Disclosure Requirements" for investment companies. The amendments changed the assessment of whether an entity is an investment company by requiring an entity to possess certain fundamental characteristics, while allowing judgment in assessing other typical characteristics. The ASU is effective January 1, 2014, and the Company does not anticipate a change in the status of any subsidiary, or a change in the accounting applied to a subsidiary, under the new guidelines.

Derivatives The FASB issued ASU 2013-10, "Inclusion of the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) as a Benchmark Interest Rate for Hedge Accounting Purposes", in July 2013. These amendments allow the Fed Funds Effective Swap Rate (OIS) to be used as a U.S. benchmark interest rate for hedge accounting purposes, in addition to the current benchmark rates of UST (the rate on direct Treasury obligations of the U.S. government) and LIBOR (the London Interbank Offered Rate on swaps). The amendments were effective on a prospective basis for new or redesignated hedging relationships on July 17, 2013. The adoption is not expected to have a significant effect on the Company's consolidated financial statements.



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## AVERAGE BALANCE SHEETS — AVERAGE RATES AND YIELDS

Three Months Ended June 30, 2013 and 2012

| (Dollars in thousands)                         | Second Quarter 2013 |                         |                        | Second Quarter 2012 |                         |                        |
|------------------------------------------------|---------------------|-------------------------|------------------------|---------------------|-------------------------|------------------------|
|                                                | Average Balance     | Interest Income/Expense | Avg. Rates Earned/Paid | Average Balance     | Interest Income/Expense | Avg. Rates Earned/Paid |
| <b>ASSETS:</b>                                 |                     |                         |                        |                     |                         |                        |
| Loans:                                         |                     |                         |                        |                     |                         |                        |
| Business <sup>(A)</sup>                        | \$3,253,577         | \$ 24,873               | 3.07 %                 | \$2,895,167         | \$ 25,796               | 3.58 %                 |
| Real estate — construction and land            | 373,359             | 3,667                   | 3.94                   | 360,000             | 3,796                   | 4.24                   |
| Real estate — business                         | 2,216,876           | 22,870                  | 4.14                   | 2,205,561           | 25,844                  | 4.71                   |
| Real estate — personal                         | 1,664,988           | 16,482                  | 3.97                   | 1,475,930           | 16,358                  | 4.46                   |
| Consumer                                       | 1,430,832           | 16,732                  | 4.69                   | 1,134,838           | 16,170                  | 5.73                   |
| Revolving home equity                          | 425,762             | 4,208                   | 3.96                   | 449,416             | 4,660                   | 4.17                   |
| Consumer credit card                           | 741,793             | 20,709                  | 11.20                  | 712,708             | 21,038                  | 11.87                  |
| Overdrafts                                     | 6,369               | —                       | —                      | 5,663               | —                       | —                      |
| Total loans                                    | 10,113,556          | 109,541                 | 4.34                   | 9,239,283           | 113,662                 | 4.95                   |
| Loans held for sale                            | 9,003               | 91                      | 4.05                   | 9,053               | 88                      | 3.91                   |
| Investment securities:                         |                     |                         |                        |                     |                         |                        |
| U.S. government and federal agency             | 400,027             | 5,139                   | 5.15                   | 330,648             | 6,232                   | 7.58                   |
| Government-sponsored enterprise obligations    | 439,075             | 1,906                   | 1.74                   | 265,620             | 1,362                   | 2.06                   |
| State and municipal obligations <sup>(A)</sup> | 1,634,196           | 14,716                  | 3.61                   | 1,322,987           | 13,243                  | 4.03                   |
| Mortgage-backed securities                     | 3,272,580           | 22,607                  | 2.77                   | 4,010,276           | 28,835                  | 2.89                   |
| Asset-backed securities                        | 3,199,393           | 7,281                   | .91                    | 2,900,122           | 8,122                   | 1.13                   |
| Other marketable securities <sup>(A)</sup>     | 188,267             | 1,396                   | 2.97                   | 135,930             | 1,664                   | 4.92                   |
| Trading securities <sup>(A)</sup>              | 22,355              | 134                     | 2.40                   | 22,748              | 150                     | 2.65                   |
| Non-marketable securities <sup>(A)</sup>       | 118,888             | 5,015                   | 16.92                  | 122,651             | 2,624                   | 8.60                   |
| Total investment securities                    | 9,274,781           | 58,194                  | 2.52                   | 9,110,982           | 62,232                  | 2.75                   |
| Short-term federal funds sold and securities   |                     |                         |                        |                     |                         |                        |
| purchased under agreements to resell           | 23,429              | 28                      | .48                    | 22,139              | 29                      | .53                    |
| Long-term securities purchased                 |                     |                         |                        |                     |                         |                        |
| under agreements to resell                     | 1,200,000           | 5,810                   | 1.94                   | 850,000             | 4,582                   | 2.17                   |
| Interest earning deposits with banks           | 116,510             | 75                      | .26                    | 163,075             | 112                     | .28                    |
| Total interest earning assets                  | 20,737,279          | 173,739                 | 3.36                   | 19,394,532          | 180,705                 | 3.75                   |
| Allowance for loan losses                      | (167,216 )          |                         |                        | (180,917 )          |                         |                        |
| Unrealized gain on investment securities       | 229,102             |                         |                        | 242,765             |                         |                        |
| Cash and due from banks                        | 365,921             |                         |                        | 357,768             |                         |                        |
| Land, buildings and equipment, net             | 358,867             |                         |                        | 356,378             |                         |                        |
| Other assets                                   | 397,392             |                         |                        | 378,726             |                         |                        |
| Total assets                                   | \$21,921,345        |                         |                        | \$20,549,252        |                         |                        |
| <b>LIABILITIES AND EQUITY:</b>                 |                     |                         |                        |                     |                         |                        |
| Interest bearing deposits:                     |                     |                         |                        |                     |                         |                        |
| Savings                                        | \$639,747           | 168                     | .11                    | \$584,196           | 175                     | .12                    |
| Interest checking and money market             | 8,932,987           | 3,207                   | .14                    | 8,369,306           | 4,459                   | .21                    |
| Time open & C.D.'s of less than \$100,000      | 1,052,574           | 1,656                   | .63                    | 1,128,716           | 2,004                   | .71                    |

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|                                                                             |              |            |      |              |            |      |   |
|-----------------------------------------------------------------------------|--------------|------------|------|--------------|------------|------|---|
| Time open & C.D.'s of \$100,000 and over                                    | 1,464,384    | 1,667      | .46  | 1,250,164    | 1,828      | .59  |   |
| Total interest bearing deposits                                             | 12,089,692   | 6,698      | .22  | 11,332,382   | 8,466      | .30  |   |
| Borrowings:                                                                 |              |            |      |              |            |      |   |
| Federal funds purchased and securities sold                                 |              |            |      |              |            |      |   |
| under agreements to repurchase                                              | 1,544,623    | 270        | .07  | 1,109,693    | 177        | .06  |   |
| Other borrowings                                                            | 103,019      | 829        | 3.23 | 111,336      | 876        | 3.16 |   |
| Total borrowings                                                            | 1,647,642    | 1,099      | .27  | 1,221,029    | 1,053      | .35  |   |
| Total interest bearing liabilities                                          | 13,737,334   | 7,797      | .23  | % 12,553,411 | 9,519      | .30  | % |
| Non-interest bearing deposits                                               | 5,768,455    |            |      | 5,404,687    |            |      |   |
| Other liabilities                                                           | 228,966      |            |      | 367,763      |            |      |   |
| Equity                                                                      | 2,186,590    |            |      | 2,223,391    |            |      |   |
| Total liabilities and equity                                                | \$21,921,345 |            |      | \$20,549,252 |            |      |   |
| Net interest margin (T/E)                                                   |              | \$ 165,942 |      |              | \$ 171,186 |      |   |
| Net yield on interest earning assets                                        |              |            | 3.21 | %            |            | 3.55 | % |
| A) Stated on a tax equivalent basis using a federal income tax rate of 35%. |              |            |      |              |            |      |   |

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## AVERAGE BALANCE SHEETS — AVERAGE RATES AND YIELDS

Six Months Ended June 30, 2013 and 2012

| (Dollars in thousands)                         | Six Months 2013 |                         |                        | Six Months 2012 |                         |                        |
|------------------------------------------------|-----------------|-------------------------|------------------------|-----------------|-------------------------|------------------------|
|                                                | Average Balance | Interest Income/Expense | Avg. Rates Earned/Paid | Average Balance | Interest Income/Expense | Avg. Rates Earned/Paid |
| <b>ASSETS:</b>                                 |                 |                         |                        |                 |                         |                        |
| Loans:                                         |                 |                         |                        |                 |                         |                        |
| Business <sup>(A)</sup>                        | \$3,205,354     | \$ 49,570               | 3.12 %                 | \$2,894,570     | \$ 51,122               | 3.55 %                 |
| Real estate — construction and land            | 362,526         | 7,025                   | 3.91                   | 370,242         | 7,898                   | 4.29                   |
| Real estate — business                         | 2,223,627       | 45,823                  | 4.16                   | 2,195,227       | 50,688                  | 4.64                   |
| Real estate — personal                         | 1,632,742       | 32,586                  | 4.02                   | 1,458,725       | 32,771                  | 4.52                   |
| Consumer                                       | 1,387,263       | 33,384                  | 4.85                   | 1,121,358       | 32,518                  | 5.83                   |
| Revolving home equity                          | 427,221         | 8,519                   | 4.02                   | 452,099         | 9,392                   | 4.18                   |
| Consumer credit card                           | 748,443         | 41,890                  | 11.29                  | 721,869         | 42,450                  | 11.83                  |
| Overdrafts                                     | 5,890           | —                       | —                      | 6,625           | —                       | —                      |
| Total loans                                    | 9,993,066       | 218,797                 | 4.42                   | 9,220,715       | 226,839                 | 4.95                   |
| Loans held for sale                            | 9,049           | 176                     | 3.92                   | 10,600          | 193                     | 3.66                   |
| Investment securities:                         |                 |                         |                        |                 |                         |                        |
| U.S. government and federal agency             | 399,126         | 4,556                   | 2.30                   | 329,377         | 7,932                   | 4.84                   |
| Government-sponsored enterprise obligations    | 453,760         | 4,052                   | 1.80                   | 274,557         | 2,778                   | 2.03                   |
| State and municipal obligations <sup>(A)</sup> | 1,618,716       | 29,679                  | 3.70                   | 1,293,145       | 26,339                  | 4.10                   |
| Mortgage-backed securities                     | 3,392,807       | 45,087                  | 2.68                   | 4,100,629       | 58,510                  | 2.87                   |
| Asset-backed securities                        | 3,203,129       | 14,643                  | .92                    | 2,831,009       | 16,118                  | 1.14                   |
| Other marketable securities <sup>(A)</sup>     | 190,826         | 2,926                   | 3.09                   | 149,273         | 3,324                   | 4.48                   |
| Trading securities <sup>(A)</sup>              | 25,027          | 264                     | 2.13                   | 27,688          | 389                     | 2.83                   |
| Non-marketable securities <sup>(A)</sup>       | 119,146         | 6,841                   | 11.58                  | 119,762         | 5,108                   | 8.58                   |
| Total investment securities                    | 9,402,537       | 108,048                 | 2.32                   | 9,125,440       | 120,498                 | 2.66                   |
| Short-term federal funds sold and securities   |                 |                         |                        |                 |                         |                        |
| purchased under agreements to resell           | 16,095          | 37                      | .46                    | 17,917          | 46                      | .52                    |
| Long-term securities purchased                 |                 |                         |                        |                 |                         |                        |
| under agreements to resell                     | 1,189,227       | 11,639                  | 1.97                   | 850,000         | 8,857                   | 2.10                   |
| Interest earning deposits with banks           | 123,395         | 152                     | .25                    | 125,497         | 167                     | .27                    |
| Total interest earning assets                  | 20,733,369      | 338,849                 | 3.30                   | 19,350,169      | 356,600                 | 3.71                   |
| Allowance for loan losses                      | (169,558 )      |                         |                        | (182,234 )      |                         |                        |
| Unrealized gain on investment securities       | 242,347         |                         |                        | 236,293         |                         |                        |
| Cash and due from banks                        | 371,142         |                         |                        | 362,332         |                         |                        |
| Land, buildings and equipment, net             | 360,103         |                         |                        | 358,595         |                         |                        |
| Other assets                                   | 386,005         |                         |                        | 382,827         |                         |                        |
| Total assets                                   | \$21,923,408    |                         |                        | \$20,507,982    |                         |                        |
| <b>LIABILITIES AND EQUITY:</b>                 |                 |                         |                        |                 |                         |                        |
| Interest bearing deposits:                     |                 |                         |                        |                 |                         |                        |
| Savings                                        | \$621,795       | 351                     | .11                    | \$567,097       | 384                     | .14                    |
| Interest checking and money market             | 9,036,966       | 6,948                   | .16                    | 8,340,520       | 9,331                   | .22                    |
| Time open & C.D.'s of less than \$100,000      | 1,060,590       | 3,405                   | .65                    | 1,142,299       | 4,110                   | .72                    |

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|                                                                              |              |            |      |              |            |      |   |
|------------------------------------------------------------------------------|--------------|------------|------|--------------|------------|------|---|
| Time open & C.D.'s of \$100,000 and over                                     | 1,401,020    | 3,366      | .48  | 1,347,208    | 3,739      | .56  |   |
| Total interest bearing deposits                                              | 12,120,371   | 14,070     | .23  | 11,397,124   | 17,564     | .31  |   |
| Borrowings:                                                                  |              |            |      |              |            |      |   |
| Federal funds purchased and securities sold                                  |              |            |      |              |            |      |   |
| under agreements to repurchase                                               | 1,373,670    | 488        | .07  | 1,198,469    | 402        | .07  |   |
| Other borrowings                                                             | 103,173      | 1,641      | 3.21 | 111,568      | 1,782      | 3.21 |   |
| Total borrowings                                                             | 1,476,843    | 2,129      | .29  | 1,310,037    | 2,184      | .34  |   |
| Total interest bearing liabilities                                           | 13,597,214   | 16,199     | .24  | % 12,707,161 | 19,748     | .31  | % |
| Non-interest bearing deposits                                                | 5,848,398    |            |      | 5,268,496    |            |      |   |
| Other liabilities                                                            | 297,384      |            |      | 321,556      |            |      |   |
| Equity                                                                       | 2,180,412    |            |      | 2,210,769    |            |      |   |
| Total liabilities and equity                                                 | \$21,923,408 |            |      | \$20,507,982 |            |      |   |
| Net interest margin (T/E)                                                    |              | \$ 322,650 |      |              | \$ 336,852 |      |   |
| Net yield on interest earning assets                                         |              |            | 3.14 | %            |            | 3.50 | % |
| (A) Stated on a tax equivalent basis using a federal income tax rate of 35%. |              |            |      |              |            |      |   |

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## Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest rate risk management focuses on maintaining consistent growth in net interest income within Board-approved policy limits. The Company primarily uses earnings simulation models to analyze net interest sensitivity to movement in interest rates. The Company performs monthly simulations which model interest rate movements and risk in accordance with changes to its balance sheet composition. For further discussion of the Company's market risk, see the Interest Rate Sensitivity section of Management's Discussion and Analysis of Financial Condition and Results of Operations included in the Company's 2012 Annual Report on Form 10-K.

The table below shows the effect that gradual rising interest rates over a twelve month period would have on the Company's net interest income given a static balance sheet.

| (Dollars in millions)   | June 30, 2013                                |                                       | March 31, 2013                               |                                       | December 31, 2012                            |                                       |        |       |    |
|-------------------------|----------------------------------------------|---------------------------------------|----------------------------------------------|---------------------------------------|----------------------------------------------|---------------------------------------|--------|-------|----|
|                         | \$ Change<br>in<br>Net<br>Interest<br>Income | % Change in<br>Net Interest<br>Income | \$ Change<br>in<br>Net<br>Interest<br>Income | % Change in<br>Net Interest<br>Income | \$ Change<br>in<br>Net<br>Interest<br>Income | % Change in<br>Net Interest<br>Income |        |       |    |
| 300 basis points rising | (\$11.8                                      | )(1.98                                | )%                                           | (\$6.1                                | )(1.03                                       | )%                                    | (\$2.1 | )(.36 | )% |
| 200 basis points rising | (4.5                                         | )(.75                                 | )                                            | .3                                    | (.05                                         | )                                     | 3.1    | .51   |    |
| 100 basis points rising | (.1                                          | )(.02                                 | )                                            | 3.2                                   | (.54                                         | )                                     | 4.9    | .82   |    |

Under the above scenarios at June 30, 2013, a gradual increase in interest rates of 100 basis points is expected to decrease net interest income from the base calculation by \$130 thousand, or .02%, and a rise of 200 basis points is expected to decrease net interest income by \$4.5 million, or .8%. Under a 300 basis points rising rate scenario, net interest income would decrease by \$11.8 million, or 2.0%. Due to the already low interest rate environment, the Company did not model falling rate scenarios.

As shown above, the rising rate scenarios over the past several quarters has a negative effect on projected net interest income. This is because the scenarios project deposit interest expense to grow, mainly in money market accounts, more quickly than longer-term earning assets re-price. Also, these scenarios project deposit run-off which is replaced by higher costing short-term borrowings. Rising rates also tend to slow prepayments of both residential mortgage loans and mortgage-backed securities, which also negatively affects net interest income. The scenarios also assume growth in loans, especially those with variable rates, which is funded by maturing investment securities, and this assumption helps offset the negative effects mentioned above.

The change in net interest income from the base calculation at June 30, 2013 for the three scenarios shown was lower than projections made at March 31, 2013, largely due to recent higher interest rates causing slowing mortgage prepayments and extended durations of the investment securities portfolio. In addition, non-maturity deposits declined since March and the funding was replaced by higher costing short-term borrowings.

The Company believes that its approach to interest rate risk has appropriately considered its susceptibility to both rising and falling rates and has adopted strategies which minimized impacts to overall interest rate risk.

## Item 4. CONTROLS AND PROCEDURES

An evaluation was performed under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of June 30, 2013. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective.

There were no changes in the Company's internal control over financial reporting that occurred during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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## PART II: OTHER INFORMATION

## Item 1. LEGAL PROCEEDINGS

The information required by this item is set forth in Part I, Item 1 under Note 16, Legal Proceedings.

## Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table sets forth information about the Company's purchases of its \$5 par value common stock, its only class of stock registered pursuant to Section 12 of the Securities Exchange Act of 1934, as amended.

| Period             | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as part of Publicly Announced Program | Maximum Number that May Yet Be Purchased Under the Program |
|--------------------|----------------------------------|------------------------------|------------------------------------------------------------------------|------------------------------------------------------------|
| April 1 — 30, 2013 | 241,198                          | \$39.36                      | 241,198                                                                | 1,078,527                                                  |
| May 1 — 31, 2013   | 122,717                          | \$40.43                      | 122,717                                                                | 955,810                                                    |
| June 1 — 30, 2013  | 19,513                           | \$43.32                      | 19,513                                                                 | 936,297                                                    |
| Total              | 383,428                          | \$39.90                      | 383,428                                                                | 936,297                                                    |

In July 2012, the Board of Directors approved the purchase of up to 3,000,000 shares of the Company's common stock. At June 30, 2013, 936,297 shares remained available to be purchased under that authorization. At a July 2013 meeting of the Board of Directors, the purchase of additional shares was approved, bringing the total shares authorized for future purchase to 4,000,000 shares.

## Item 6. EXHIBITS

See Index to Exhibits

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SIGNATURES

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

COMMERCE BANCSHARES, INC.

By /s/ THOMAS J. NOACK  
Thomas J. Noack  
Vice President & Secretary

Date: August 6, 2013

By /s/ JEFFERY D. ABERDEEN  
Jeffery D. Aberdeen  
Controller  
(Chief Accounting Officer)

Date: August 6, 2013



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INDEX TO EXHIBITS

31.1 — Certification of CEO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 — Certification of CFO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32 — Certifications of CEO and CFO pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

101 — Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Changes in Equity, (v) the Consolidated Statements of Cash Flows and (vi) the Notes to Consolidated Financial Statements, tagged as blocks of text and in detail