ZIONS BANCORPORATION /UT/
Form 10-Q
November 07, 2008
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# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

# FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
**For the quarterly period ended September 30, 2008**

**OR**

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
**For the transition period from _________ to _________**

**COMMISSION FILE NUMBER 001-12307**

# ZIONS BANCORPORATION

**(Exact name of registrant as specified in its charter)**

| | |
|---|---|
| **UTAH** | **87-0227400** |
| **(State or other jurisdiction of incorporation or organization)** | **(I.R.S. Employer Identification No.)** |
| **ONE SOUTH MAIN, 15TH FLOOR SALT LAKE CITY, UTAH** | **84133** |
| **(Address of principal executive offices)** | **(Zip Code)** |

**Registrant s telephone number, including area code: (801) 524-4787**

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

Yes x No ¨

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

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company ¨

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

Yes ¨ No x

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

| | |
|---|---|
| Common Stock, without par value, outstanding at October 31, 2008 | 115,343,553 shares |

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**ZIONS BANCORPORATION AND SUBSIDIARIES**

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS (Unaudited)

ZIONS BANCORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

| **(In thousands, except share amounts)** | **September 30, 2008 (Unaudited)** | **December 31, 2007** | **September 30, 2007 (Unaudited)** |
|---|---|---|---|
| ASSETS | | | |
| Cash and due from banks | $ 1,441,957 | $ 1,855,155 | $ 1,481,238 |
| Money market investments: | | | |
| Interest-bearing deposits and commercial paper | 568,875 | 726,446 | 513,395 |
| Federal funds sold | 274,129 | 102,225 | 23,567 |
| Security resell agreements | 170,009 | 671,537 | 484,678 |
| Investment securities: | | | |
| Held-to-maturity, at adjusted cost (approximate fair value $1,587,006, $702,148 and $686,026) | 1,917,354 | 704,441 | 695,842 |
| Available-for-sale, at fair value | 2,792,236 | 5,134,610 | 4,549,721 |
| Trading account, at fair value (includes $531, $741 and $22 transferred as collateral under repurchase agreements) | 45,769 | 21,849 | 15,494 |
| | 4,755,359 | 5,860,900 | 5,261,057 |
| Loans: | | | |
| Loans held for sale | 152,095 | 207,943 | 200,653 |
| Loans and leases | 41,876,371 | 39,044,163 | 37,778,228 |
| | 42,028,466 | 39,252,106 | 37,978,881 |
| Less: | | | |
| Unearned income and fees, net of related costs | 140,773 | 164,327 | 156,622 |
| Allowance for loan losses | 609,433 | 459,376 | 418,165 |
| Loans and leases, net of allowance | 41,278,260 | 38,628,403 | 37,404,094 |
| Other noninterest-bearing investments | 1,170,367 | 1,034,412 | 1,043,475 |
| Premises and equipment, net | 675,480 | 655,712 | 658,294 |
| Goodwill | 2,009,504 | 2,009,513 | 2,021,519 |
| Core deposit and other intangibles | 133,989 | 149,493 | 172,140 |
| Other real estate owned | 156,817 | 15,201 | 11,973 |
| Other assets | 1,339,422 | 1,238,417 | 969,256 |
| | $ 53,974,168 | $ 52,947,414 | $ 50,044,686 |
| LIABILITIES AND SHAREHOLDERS EQUITY | | | |
| Deposits: | | | |
| Noninterest-bearing demand | $ 9,413,484 | $ 9,618,300 | $ 9,322,668 |
| Interest-bearing: | | | |
| Savings and NOW | 4,341,873 | 4,507,837 | 4,365,600 |
| Money market | 11,703,163 | 10,304,225 | 10,446,015 |
| Internet money market | 2,384,125 | 2,163,014 | 1,707,544 |
| Time under $100,000 | 2,954,116 | 2,562,363 | 2,599,595 |

| | | | |
|---|---|---|---|
| Time $100,000 and over | 4,468,225 | 4,391,588 | 4,535,644 |
| Foreign | 3,325,915 | 3,375,426 | 2,797,647 |
| | 38,590,901 | 36,922,753 | 35,774,713 |
| Securities sold, not yet purchased | 29,528 | 224,269 | 21,036 |
| Federal funds purchased | 1,179,197 | 2,463,460 | 2,391,805 |
| Security repurchase agreements | 734,379 | 1,298,112 | 1,070,702 |
| Other liabilities | 649,672 | 644,375 | 560,853 |
| Commercial paper | 40,493 | 297,850 | 411,007 |
| Federal Home Loan Bank advances and other borrowings: | | | |
| One year or less | 4,455,234 | 3,181,990 | 2,037,644 |
| Over one year | 128,855 | 127,612 | 128,218 |
| Long-term debt | 2,569,594 | 2,463,254 | 2,354,317 |
| Total liabilities | 48,377,853 | 47,623,675 | 44,750,295 |
| Minority interest | 30,288 | 30,939 | 37,411 |
| Shareholders equity: | | | |
| Capital stock: | | | |
| Preferred stock, without par value, authorized 3,000,000 shares: | | | |
| Series A and C (liquidation preference $1,000 per share); issued and outstanding 240,000 and 46,949 shares | 286,949 | 240,000 | 240,000 |
| Common stock, without par value; authorized 350,000,000 shares; issued and outstanding 115,302,598, 107,116,505 and 106,934,360 shares | 2,482,517 | 2,212,237 | 2,200,228 |
| Retained earnings | 2,968,242 | 2,910,692 | 2,914,439 |
| Accumulated other comprehensive income (loss) | (157,305) | (58,835) | (86,914) |
| Deferred compensation | (14,376) | (11,294) | (10,773) |
| Total shareholders equity | 5,566,027 | 5,292,800 | 5,256,980 |
| | $ 53,974,168 | $ 52,947,414 | $ 50,044,686 |

*See accompanying notes to consolidated financial statements.*

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ZIONS BANCORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

| (In thousands, except per share amounts) | Three Months Ended September 30, 2008 | Three Months Ended September 30, 2007 | Nine Months Ended September 30, 2008 | Nine Months Ended September 30, 2007 |
|---|---|---|---|---|
| Interest income: | | | | |
| Interest and fees on loans | $ 663,677 | $ 724,598 | $ 1,995,227 | $ 2,096,197 |
| Interest on loans held for sale | 1,916 | 3,695 | 7,632 | 11,892 |
| Lease financing | 5,515 | 5,461 | 17,100 | 15,901 |
| Interest on money market investments | 9,267 | 10,841 | 40,608 | 24,939 |
| Interest on securities: | | | | |
| Held-to-maturity taxable | 21,780 | 2,343 | 39,965 | 6,610 |
| Held-to-maturity nontaxable | 6,319 | 6,402 | 18,972 | 18,720 |
| Available-for-sale taxable | 25,044 | 61,248 | 122,459 | 193,580 |
| Available-for-sale nontaxable | 1,697 | 2,274 | 5,459 | 7,130 |
| Trading account | 437 | 880 | 1,277 | 2,838 |
| Total interest income | 735,652 | 817,742 | 2,248,699 | 2,377,807 |
| Interest expense: | | | | |
| Interest on savings and money market deposits | 90,720 | 123,586 | 274,851 | 353,984 |
| Interest on time and foreign deposits | 74,837 | 119,781 | 264,519 | 353,111 |
| Interest on short-term borrowings | 47,518 | 59,034 | 153,907 | 151,095 |
| Interest on long-term borrowings | 30,574 | 38,704 | 92,218 | 116,550 |
| Total interest expense | 243,649 | 341,105 | 785,495 | 974,740 |
| Net interest income | 492,003 | 476,637 | 1,463,204 | 1,403,067 |
| Provision for loan losses | 156,606 | 55,354 | 363,080 | 82,228 |
| Net interest income after provision for loan losses | 335,397 | 421,283 | 1,100,124 | 1,320,839 |
| Noninterest income: | | | | |
| Service charges and fees on deposit accounts | 53,695 | 46,919 | 154,347 | 135,420 |
| Other service charges, commissions and fees | 42,794 | 44,471 | 127,137 | 126,159 |
| Trust and wealth management income | 8,865 | 9,040 | 28,842 | 26,381 |
| Capital markets and foreign exchange | 12,257 | 11,325 | 34,850 | 32,956 |
| Dividends and other investment income | 7,042 | 14,720 | 30,361 | 37,084 |
| Loan sales and servicing income | 3,633 | 11,607 | 19,959 | 29,863 |
| Income from securities conduit | 336 | 3,221 | 3,960 | 15,704 |
| Fair value and nonhedge derivative loss | (26,155) | (9,391) | (42,157) | (7,222) |
| Equity securities gains, net | 12,971 | 11,072 | 14,918 | 16,370 |
| Fixed income securities gains, net | 135 | 58 | 1,988 | 3,772 |
| Impairment losses on investment securities and valuation losses on securities purchased from Lockhart Funding | (28,022) | | (112,772) | |
| Other | 2,059 | 2,781 | 11,549 | 16,091 |
| Total noninterest income | 89,610 | 145,823 | 272,982 | 432,578 |

| | | | | |
|---|---|---|---|---|
| Noninterest expense: | | | | |
| Salaries and employee benefits | 208,995 | 204,488 | 619,640 | 608,743 |
| Occupancy, net | 30,552 | 27,203 | 84,715 | 80,126 |
| Furniture and equipment | 24,281 | 23,996 | 73,629 | 71,535 |
| Legal and professional services | 11,297 | 10,918 | 30,743 | 31,697 |
| Postage and supplies | 9,257 | 10,024 | 27,582 | 27,096 |
| Advertising | 6,782 | 6,624 | 20,653 | 20,598 |
| Impairment losses on long-lived assets | 2,239 | | 2,239 | |
| Merger related expense | 384 | 682 | 972 | 4,579 |
| Amortization of core deposit and other intangibles | 8,096 | 11,495 | 25,107 | 34,436 |
| Provision (credit) for unfunded lending commitments | (3,264) | 172 | 2,044 | 1,700 |
| Other | 73,657 | 56,429 | 189,472 | 171,112 |
| Total noninterest expense | 372,276 | 352,031 | 1,076,796 | 1,051,622 |
| Income before income taxes and minority interest | 52,731 | 215,075 | 296,310 | 701,795 |
| Income taxes | 11,214 | 71,853 | 83,147 | 246,772 |
| Minority interest | 3,757 | 7,490 | (3,544) | 6,819 |
| Net income | 37,760 | 135,732 | 216,707 | 448,204 |
| Preferred stock dividends | 4,409 | 3,770 | 9,316 | 10,980 |
| Net earnings applicable to common shareholders | $ 33,351 | $ 131,962 | $ 207,391 | $ 437,224 |
| Weighted average common shares outstanding during the period: | | | | |
| Basic shares | 108,407 | 106,814 | 107,176 | 107,671 |
| Diluted shares | 108,497 | 107,880 | 107,333 | 109,059 |
| Net earnings per common share: | | | | |
| Basic | $ 0.31 | $ 1.24 | $ 1.94 | $ 4.06 |
| Diluted | 0.31 | 1.22 | 1.93 | 4.01 |

*See accompanying notes to consolidated financial statements.*

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ZIONS BANCORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY AND COMPREHENSIVE INCOME

(Unaudited)

| (In thousands, except share and per share amounts) | Preferred stock | Common stock Shares | Common stock Amount | Retained earnings | Accumulated other comprehensive income (loss) | Deferred compensation | Total shareholders equity |
|---|---|---|---|---|---|---|---|
| Balance, December 31, 2007 | $ 240,000 | 107,116,505 | $ 2,212,237 | $ 2,910,692 | $ (58,835) | $ (11,294) | $ 5,292,800 |
| Cumulative effect of change in accounting principle, adoption of SFAS 159 | | | | (11,471) | 11,471 | | |
| Comprehensive income: | | | | | | | |
| Net income for the period | | | | 216,707 | | | 216,707 |
| Other comprehensive loss, net of tax: | | | | | | | |
| Net realized and unrealized holding losses on investments and retained interests | | | | | (210,856) | | |
| Foreign currency translation | | | | | (52) | | |
| Reclassification for net realized losses on investments recorded in operations | | | | | 67,129 | | |
| Net unrealized gains on derivative instruments | | | | | 33,104 | | |
| Pension and postretirement | | | | | 734 | | |
| Other comprehensive loss | | | | | (109,941) | | (109,941) |
| Total comprehensive income | | | | | | | 106,766 |
| Issuance of preferred stock | 46,949 | | (503) | | | | 46,446 |
| Issuance of common stock | | 7,194,079 | 244,889 | | | | 244,889 |
| Stock issued under dividend reinvestment plan | | 39,857 | 1,261 | | | | 1,261 |
| Net stock issued under employee plans and related tax benefits | | 952,157 | 24,633 | | | | 24,633 |
| Dividends declared on preferred stock | | | | (9,316) | | | (9,316) |
| Dividends on common stock, $1.29 per share | | | | (138,370) | | | (138,370) |
| Change in deferred compensation | | | | | | (3,082) | (3,082) |
| Balance, September 30, 2008 | $ 286,949 | 115,302,598 | $ 2,482,517 | $ 2,968,242 | $ (157,305) | $ (14,376) | $ 5,566,027 |
| | | | | | | | |
| Balance, December 31, 2006 | $ 240,000 | 106,720,884 | $ 2,230,303 | $ 2,602,189 | $ (75,849) | $ (9,620) | $ 4,987,023 |
| Cumulative effect of change in accounting principle, adoption of FIN 48 | | | | 10,408 | | | 10,408 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Comprehensive income: | | | | | | | |
| Net income for the period | | | | 448,204 | | | 448,204 |
| Other comprehensive loss, net of tax: | | | | | | | |
| Net realized and unrealized holding losses on investments and retained interests | | | | | (49,338) | | |
| Foreign currency translation | | | | | 12 | | |
| Reclassification for net realized gains on investments recorded in operations | | | | | (3,889) | | |
| Net unrealized gains on derivative instruments | | | | | 42,150 | | |
| Other comprehensive loss | | | | | (11,065) | | (11,065) |
| Total comprehensive income | | | | | | | 437,139 |
| Common stock issued in acquisition | | 2,600,117 | 206,075 | | | | 206,075 |
| Stock redeemed and retired | | (3,933,128) | (318,756) | | | | (318,756) |
| Net stock issued under employee plans and related tax benefits | | 1,546,487 | 82,606 | | | | 82,606 |
| Dividends declared on preferred stock | | | | (10,980) | | | (10,980) |
| Dividends on common stock, $1.25 per share | | | | (135,382) | | | (135,382) |
| Change in deferred compensation | | | | | | (1,153) | (1,153) |
| Balance, September 30, 2007 | $ 240,000 | 106,934,360 | $ 2,200,228 | $ 2,914,439 | $ (86,914) | $ (10,773) | $ 5,256,980 |

Total comprehensive income for the three months ended September 30, 2008 and 2007 was $38,780 and $161,658, respectively.

*See accompanying notes to consolidated financial statements.*

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ZIONS BANCORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

| (In thousands) | Three Months Ended September 30, 2008 | Three Months Ended September 30, 2007 | Nine Months Ended September 30, 2008 | Nine Months Ended September 30, 2007 |
|---|---|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | | |
| Net income for the period | $ 37,760 | $ 135,732 | $ 216,707 | $ 448,204 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | | |
| Impairment and valuation losses on investment securities and long-lived assets | 30,261 | | 115,011 | |
| Provision for loan losses | 156,606 | 55,354 | 363,080 | 82,228 |
| Depreciation of premises and equipment | 17,918 | 18,438 | 52,830 | 58,090 |
| Amortization | 19,729 | 12,888 | 48,996 | 35,883 |
| Deferred income tax benefit | (48,293) | (30,075) | (119,187) | (52,099) |
| Share-based compensation | 8,875 | 6,499 | 23,255 | 19,481 |
| Common stock issued for 401(k) employer match | 4,379 | | 4,379 | |
| Excess tax benefits from share-based compensation | (128) | (947) | (527) | (11,540) |
| Gain (loss) allocated to minority interest | 3,757 | 7,490 | (3,544) | 6,819 |
| Equity securities gains, net | (12,971) | (11,072) | (14,918) | (16,370) |
| Fixed income securities gains, net | (135) | (58) | (1,988) | (3,772) |
| Net decrease (increase) in trading securities | 5,901 | 7,314 | (15,819) | 47,942 |
| Principal payments on and proceeds from sales of loans held for sale | 224,344 | 327,892 | 887,700 | 895,809 |
| Additions to loans held for sale | (221,828) | (333,500) | (851,599) | (938,500) |
| Net losses (gains) on sales of loans, leases and other assets | 4,587 | (6,225) | (5,956) | (12,179) |
| Income from increase in cash surrender value of bank-owned life insurance | (6,393) | (6,498) | (18,994) | (19,655) |
| Change in accrued income taxes | 8,861 | 15,721 | (68,764) | 28,782 |
| Change in accrued interest receivable | 14,171 | (6,685) | 36,390 | (5,713) |
| Change in other assets | 164,171 | 74,884 | 82,898 | 70,979 |
| Change in other liabilities | 87,690 | (60,065) | 60,365 | (105,845) |
| Change in accrued interest payable | 1,308 | 4,911 | (10,016) | 2,740 |
| Other, net | (5,271) | (5,896) | 3,580 | (18,833) |
| Net cash provided by operating activities | 495,299 | 206,102 | 783,879 | 512,451 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | | | |
| Net decrease (increase) in money market investments | 250,244 | (353,387) | 487,195 | (351,064) |
| Proceeds from maturities of investment securities held-to-maturity | 28,379 | 36,788 | 82,271 | 90,822 |
| Purchases of investment securities held-to-maturity | (43,162) | (30,339) | (83,345) | (110,091) |
| Proceeds from sales of investment securities available-for-sale | 82,422 | 251,856 | 586,878 | 610,441 |
| Proceeds from maturities of investment securities available-for-sale | 382,356 | 701,567 | 3,021,041 | 2,056,755 |
| Purchases of investment securities available-for-sale | (459,523) | (969,231) | (2,786,420) | (2,250,559) |
| Proceeds from sales of loans and leases | 211,808 | 11,850 | 260,947 | 42,567 |
| Securitized loans purchased | (8,639) | | (1,165,943) | |
| Net increase in loans and leases | (358,017) | (1,000,894) | (2,288,981) | (2,430,212) |
| Net decrease (increase) in other noninterest-bearing investments | (6,624) | (45,145) | (120,492) | 42,069 |
| Proceeds from sales of premises and equipment and other assets | 106 | 3,221 | 8,534 | 6,975 |
| Purchases of premises and equipment | (37,999) | (28,592) | (81,806) | (77,479) |
| Proceeds from sales of other real estate owned | 14,875 | 1,593 | 33,866 | 6,684 |
| Net cash received from (paid for) acquisitions | 688,940 | (12,970) | 688,940 | 27,274 |
| Net cash received from sale of subsidiary | | | | 6,995 |

| | | | | |
|---|---|---|---|---|
| Net cash provided by (used in) investing activities | 745,166 | (1,433,683) | (1,357,315) | (2,328,823) |

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ZIONS BANCORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)

(Unaudited)

| (In thousands) | Three Months Ended September 30, 2008 | Three Months Ended September 30, 2007 | Nine Months Ended September 30, 2008 | Nine Months Ended September 30, 2007 |
|---|---|---|---|---|
| CASH FLOWS FROM FINANCING ACTIVITIES: | | | | |
| Net increase (decrease) in deposits | $ 250,943 | $ (515,847) | $ 936,107 | $ (406,778) |
| Net change in short-term funds borrowed | (1,933,434) | 1,727,137 | (1,027,016) | 2,209,805 |
| Proceeds from FHLB advances and other borrowings over one year | | | 3,500 | |
| Payments on FHLB advances and other borrowings over one year | (619) | (614) | (2,257) | (8,840) |
| Proceeds from issuance of long-term debt | 28,460 | | 261,336 | |
| Debt issuance costs | (64) | | (675) | (32) |
| Payments on long-term debt | (137,000) | (7,732) | (155,025) | (34,982) |
| Proceeds from issuance of preferred stock | 46,446 | | 46,446 | |
| Proceeds from issuance of common stock | 244,914 | 4,017 | 246,355 | 56,423 |
| Payments to redeem common stock | (55) | (90,129) | (2,635) | (321,974) |
| Excess tax benefits from share-based compensation | 128 | 947 | 527 | 11,540 |
| Dividends paid on preferred stock | (4,409) | (3,770) | (9,316) | (10,980) |
| Dividends paid on common stock | (45,542) | (46,136) | (137,109) | (135,382) |
| Net cash provided by (used in) financing activities | (1,550,232) | 1,067,873 | 160,238 | 1,358,800 |
| Net decrease in cash and due from banks | (309,767) | (159,708) | (413,198) | (457,572) |
| Cash and due from banks at beginning of period | 1,751,724 | 1,640,946 | 1,855,155 | 1,938,810 |
| Cash and due from banks at end of period | $ 1,441,957 | $ 1,481,238 | $ 1,441,957 | $ 1,481,238 |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION: | | | | |
| Cash paid for: | | | | |
| Interest | $ 239,041 | $ 335,531 | $ 793,697 | $ 964,517 |
| Income taxes | 42,150 | 84,489 | 259,402 | 256,472 |
| Noncash items: | | | | |
| Investment securities available-for-sale transferred to investment securities held-to-maturity | | | 1,226,832 | |
| Loans transferred to other real estate owned | 57,951 | 4,587 | 192,425 | 14,391 |
| Acquisitions: | | | | |
| Common stock issued | | | | 206,075 |
| Assets acquired | 66,192 | | 66,192 | 1,348,233 |
| Liabilities assumed | 737,116 | | 737,116 | 1,142,158 |

*See accompanying notes to consolidated financial statements.*

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ZIONS BANCORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

September 30, 2008

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Zions Bancorporation ( the Parent ) and its majority-owned subsidiaries (collectively the Company, Zions, we, our, us ) have been prepared in accordance with U.S. generally accepted accounting principles for inte financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Certain prior period amounts have been reclassified to conform to the current period presentation. These reclassifications did not affect net income or shareholders equity.

Operating results for the three- and nine-month periods ended September 30, 2008 are not necessarily indicative of the results that may be expected in future periods. The consolidated balance sheet at December 31, 2007 is from the audited financial statements at that date, but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2007.

The Company provides a full range of banking and related services through banking subsidiaries in ten Western and Southwestern states as follows: Zions First National Bank ( Zions Bank ), in Utah and Idaho; California Bank & Trust ( CB&T ); Amegy Corporation ( Amegy ) and its subsidiary, Amegy Bank, in Texas; National Bank of Arizona ( NBA ); Nevada State Bank ( NSB ); Vectra Bank Colorado ( Vectra ), in Colorado and New Mexico; The Commerce Bank of Washington ( TCBW ); and The Commerce Bank of Oregon ( TCBO ). The Parent also owns and operates certain nonbank subsidiaries that engage in the development and sale of financial technologies and related services.

2. CERTAIN RECENT ACCOUNTING PRONOUNCEMENTS

In March 2008, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 161, *Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133*. SFAS 161, among other things, requires greater transparency in disclosing information about derivatives including the objectives for their use, the volume of derivative activity, tabular disclosure of financial statement amounts, and any credit-risk-related features. The Statement is effective for annual and interim financial statements beginning after November 15, 2008. Earlier application is encouraged but not required. Management is evaluating the impact this Statement may have on the Company s financial statements.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations*, and SFAS No. 160, *Accounting and Reporting of Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51*. These new standards will significantly change the financial accounting and reporting of business combination transactions and noncontrolling (or minority) interests in consolidated financial statements. Both Statements are effective for annual and interim financial statements beginning on or after December 15, 2008. Generally, adoption is prospective and early adoption is prohibited. Management is evaluating the impact these Statements may have on the Company s financial statements.

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Effective January 1, 2008, we adopted the provisions of FASB Staff Position ( FSP ) FIN 39-1, *Offsetting of Amounts Related to Certain Contracts*. FSP FIN 39-1 permits entities to offset fair value amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) against recognized fair value amounts of derivatives executed with the same counterparty under a master netting arrangement. At September 30, 2008, cash collateral was used to reduce recorded amounts of derivative assets by approximately $69 million. The reduction of derivative liabilities was insignificant.

Additional accounting pronouncements recently adopted are discussed where applicable in the Notes to Consolidated Financial Statements.

3. ACQUISITION

Effective September 5, 2008, the Company acquired from the FDIC the insured deposits and certain assets of the failed Silver State Bank, headquartered in Henderson, Nevada. The acquisition was made through the Company s Nevada State Bank and National Bank of Arizona subsidiaries and included approximately $737 million of deposits and $66 million of assets.

4. INVESTMENT SECURITIES

As a result of an ongoing valuation review of our investment securities portfolio, we recognized a pretax charge of approximately $28.0 million during the third quarter of 2008 for certain investment securities deemed to have other-than-temporary impairment ( OTTI ). Details of this OTTI are as follows:

$19.2 million for three bank and insurance trust preferred collateralized debt obligations ( CDOs )

$1.3 million for two bank and insurance income notes (OTTI also taken previously)

$4.1 million for three trust preferred CDOs related to real estate investment trusts ( REITs ) (OTTI also taken previously)

$3.4 million for two structured asset-backed ( ABS ) CDOs

For the first nine months of 2008, total OTTI was $107.6 million. As discussed in Note 5, valuation losses on securities purchased from Lockhart Funding, LLC ( Lockhart ) during the first quarter of 2008 were $5.2 million. The total of these amounts comprises the Impairment losses on investment securities and valuation losses on securities purchased from Lockhart Funding in the statement of income for the first nine months of 2008.

During the second quarter of 2008, we reassessed the classification of certain asset-backed and trust preferred CDOs. On April 28, 2008, we reclassified approximately $1.2 billion at fair value of these available-for-sale ( AFS ) securities to held-to-maturity ( HTM ). The related unrealized pretax loss of approximately $273 million included in accumulated other comprehensive income ( OCI ) remained in OCI and is being amortized as a yield adjustment through earnings over the remaining terms of the securities. No gain or loss was recognized at the time of reclassification. We consider the HTM classification to be more appropriate because we have the ability and the intent to hold these securities to maturity.

At September 30, 2008, unrealized pretax losses recognized in OCI were $248.5 million for HTM securities and $145.8 million for AFS securities.

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5. OFF-BALANCE SHEET ARRANGEMENT

Zions Bank provides a liquidity facility for a fee to Lockhart, which is an off-balance sheet qualifying special-purpose entity ( QSPE ) securities conduit. Lockhart was structured to purchase floating rate U.S. Government and AAA-rated securities with funds from the issuance of asset-backed commercial paper. Zions Bank also provides interest rate hedging support and administrative and investment advisory services for a fee.

Pursuant to the Liquidity Agreement, Zions Bank is required to purchase nondefaulted securities from Lockhart to provide funds for Lockhart to repay maturing commercial paper upon Lockhart s inability to access a sufficient amount of funding in the commercial paper market, or upon a commercial paper market disruption as specified in governing documents for Lockhart. Pursuant to the governing documents, including the Liquidity Agreement, if any security in Lockhart is downgraded below AA-, or the downgrade of one or more securities results in more than ten securities having ratings of AA+ to AA-, Zions Bank must either 1) place its letter of credit on the security, 2) obtain credit enhancement from a third party, or 3) purchase the security from Lockhart at book value. Zions Bank may incur losses if it is required to purchase securities from Lockhart when the fair value of the securities at the time of purchase is less than book value.

During the first and second quarters of 2008, Zions Bank purchased an aggregate of $1,067 million of securities and related accrued interest at book value from Lockhart. Of these purchases, $792 million were required by the Liquidity Agreement when the securities, and MBIA Inc. which insured certain of the securities, were downgraded below AA-. The remaining $275 million were due to the inability of Lockhart to issue a sufficient amount of commercial paper.

The securities purchased included $987 million which comprised the entire remaining small business loan securitizations created by Zions Bank and held by Lockhart. No gain or loss was recognized on these purchases. Upon dissolution of the securitization trusts (including a total of $170 million of related securities owned by the Parent), Zions Bank recorded $1,180 million of loans on its balance sheet including $23 million of premium. See further discussion of this premium in Note 9.

The commitment of Zions Bank to Lockhart cannot exceed the book value of Lockhart s securities portfolio, which was approximately $828 million at September 30, 2008. Lockhart is limited in size by program agreements, agreements with rating agencies, and the size of the liquidity facility. The book value of Lockhart s remaining securities portfolio exceeded the fair value of the securities by approximately $110 million at September 30, 2008. During the first quarter of 2008, Zions Bank recorded valuation losses of approximately $5.2 million when it purchased certain securities from Lockhart.

As permitted by the governing documents, the Company has also purchased asset-backed commercial paper from Lockhart and held approximately $557 million on its balance sheet at September 30, 2008. The average amount of Lockhart commercial paper included in money market investments for the three months ended September 30, 2008 was approximately $597 million. These purchases were made to provide liquidity to Lockhart due to ongoing contraction and disruptions in the asset-backed commercial paper markets. If at any given time the Company were to own more than 90% of Lockhart s outstanding commercial paper (beneficial interest), Lockhart would cease to be a QSPE and the Company would be required to consolidate Lockhart in its financial statements.

On September 15, 2008, the FASB issued a proposed amendment, *Accounting for Transfers of Financial Assets, an amendment of FASB Statement No. 140*, that among other things, would remove the concept of a QSPE and remove the exception from applying FIN 46R to QSPEs. The proposed amendment would be effective for calendar-year companies beginning in 2010. Management is monitoring these developments as they relate to the operations and existence of Lockhart.

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6. DEBT

During the third quarter and first nine months of 2008, the Company issued a net amount of $28.5 million and $261.3 million, respectively, of one- and two-year senior medium-term notes at coupon rates ranging from 4.50% to 5.65%. Interest is payable semiannually. These unsecured notes were sold via Zions online auction process and direct sales. They were issued under the Company s existing shelf registration with the Securities and Exchange Commission ( SEC ).

The Company repaid senior medium-term notes of $137 million and $155 million during the third quarter and first nine months of 2008, respectively.

7. INCOME TAXES

The lower effective tax rate during the third quarter of 2008 is mainly due to lower taxable income in 2008, which increased the proportion of nontaxable income relative to total income. Income tax expense for the first nine months of 2008 included a net benefit of approximately $5.3 million primarily from a settlement with governmental authorities during the second quarter that allowed the Company to reduce its liability and related interest for uncertain tax positions under the provisions of FIN 48.

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8. SHAREHOLDERS EQUITY

Changes in accumulated other comprehensive income (loss) are summarized as follows (*in thousands*):

| | Net unrealized gains (losses) on investments, retained interests and other | Net unrealized gains (losses) on derivative instruments | Pension and post-retirement | Total |
|---|---|---|---|---|
| Nine Months Ended September 30, 2008: | | | | |
| Balance, December 31, 2007 | $ (108,766) | $ 65,213 | $ (15,282) | $ (58,835) |
| Cumulative effect of change in accounting principle, adoption of SFAS 159 | 11,471 | | | 11,471 |
| Other comprehensive income (loss), net of tax: | | | | |
| Net realized and unrealized holding losses, net of income tax benefit of $130,611 | (210,856) | | | (210,856) |
| Foreign currency translation | (52) | | | (52) |
| Reclassification for net realized losses recorded in operations, net of income tax benefit of $41,582 | 67,129 | | | 67,129 |
| Net unrealized gains, net of reclassification to operations of $40,219 and income tax expense of $20,927 | | 33,104 | | 33,104 |
| Pension and postretirement, net of income tax expense of $477 | | | 734 | 734 |
| Other comprehensive income (loss) | (143,779) | 33,104 | 734 | (109,941) |
| Balance, September 30, 2008 | $ (241,074) | $ 98,317 | $ (14,548) | $ (157,305) |
| Nine Months Ended September 30, 2007: | | | | |
| Balance, December 31, 2006 | $ (18,371) | $ (41,716) | $ (15,762) | $ (75,849) |
| Other comprehensive income (loss), net of tax: | | | | |
| Net realized and unrealized holding losses, net of income tax benefit of $30,562 | (49,338) | | | (49,338) |
| Foreign currency translation | 12 | | | 12 |
| Reclassification for net realized gains recorded in operations, net of income tax expense of $2,409 | (3,889) | | | (3,889) |
| Net unrealized gains, net of reclassification to operations of $(33,432) and income tax expense of $27,953 | | 42,150 | | 42,150 |
| Other comprehensive income (loss) | (53,215) | 42,150 | | (11,065) |
| Balance, September 30, 2007 | $ (71,586) | $ 434 | $ (15,762) | $ (86,914) |

On July 2, 2008, the Company completed a $47 million offering of 9.50% Series C Fixed-Rate Non-Cumulative Perpetual Preferred Stock. The Company issued 46,949 shares in the form of 1,877,971 depositary shares with each depositary share representing a 1/40th ownership interest in a share of the preferred stock. Terms and conditions, except for the dividend amount, are generally similar to the existing issuance of Series A floating rate preferred stock described in the Company s Annual Report on Form 10-K for the year ended December 31, 2007. The offering was sold via Zions online auction process and direct sales primarily by the Company s broker/dealer subsidiary.

During September 8-11, 2008, the Company issued $250 million of new common stock consisting of 7,194,079 shares at an average price of $34.75 per share. Net of issuance costs and fees, this issuance added $244.9 million to common shareholders equity.

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On October 27, 2008, the U.S. Department of the Treasury gave preliminary approval to the Company s application to receive a capital investment of $1.4 billion. The application was made under the Treasury s Capital Purchase Program announced on October 14, 2008. The capital investment is expected to be received prior to year-end and will be in the form of nonvoting senior preferred shares pari passu with the Company s existing preferred shares. The Company will also issue to the Treasury warrants exercisable for 10 years to purchase $210 million of the Company s common shares. The number of common shares issuable under the warrants will be determined from the average share price during a specified 20-day trading period. The preferred shares will qualify for regulatory Tier 1 capital and may be redeemed after three years. They will have a dividend rate of 5% for the first five years, increasing to 9% thereafter. Among other things, the Company will be subject to restrictions and conditions including those related to common dividends, share repurchases, executive compensation, and corporate governance.

9. FAIR VALUE

Effective January 1, 2008, the Company adopted SFAS No. 157, *Fair Value Measurements*, and SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*. Both Standards address the application of fair value accounting and reporting.

**Fair Value Measurements**

SFAS 157 defines fair value, establishes a consistent framework for measuring fair value, and enhances disclosures about fair value measurements. In February 2008, the FASB amended SFAS 157 with the issuance of FSP FAS 157-1, which excludes with certain exceptions SFAS No. 13, *Accounting for Leases*, from the scope of SFAS 157, and FSP FAS 157-2, which delayed the adoption of SFAS 157 for one year for the measurement of nonfinancial assets and nonfinancial liabilities. There was no material effect from the adoption of SFAS 157 on the Company s consolidated financial statements.

SFAS 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. To measure fair value, SFAS 157 has established a hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs. This hierarchy uses three levels of inputs to measure the fair value of assets and liabilities as follows:

Level 1 Quoted prices in active markets for identical assets or liabilities; includes certain U.S. Treasury and other U.S. Government and agency securities actively traded in over-the-counter markets; certain securities sold, not yet purchased; and certain derivatives.

Level 2 Observable inputs other than Level 1 including quoted prices for similar assets or liabilities, quoted prices in less active markets, or other observable inputs that can be corroborated by observable market data; also includes derivative contracts whose value is determined using a pricing model with observable market inputs or can be derived principally from or corroborated by observable market data. This category generally includes certain U.S. Government and agency securities; certain CDO securities; corporate debt securities; certain private equity investments; certain securities sold, not yet purchased; and certain derivatives.

Level 3 Unobservable inputs supported by little or no market activity for financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation; also includes observable inputs for nonbinding single dealer quotes not corroborated by observable market data. This category generally includes certain CDO securities, certain private equity investments, and retained interests from securitizations.

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The Company uses fair value to measure certain assets and liabilities on a recurring basis when fair value is the primary measure for accounting. This is done primarily for available-for-sale and trading investment securities; certain private equity investments; certain retained interests from securitizations; securities sold, not yet purchased; and derivatives. Fair value is used on a nonrecurring basis to measure certain assets when applying lower of cost or market accounting or when adjusting carrying values, such as for loans held for sale, impaired loans, certain private equity investments, and other real estate owned. Fair value is also used when evaluating impairment on certain assets, including held-to-maturity and available-for-sale securities, goodwill, and core deposit and other intangibles, and for annual disclosures required by SFAS No. 107, *Disclosures about Fair Value of Financial Instruments*.

Available-for-sale and trading investment securities are fair valued under Level 1 using quoted market prices when available for identical securities. When quoted prices are not available, fair values are determined under Level 2 using quoted prices for similar securities or independent pricing services that incorporate observable market data when possible. Available-for-sale securities include certain CDOs that consist of trust preferred securities related to banks and insurance companies and to REITs. Where possible, the fair value of these CDOs is priced under Level 2 using a whole market price quote method that incorporates matrix pricing and uses the prices of securities of similar type and rating to value comparable securities held by the Company. This method is described more fully in the Company s Annual Report on Form 10-K for the year ended December 31, 2007. If sufficient information is not available for matrix pricing, fair value is determined under Level 3 using nonbinding single dealer quotes or the model pricing discussed subsequently.

At September 30, 2008 due to the market conditions subsequently described, the Company determined that certain CDOs with an amortized cost of $1,878 million at September 30, 2008 previously fair valued under a Level 2 matrix approach would be more appropriately fair valued under a Level 3 cash flow modeling approach. Additional securities of $190 million at amortized cost previously fair valued with Level 3 single dealer quotes were also moved to a Level 3 cash flow modeling approach. The total of these amounts, or $2,068 million, included approximately $1,353 million accounted for as HTM securities.

Because of recent market disruptions, particularly during the third quarter of 2008, both the SEC on September 30, 2008 (Release No. 2008-234) and the FASB on October 10, 2008 (FSP FAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active*) issued additional guidance on fair value accounting when markets become distressed and inactive. In general, this guidance clarifies under such market conditions when and how an entity might appropriately determine fair value using unobservable inputs under Level 3 rather than using observable inputs under Level 2, particularly when significant adjustments become necessary under Level 2 and extensive judgment must be employed to evaluate inputs and results in estimating fair value.

The Company values its CDO portfolio using several methodologies that primarily include internal and third party models and to a lesser extent dealer quotes and pricing services. A licensed model is used internally to fair value bank and insurance trust preferred CDOs. This model uses estimated values of expected losses on underlying collateral and applies market-based discount rates on resultant cash flows to estimate fair value. Third party models are used to fair value certain REIT and ABS CDOs. These models utilize relevant data assumptions, which are evaluated by the Company for reasonableness. These assumptions include but are not limited to probability of default, collateral recovery rates, discount rates, over-collateralization levels, and rating transition probability matrices from rating agencies. The model prices obtained from third party services were evaluated for reasonableness including quarter to quarter changes in assumptions and comparison to other available data which included third party and internal model results and valuations. The Company s decision to use Level 3 model pricing for certain CDOs was made due to continued trading contraction of these securities and the lack of observable market inputs to value such securities.

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Private equity investments valued under Level 2 on a recurring basis are investments in partnerships that invest in financial institutions. Fair values are determined from net asset values provided by the partnerships. Private equity investments valued under Level 3 on a nonrecurring basis are recorded initially at acquisition cost, which is considered the best indication of fair value unless there have been significant subsequent positive or negative developments that justify an adjustment in the fair value estimate. Subsequent adjustments to recorded amounts are based as necessary on current and projected financial performance, recent financing activities, economic and market conditions, market comparables, market liquidity, sales restrictions, and other factors.

Retained interests from securitizations are fair valued under Level 3 based on the modeling techniques previously described. The assumptions used in the models are evaluated quarterly.

Derivatives are fair valued primarily under Level 2 using third party services. Observable market inputs include yield curves, option volatilities, counterparty credit risk, and other related data. Certain foreign exchange derivatives have been fair valued under Level 1 because they are traded in active markets. Amounts disclosed in the following table are net of the cash collateral offsets pursuant to the guidance of FSP FIN 39-1, as discussed in Note 2.

Securities sold, not yet purchased are fair valued under Level 1 when quoted prices are available for the securities involved. Those under Level 2 are fair valued similar to trading account investment securities.

Assets and liabilities measured at fair value on a recurring basis, including those elected under SFAS 159, are summarized as follows at September 30, 2008 *(in thousands)*:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| **ASSETS** | | | | |
| Investment securities: | | | | |
| Available-for-sale | $ 40,610 | $ 1,985,267 | $ 766,359 | $ 2,792,236 |
| Trading account | | 40,364 | 5,405 (1) | 45,769 |
| Other noninterest-bearing investments: | | | | |
| Private equity | | 26,660 | | 26,660 |
| Other assets: | | | | |
| Derivatives | 9,847 | 286,795 | | 296,642 |
| | $ 50,457 | $ 2,339,086 | $ 771,764 | $ 3,161,307 |
| **LIABILITIES** | | | | |
| Securities sold, not yet purchased | | $ 29,528 | | $ 29,528 |
| Other liabilities: | | | | |
| Derivatives | $ 6,747 | 158,229 | | 164,976 |
| Other | | | $ 1,422 | 1,422 |
| | $ 6,747 | $ 187,757 | $ 1,422 | $ 195,926 |

(1) Elected under SFAS 159 for fair value option, as discussed subsequently.

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The following reconciles the beginning and ending balances of assets and liabilities for the three- and nine-month periods ended September 30, 2008 that are measured at fair value on a recurring basis using Level 3 inputs *(in thousands)*:

| | Level 3 Instruments Three Months Ended September 30, 2008 | | | |
|---|---|---|---|---|
| | Investment securities | | Retained | |
| | Available-for-sale | Trading account (1) | interests from securitizations (1) | Other liabilities |
| Balance at June 30, 2008 | $ 182,268 | $ 5,724 | $ | $ (292) |
| Total net gains (losses) included in: | | | | |
| Statement of income (2): | | | | |
| Fair value and nonhedge derivative income (loss) | | (319) | | |
| Impairment losses on available-for sale securities | (14,006) | | | |
| Other noninterest expense | | | | (1,130) |
| Other comprehensive income (loss) | (57,429) | | | |
| Purchases, sales, issuances, and settlements, net | (4,315) | | | |
| Net transfers in (out) | 659,841 | | | |
| Balance at September 30, 2008 | $ 766,359 | $ 5,405 | $ | $ (1,422) |

| | Level 3 Instruments Nine Months Ended September 30, 2008 | | | |
|---|---|---|---|---|
| | Investment securities | | Retained | |
| | Available-for-sale | Trading account (1) | interests from securitizations (1) | Other liabilities |
| Balance at January 1, 2008 | $ 337,338 | $ 8,100 | $ 42,426 | $ (44) |
| Total net gains (losses) included in: | | | | |
| Statement of income (2): | | | | |
| Fair value and nonhedge derivative income (loss) | | (2,695) | (2,098) | |
| Impairment losses on available-for sale securities and valuation losses on securities purchased from Lockhart Funding | (82,032) | | | |
| Other noninterest expense | | | | (378) |
| Other comprehensive income (loss) | (123,560) | | | |
| Proceeds from ESOARS auction | | | | |