

COMMERCE BANCSHARES INC /MO/  
Form 10-Q  
November 07, 2016  
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q  
(Mark One)

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

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For the quarterly period ended September 30, 2016

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

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

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

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

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

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

Yes  No

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

Yes  No

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

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

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

Yes  No

As of November 2, 2016, the registrant had outstanding 96,592,152 shares of its \$5 par value common stock, registrant's only class of common stock.

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Commerce Bancshares, Inc. and Subsidiaries

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## PART I: FINANCIAL INFORMATION

## Item 1. FINANCIAL STATEMENTS

Commerce Bancshares, Inc. and Subsidiaries  
CONSOLIDATED BALANCE SHEETS

|  | September 30,<br>2016<br>(Unaudited)<br>(In thousands) | December 31,<br>2015 |
|--|--|----------------------|
| <b>ASSETS</b>  |  |                      |
| Loans  | \$ 13,230,241  | \$ 12,436,692        |
| Allowance for loan losses  | (154,532 )   | (151,532 )           |
| Net loans  | 13,075,709   | 12,285,160           |
| Loans held for sale (including \$4,447,000 of residential mortgage loans carried at fair value at September 30, 2016 and \$4,981,000 at December 31, 2015) | 9,511  | 7,607                |
| Investment securities:   |  |                      |
| Available for sale (\$578,090,000 pledged at September 30, 2016 and \$568,257,000 at December 31, 2015 to secure swap and repurchase agreements)           | 9,438,871  | 9,777,004            |
| Trading  | 28,586   | 11,890               |
| Non-marketable   | 108,224  | 112,786              |
| Total investment securities  | 9,575,681  | 9,901,680            |
| Federal funds sold and short-term securities purchased under agreements to resell  | 13,415   | 14,505               |
| Long-term securities purchased under agreements to resell  | 725,000  | 875,000              |
| Interest earning deposits with banks   | 56,767   | 23,803               |
| Cash and due from banks  | 396,938  | 464,411              |
| Land, buildings and equipment, net   | 339,196  | 352,581              |
| Goodwill   | 138,921  | 138,921              |
| Other intangible assets, net   | 6,621  | 6,669                |
| Other assets   | 396,709  | 534,625              |
| Total assets   | \$24,734,468   | \$24,604,962         |
| <b>LIABILITIES AND EQUITY</b>  |  |                      |
| Deposits:  |  |                      |
| Non-interest bearing   | \$7,130,415  | \$7,146,398          |
| Savings, interest checking and money market  | 11,023,526   | 10,834,746           |
| Time open and C.D.'s of less than \$100,000  | 732,575  | 785,191              |
| Time open and C.D.'s of \$100,000 and over   | 1,279,644  | 1,212,518            |
| Total deposits   | 20,166,160   | 19,978,853           |
| Federal funds purchased and securities sold under agreements to repurchase   | 1,489,891  | 1,963,552            |
| Other borrowings   | 101,415  | 103,818              |
| Other liabilities  | 416,189  | 191,321              |
| Total liabilities  | 22,173,655   | 22,237,544           |
| Commerce Bancshares, Inc. stockholders' equity:  |  |                      |
| Preferred stock, \$1 par value   |  |                      |
| Authorized 2,000,000 shares; issued 6,000 shares   | 144,784  | 144,784              |
| Common stock, \$5 par value  |  |                      |
| Authorized 120,000,000 shares;   |  |                      |
| issued 97,972,433 shares   | 489,862  | 489,862              |

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|  |              |              |
|--|--------------|--------------|
| Capital surplus  | 1,335,150    | 1,337,677    |
| Retained earnings  | 515,081      | 383,313      |
| Treasury stock of 1,212,837 shares at September 30, 2016<br>and 603,003 shares at December 31, 2015, at cost | (50,538      | ) (26,116 )  |
| Accumulated other comprehensive income   | 121,082      | 32,470       |
| Total Commerce Bancshares, Inc. stockholders' equity   | 2,555,421    | 2,361,990    |
| Non-controlling interest   | 5,392        | 5,428        |
| Total equity   | 2,560,813    | 2,367,418    |
| Total liabilities and equity   | \$24,734,468 | \$24,604,962 |

See accompanying notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF INCOME

|   | For the Three<br>Months Ended<br>September 30 |            | For the Nine<br>Months Ended<br>September 30 |            |
|---|---|------------|--|------------|
|   | 2016  | 2015       | 2016   | 2015       |
| (In thousands, except per share data)   |   |            |  |            |
|   | (Unaudited)                                   |            |  |            |
| <b>INTEREST INCOME</b>  |   |            |  |            |
| Interest and fees on loans  | \$ 123,750                                    | \$ 114,954 | \$ 364,234                                   | \$ 339,707 |
| Interest and fees on loans held for sale  | 334   | 48         | 1,161  | 108        |
| Interest on investment securities   | 51,661  | 50,716     | 155,250                                      | 142,416    |
| Interest on federal funds sold and short-term securities purchased under agreements to resell | 20  | 21         | 63   | 45         |
| Interest on long-term securities purchased under agreements to resell                         | 3,328   | 3,273      | 10,157                                       | 9,994      |
| Interest on deposits with banks   | 268   | 103        | 689  | 404        |
| Total interest income   | 179,361                                       | 169,115    | 531,554                                      | 492,674    |
| <b>INTEREST EXPENSE</b>   |   |            |  |            |
| Interest on deposits:   |   |            |  |            |
| Savings, interest checking and money market   | 3,619   | 3,356      | 10,651                                       | 9,951      |
| Time open and C.D.'s of less than \$100,000   | 683   | 786        | 2,134  | 2,484      |
| Time open and C.D.'s of \$100,000 and over  | 2,186   | 1,554      | 6,519  | 4,468      |
| Interest on federal funds purchased and securities sold under agreements to repurchase        | 724   | 483        | 2,337  | 1,271      |
| Interest on other borrowings  | 906   | 898        | 3,066  | 2,667      |
| Total interest expense  | 8,118   | 7,077      | 24,707                                       | 20,841     |
| Net interest income   | 171,243                                       | 162,038    | 506,847                                      | 471,833    |
| Provision for loan losses   | 7,263   | 8,364      | 25,918                                       | 19,541     |
| Net interest income after provision for loan losses   | 163,980                                       | 153,674    | 480,929                                      | 452,292    |
| <b>NON-INTEREST INCOME</b>  |   |            |  |            |
| Bank card transaction fees  | 47,006  | 44,635     | 136,541                                      | 132,606    |
| Trust fees  | 30,951  | 29,302     | 90,435                                       | 88,815     |
| Deposit account charges and other fees  | 22,241  | 20,674     | 64,260                                       | 58,810     |
| Capital market fees   | 2,751   | 2,620      | 7,976  | 8,360      |
| Consumer brokerage services   | 3,375   | 3,687      | 10,375                                       | 10,530     |
| Loan fees and sales   | 3,123   | 1,855      | 8,829  | 6,127      |
| Other   | 9,872   | 8,515      | 36,497                                       | 26,849     |
| Total non-interest income   | 119,319                                       | 111,288    | 354,913                                      | 332,097    |
| INVESTMENT SECURITIES GAINS (LOSSES), NET   | (1,965)                                       | (378)      | (3,704)                                      | 7,800      |
| <b>NON-INTEREST EXPENSE</b>   |   |            |  |            |
| Salaries and employee benefits  | 107,004                                       | 100,874    | 318,671                                      | 298,603    |
| Net occupancy   | 12,366  | 11,247     | 34,761                                       | 33,807     |
| Equipment   | 4,842   | 4,789      | 14,257                                       | 14,171     |
| Supplies and communication  | 5,968   | 5,609      | 18,490                                       | 16,416     |
| Data processing and software  | 23,663  | 21,119     | 69,332                                       | 61,670     |
| Marketing   | 4,399   | 4,343      | 12,601                                       | 12,568     |
| Deposit insurance   | 3,576   | 2,981      | 9,884  | 9,001      |
| Other   | 19,424  | 20,440     | 57,808                                       | 54,474     |
| Total non-interest expense  | 181,242                                       | 171,402    | 535,804                                      | 500,710    |

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|  |          |          |           |           |
|--|----------|----------|-----------|-----------|
| Income before income taxes                           | 100,092  | 93,182   | 296,334   | 291,479   |
| Less income taxes                                    | 30,942   | 27,969   | 91,854    | 88,929    |
| Net income   | 69,150   | 65,213   | 204,480   | 202,550   |
| Less non-controlling interest expense                | 605      | 601      | 668       | 2,530     |
| Net income attributable to Commerce Bancshares, Inc. | 68,545   | 64,612   | 203,812   | 200,020   |
| Less preferred stock dividends                       | 2,250    | 2,250    | 6,750     | 6,750     |
| Net income available to common shareholders          | \$66,295 | \$62,362 | \$197,062 | \$193,270 |
| Net income per common share — basic                  | \$.69    | \$.63    | \$2.04    | \$1.93    |
| Net income per common share — diluted                | \$.68    | \$.63    | \$2.03    | \$1.93    |

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<br>September 30 |          | For the Nine Months<br>Ended September 30 |           |
|---|---|----------|---|-----------|
|   | 2016  | 2015     | 2016                                      | 2015      |
|   | (Unaudited)                                   |          |   |           |
| Net income  | \$69,150                                      | \$65,213 | \$204,480                                 | \$202,550 |
| Other comprehensive income (loss):  |   |          |   |           |
| Net unrealized gains (losses) on securities for which a portion of an other-than-temporary impairment has been recorded in earnings | 46  | (327 )   | (352 )                                    | (306 )    |
| Net unrealized gains (losses) on other securities   | (13,747 )                                     | 16,891   | 87,887                                    | 2,754     |
| Pension loss amortization   | 359   | 283      | 1,077                                     | 1,095     |
| Other comprehensive income (loss)   | (13,342 )                                     | 16,847   | 88,612                                    | 3,543     |
| Comprehensive income  | 55,808  | 82,060   | 293,092                                   | 206,093   |
| Less non-controlling interest expense   | 605   | 601      | 668                                       | 2,530     |
| Comprehensive income attributable to Commerce Bancshares, Inc.  | \$55,203                                      | \$81,459 | \$292,424                                 | \$203,563 |
| 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<br>per share data)                               | Preferred<br>Stock | Common<br>Stock | Capital<br>Surplus | Retained<br>Earnings | Treasury<br>Stock | Accumulated<br>Other<br>Comprehensive<br>Income<br>(Loss) | Non-Controlling<br>Interest | Total        |
|--|--------------------|-----------------|--------------------|----------------------|-------------------|---|-----------------------------|--------------|
|  | (Unaudited)        |                 |                    |                      |                   |   |                             |              |
| Balance January 1, 2016  | \$ 144,784         | \$ 489,862      | \$ 1,337,677       | \$ 383,313           | \$ (26,116 )      | \$ 32,470   | \$ 5,428                    | \$ 2,367,418 |
| Net income   |                    |                 |                    | 203,812              |                   |   | 668                         | 204,480      |
| Other comprehensive<br>income  |                    |                 |                    |                      |                   | 88,612  |                             | 88,612       |
| Distributions to<br>non-controlling interest                           |                    |                 |                    |                      |                   |   | (704 )                      | (704 )       |
| Purchases of treasury<br>stock   |                    |                 |                    |                      | (38,476 )         |   |                             | (38,476 )    |
| Issuance of stock under<br>purchase and equity<br>compensation plans   |                    |                 | (14,057 )          |                      | 14,054            |   |                             | (3 )         |
| Excess tax benefit<br>related to equity<br>compensation plans          |                    |                 | 2,629              |                      |                   |   |                             | 2,629        |
| Stock-based<br>compensation  |                    |                 | 8,901              |                      |                   |   |                             | 8,901        |
| Cash dividends on<br>common stock (\$.675<br>per share)                |                    |                 |                    | (65,294 )            |                   |   |                             | (65,294 )    |
| Cash dividends on<br>preferred stock (\$1.125<br>per depositary share) |                    |                 |                    | (6,750 )             |                   |   |                             | (6,750 )     |
| Balance September 30,<br>2016  | \$ 144,784         | \$ 489,862      | \$ 1,335,150       | \$ 515,081           | \$ (50,538 )      | \$ 121,082  | \$ 5,392                    | \$ 2,560,813 |
| Balance January 1, 2015  | \$ 144,784         | \$ 484,155      | \$ 1,229,075       | \$ 426,648           | \$ (16,562 )      | \$ 62,093   | \$ 4,053                    | \$ 2,334,246 |
| Net income   |                    |                 |                    | 200,020              |                   |   | 2,530                       | 202,550      |
| Other comprehensive<br>income  |                    |                 |                    |                      |                   | 3,543   |                             | 3,543        |
| Distributions to<br>non-controlling interest                           |                    |                 |                    |                      |                   |   | (845 )                      | (845 )       |
| Purchases of treasury<br>stock   |                    |                 |                    |                      | (9,147 )          |   |                             | (9,147 )     |
| Accelerated share<br>repurchase agreements                             |                    |                 | 60,000             |                      | (160,000 )        |   |                             | (100,000 )   |
| Issuance of stock under<br>purchase and equity<br>compensation plans   |                    |                 | (15,302 )          |                      | 17,216            |   |                             | 1,914        |
| Excess tax benefit<br>related to equity                                |                    |                 | 1,871              |                      |                   |   |                             | 1,871        |

|  |            |            |              |            |              |           |          |              |
|--|------------|------------|--------------|------------|--------------|-----------|----------|--------------|
| compensation plans   |            |            |              |            |              |           |          |              |
| Stock-based compensation   |            | 7,702      |              |            |              |           |          | 7,702        |
| Cash dividends on common stock (\$.643 per share)                |            |            | (64,041 )    |            |              |           |          | (64,041 )    |
| Cash dividends on preferred stock (\$1.125 per depositary share) |            |            | (6,750 )     |            |              |           |          | (6,750 )     |
| Balance September 30, 2015                                       | \$ 144,784 | \$ 484,155 | \$ 1,283,346 | \$ 555,877 | \$ (168,493) | \$ 65,636 | \$ 5,738 | \$ 2,371,043 |

See accompanying notes to consolidated financial statements.

Table of ContentsCommerce Bancshares, Inc. and Subsidiaries  
CONSOLIDATED STATEMENTS OF CASH FLOWS

| (In thousands)   | For the Nine Months<br>Ended September 30 |              |
|--|---|--------------|
|  | 2016                                      | 2015         |
|  | (Unaudited)                               |              |
| <b>OPERATING ACTIVITIES:</b>   |   |              |
| Net income   | \$204,480                                 | \$202,550    |
| Adjustments to reconcile net income to net cash provided by operating activities:                                |   |              |
| Provision for loan losses  | 25,918                                    | 19,541       |
| Provision for depreciation and amortization  | 30,997                                    | 32,100       |
| Amortization of investment security premiums, net  | 23,357                                    | 23,249       |
| Investment securities (gains) losses, net (A)  | 3,704                                     | (7,800 )     |
| Net gains on sales of loans held for sale  | (4,924 )                                  | (2,184 )     |
| Originations of loans held for sale  | (115,768 )                                | (75,589 )    |
| Proceeds from sales of loans held for sale   | 117,746                                   | 72,973       |
| Net (increase) decrease in trading securities, excluding unsettled transactions                                  | 77,262                                    | (5,042 )     |
| Stock-based compensation   | 8,901                                     | 7,702        |
| Increase in interest receivable  | (331 )                                    | (2,652 )     |
| Increase (decrease) in interest payable  | 269                                       | (96 )        |
| Increase in income taxes payable   | 1,787                                     | 16,312       |
| Excess tax benefit related to equity compensation plans  | (2,629 )                                  | (1,871 )     |
| Other changes, net   | (24,602 )                                 | (365 )       |
| Net cash provided by operating activities  | 346,167                                   | 278,828      |
| <b>INVESTING ACTIVITIES:</b>   |   |              |
| Proceeds from sales of investment securities (A)   | 7,946                                     | 684,893      |
| Proceeds from maturities/pay downs of investment securities (A)  | 1,659,778                                 | 1,923,785    |
| Purchases of investment securities (A)   | (1,080,003 )                              | (2,507,803 ) |
| Net increase in loans  | (817,886 )                                | (782,559 )   |
| Repayments of long-term securities purchased under agreements to resell  | 150,000                                   | 75,000       |
| Purchases of land, buildings and equipment   | (18,479 )                                 | (22,718 )    |
| Sales of land, buildings and equipment   | 5,831                                     | 4,752        |
| Net cash used in investing activities  | (92,813 )                                 | (624,650 )   |
| <b>FINANCING ACTIVITIES:</b>   |   |              |
| Net increase (decrease) in non-interest bearing, savings, interest checking and money market deposits            | 280,495                                   | (319,853 )   |
| Net increase (decrease) in time open and C.D.'s  | 14,510                                    | (130,591 )   |
| Net increase (decrease) in federal funds purchased and short-term securities sold under agreements to repurchase | (473,661 )                                | 330,679      |
| Repayment of long-term borrowings  | (3,872 )                                  | (227 )       |
| Additional long-term borrowings  | 1,469                                     | —            |
| Purchases of treasury stock  | (38,476 )                                 | (9,147 )     |
| Accelerated share repurchase agreements  | —   | (100,000 )   |
| Issuance of stock under equity compensation plans  | (3 )                                      | 1,914        |
| Excess tax benefit related to equity compensation plans  | 2,629                                     | 1,871        |
| Cash dividends paid on common stock  | (65,294 )                                 | (64,041 )    |
| Cash dividends paid on preferred stock   | (6,750 )                                  | (6,750 )     |
| Net cash used in financing activities  | (288,953 )                                | (296,145 )   |

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|  |           |            |
|--|-----------|------------|
| Decrease in cash and cash equivalents  | (35,599 ) | (641,967 ) |
| Cash and cash equivalents at beginning of year                                     | 502,719   | 1,100,717  |
| Cash and cash equivalents at September 30  | \$467,120 | \$458,750  |
| (A) Available for sale and non-marketable securities                               |           |            |
| Income tax payments, net   | \$88,531  | \$70,860   |
| Interest paid on deposits and borrowings   | \$24,438  | \$20,937   |
| Loans transferred to foreclosed real estate  | \$1,031   | \$2,459    |
| Loans transferred from held for investment to held for sale, net                   | \$42,688  | \$—        |
| Settlement of accelerated stock repurchase agreement and receipt of treasury stock | \$—       | \$60,000   |
| See accompanying notes to consolidated financial statements.                       |           |            |

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Commerce Bancshares, Inc. and Subsidiaries

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2016 (Unaudited)

## 1. Principles of Consolidation and Presentation

The accompanying consolidated financial statements include the accounts of Commerce Bancshares, Inc. and all majority-owned subsidiaries (the Company). Most of the Company's operations are conducted by its subsidiary bank, Commerce Bank (the Bank). The consolidated financial statements in this report have not been audited by an independent registered public accounting firm, but in the opinion of management, all adjustments necessary to present fairly the financial position and the results of operations for the interim periods have been made. All such adjustments are of a normal recurring nature. All significant intercompany accounts and transactions have been eliminated. Certain reclassifications were made to 2015 data to conform to current year presentation. In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and revenues and expenses for the period. Actual results could differ significantly from those estimates. Management has evaluated subsequent events for potential recognition or disclosure. The results of operations for the three and nine month periods ended September 30, 2016 are not necessarily indicative of results to be attained for the full year or any other interim period.

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

## 2. Loans and Allowance for Loan Losses

Major classifications within the Company's held for investment loan portfolio at September 30, 2016 and December 31, 2015 are as follows:

| (In thousands)                      | September 30,<br>2016 | December 31,<br>2015 |
|-------------------------------------|-----------------------|----------------------|
| Commercial:                         |                       |                      |
| Business                            | \$ 4,770,883          | \$ 4,397,893         |
| Real estate – construction and land | 800,545               | 624,070              |
| Real estate – business              | 2,520,528             | 2,355,544            |
| Personal Banking:                   |                       |                      |
| Real estate – personal              | 1,968,005             | 1,915,953            |
| Consumer                            | 1,972,969             | 1,924,365            |
| Revolving home equity               | 417,591               | 432,981              |
| Consumer credit card                | 760,022               | 779,744              |
| Overdrafts                          | 19,698                | 6,142                |
| Total loans                         | \$ 13,230,241         | \$ 12,436,692        |

At September 30, 2016, loans of \$3.6 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 \$1.6 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 nine months ended September 30, 2016 and 2015, respectively, follows:

| (In thousands)                    | For the Three Months Ended September 30 |                  |           | For the Nine Months Ended September 30 |                  |           |
|-----------------------------------|---|------------------|-----------|--|------------------|-----------|
|                                   | Commercial                              | Personal Banking | Total     | Commercial                             | Personal Banking | Total     |
| Balance at beginning of period    | \$89,198                                | \$64,634         | \$153,832 | \$82,086                               | \$69,446         | \$151,532 |
| Provision                         | (1,411)                                 | 8,674            | 7,263     | 4,309                                  | 21,609           | 25,918    |
| Deductions:                       |   |                  |           |  |                  |           |
| Loans charged off                 | 291                                     | 11,872           | 12,163    | 2,465                                  | 35,633           | 38,098    |
| Less recoveries on loans          | 2,759                                   | 2,841            | 5,600     | 6,325                                  | 8,855            | 15,180    |
| Net loan charge-offs (recoveries) | (2,468)                                 | 9,031            | 6,563     | (3,860)                                | 26,778           | 22,918    |
| Balance September 30, 2016        | \$90,255                                | \$64,277         | \$154,532 | \$90,255                               | \$64,277         | \$154,532 |
| Balance at beginning of period    | \$86,329                                | \$65,203         | \$151,532 | \$89,622                               | \$66,910         | \$156,532 |
| Provision                         | (1,976)                                 | 10,340           | 8,364     | (6,089)                                | 25,630           | 19,541    |
| Deductions:                       |   |                  |           |  |                  |           |
| Loans charged off                 | 903                                     | 11,321           | 12,224    | 3,035                                  | 34,194           | 37,229    |
| Less recoveries on loans          | 1,167                                   | 2,693            | 3,860     | 4,119                                  | 8,569            | 12,688    |
| Net loan charge-offs (recoveries) | (264)                                   | 8,628            | 8,364     | (1,084)                                | 25,625           | 24,541    |
| Balance September 30, 2015        | \$84,617                                | \$66,915         | \$151,532 | \$84,617                               | \$66,915         | \$151,532 |

The following table shows the balance in the allowance for loan losses and the related loan balance at September 30, 2016 and December 31, 2015, 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      | Outstanding | Allowance       | Outstanding |

|                    | Loan<br>Losses   | Losses    |              |  |
|--------------------|------------------|-----------|--------------|--|
| September 30, 2016 |                  |           |              |  |
| Commercial         | \$1,816\$ 44,526 | \$88,439  | \$8,047,430  |  |
| Personal Banking   | 1,253 20,594     | 63,024    | 5,117,691    |  |
| Total              | \$3,069\$ 65,120 | \$151,463 | \$13,165,121 |  |
| December 31, 2015  |                  |           |              |  |
| Commercial         | \$1,927\$ 43,027 | \$80,159  | \$7,334,480  |  |
| Personal Banking   | 1,557 22,287     | 67,889    | 5,036,898    |  |
| Total              | \$3,484\$ 65,314 | \$148,048 | \$12,371,378 |  |

#### Impaired loans

The table below shows the Company's investment in impaired loans at September 30, 2016 and December 31, 2015. These loans consist of all loans on non-accrual status and other restructured loans whose terms have been modified and classified as troubled debt restructurings. These restructured loans are performing in accordance with their modified terms, and because the Company believes it probable that all amounts due under the modified terms of the agreements will be collected, interest on these loans is being recognized on an accrual basis. They are discussed further in the "Troubled debt restructurings" section on page 14.

| (In thousands)                | Sept.<br>30,<br>2016 | Dec. 31,<br>2015 |
|-------------------------------|----------------------|------------------|
| Non-accrual loans             | \$15,645             | \$26,575         |
| Restructured loans (accruing) | 49,475               | 38,739           |
| Total impaired loans          | \$65,120             | \$65,314         |



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The following table provides additional information about impaired loans held by the Company at September 30, 2016 and December 31, 2015, 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 |
|-------------------------------------|------------------------|--------------------------------|----------------------|
| September 30, 2016                  |                        |                                |                      |
| With no related allowance recorded: |                        |                                |                      |
| Business                            | \$ 7,053               | \$ 10,018                      | \$ —                 |
| Real estate – construction and land | 1,228                  | 1,594                          | —                    |
|                                     | \$ 8,281               | \$ 11,612                      | \$ —                 |
| With an allowance recorded:         |                        |                                |                      |
| Business                            | \$ 28,369              | \$ 30,171                      | \$ 1,284             |
| Real estate – construction and land | 214                    | 219                            | 18                   |
| Real estate – business              | 7,662                  | 9,077                          | 514                  |
| Real estate – personal              | 6,703                  | 9,564                          | 602                  |
| Consumer                            | 5,537                  | 5,537                          | 66                   |
| Revolving home equity               | 636                    | 646                            | 18                   |
| Consumer credit card                | 7,718                  | 7,718                          | 567                  |
|                                     | \$ 56,839              | \$ 62,932                      | \$ 3,069             |
| Total                               | \$ 65,120              | \$ 74,544                      | \$ 3,069             |
| December 31, 2015                   |                        |                                |                      |
| With no related allowance recorded: |                        |                                |                      |
| Business                            | \$ 9,330               | \$ 11,777                      | \$ —                 |
| Real estate – construction and land | 2,961                  | 8,956                          | —                    |
| Real estate – business              | 4,793                  | 6,264                          | —                    |
| Real estate – personal              | 373                    | 373                            | —                    |
|                                     | \$ 17,457              | \$ 27,370                      | \$ —                 |
| With an allowance recorded:         |                        |                                |                      |
| Business                            | \$ 18,227              | \$ 20,031                      | \$ 1,119             |
| Real estate – construction and land | 1,227                  | 2,804                          | 63                   |
| Real estate – business              | 6,489                  | 9,008                          | 745                  |
| Real estate – personal              | 7,667                  | 10,530                         | 831                  |
| Consumer                            | 5,599                  | 5,599                          | 63                   |
| Revolving home equity               | 704                    | 852                            | 67                   |
| Consumer credit card                | 7,944                  | 7,944                          | 596                  |
|                                     | \$ 47,857              | \$ 56,768                      | \$ 3,484             |
| Total                               | \$ 65,314              | \$ 84,138                      | \$ 3,484             |

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Total average impaired loans for the three and nine month periods ended September 30, 2016 and 2015, respectively, are shown in the table below.

| (In thousands)                                | Commercial | Personal<br>Banking | Total     |
|---|------------|---------------------|-----------|
| Average Impaired Loans:                       |            |                     |           |
| For the three months ended September 30, 2016 |            |                     |           |
| Non-accrual loans                             | \$ 15,106  | \$ 3,928            | \$ 19,034 |
| Restructured loans (accruing)                 | 31,372     | 17,082              | 48,454    |
| Total   | \$ 46,478  | \$ 21,010           | \$ 67,488 |
| For the nine months ended September 30, 2016  |            |                     |           |
| Non-accrual loans                             | \$ 19,387  | \$ 4,336            | \$ 23,723 |
| Restructured loans (accruing)                 | 29,117     | 17,359              | 46,476    |
| Total   | \$ 48,504  | \$ 21,695           | \$ 70,199 |
| For the three months ended September 30, 2015 |            |                     |           |
| Non-accrual loans                             | \$ 21,119  | \$ 5,179            | \$ 26,298 |
| Restructured loans (accruing)                 | 13,399     | 18,221              | 31,620    |
| Total   | \$ 34,518  | \$ 23,400           | \$ 57,918 |
| For the nine months ended September 30, 2015  |            |                     |           |
| Non-accrual loans                             | \$ 25,784  | \$ 5,791            | \$ 31,575 |
| Restructured loans (accruing)                 | 16,612     | 18,854              | 35,466    |
| Total   | \$ 42,396  | \$ 24,645           | \$ 67,041 |

The table below shows interest income recognized during the three and nine month periods ended September 30, 2016 and 2015, respectively, 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 14.

| (In thousands)                                | For the<br>Three<br>Months<br>Ended<br>September<br>30 |        | For the Nine<br>Months Ended<br>September 30 |          |
|---|--|--------|--|----------|
|   | 2016   | 2015   | 2016   | 2015     |
| Interest income recognized on impaired loans: |  |        |  |          |
| Business                                      | \$ 277   | \$ 63  | \$ 830                                       | \$ 188   |
| Real estate – construction and land           | 2  | 22     | 7  | 66       |
| Real estate – business                        | 42   | 33     | 126  | 99       |
| Real estate – personal                        | 39   | 47     | 118  | 142      |
| Consumer                                      | 89   | 87     | 267  | 261      |
| Revolving home equity                         | 7  | 6      | 22   | 17       |
| Consumer credit card                          | 174  | 186    | 522  | 558      |
| Total   | \$ 630   | \$ 444 | \$ 1,892                                     | \$ 1,331 |

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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 September 30, 2016 and December 31, 2015.

| (In thousands)                      | Current or<br>Less Than<br>30 Days<br>Past Due | 30 – 89<br>Days<br>Past<br>Due | 90 Days<br>Past Due<br>and Still<br>Accruing | Non-accrual | Total        |
|-------------------------------------|--|--------------------------------|--|-------------|--------------|
| September 30, 2016                  |  |                                |  |             |              |
| Commercial:                         |  |                                |  |             |              |
| Business                            | \$4,758,519                                    | \$3,100                        | \$ 506                                       | \$ 8,758    | \$4,770,883  |
| Real estate – construction and land | 794,731  | 2,357                          | 2,147  | 1,310       | 800,545      |
| Real estate – business              | 2,513,270                                      | 5,011                          | 327  | 1,920       | 2,520,528    |
| Personal Banking:                   |  |                                |  |             |              |
| Real estate – personal              | 1,954,889                                      | 6,901                          | 2,581  | 3,634       | 1,968,005    |
| Consumer                            | 1,951,011                                      | 19,510                         | 2,448  | —           | 1,972,969    |
| Revolving home equity               | 414,251  | 2,246                          | 1,071  | 23          | 417,591      |
| Consumer credit card                | 742,820  | 9,366                          | 7,836  | —           | 760,022      |
| Overdrafts                          | 19,254   | 444                            | —  | —           | 19,698       |
| Total                               | \$13,148,745                                   | \$48,935                       | \$ 16,916                                    | \$ 15,645   | \$13,230,241 |
| December 31, 2015                   |  |                                |  |             |              |
| Commercial:                         |  |                                |  |             |              |
| Business                            | \$4,384,149                                    | \$2,306                        | \$ 564                                       | \$ 10,874   | \$4,397,893  |
| Real estate – construction and land | 617,838  | 3,142                          | —  | 3,090       | 624,070      |
| Real estate – business              | 2,340,919                                      | 6,762                          | —  | 7,863       | 2,355,544    |
| Personal Banking:                   |  |                                |  |             |              |
| Real estate – personal              | 1,901,330                                      | 7,117                          | 3,081  | 4,425       | 1,915,953    |
| Consumer                            | 1,903,389                                      | 18,273                         | 2,703  | —           | 1,924,365    |
| Revolving home equity               | 427,998  | 2,641                          | 2,019  | 323         | 432,981      |
| Consumer credit card                | 762,750  | 8,894                          | 8,100  | —           | 779,744      |
| Overdrafts                          | 5,834  | 308                            | —  | —           | 6,142        |
| Total                               | \$12,344,207                                   | \$49,443                       | \$ 16,467                                    | \$ 26,575   | \$12,436,692 |

## 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<br>Estate-Construction | Real<br>Estate-<br>Business | Total       |
|--------------------|-------------|-----------------------------|-----------------------------|-------------|
| September 30, 2016 |             |                             |                             |             |
| Pass               | \$4,625,175 | \$ 798,168                  | \$2,421,327                 | \$7,844,670 |
| Special mention    | 76,105      | 860                         | 46,281                      | 123,246     |
| Substandard        | 60,845      | 207                         | 51,000                      | 112,052     |
| Non-accrual        | 8,758       | 1,310                       | 1,920                       | 11,988      |
| Total              | \$4,770,883 | \$ 800,545                  | \$2,520,528                 | \$8,091,956 |
| December 31, 2015  |             |                             |                             |             |
| Pass               | \$4,278,857 | \$ 618,788                  | \$2,281,565                 | \$7,179,210 |
| Special mention    | 49,302      | 1,033                       | 15,009                      | 65,344      |
| Substandard        | 58,860      | 1,159                       | 51,107                      | 111,126     |
| Non-accrual        | 10,874      | 3,090                       | 7,863                       | 21,827      |
| Total              | \$4,397,893 | \$ 624,070                  | \$2,355,544                 | \$7,377,507 |

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 September 30, 2016, these were comprised of \$251.7 million in personal real estate loans, or 4.9% of the Personal Banking portfolio, compared to \$257.8 million at December 31, 2015. For the remainder of loans in the Personal Banking portfolio, the table below shows the percentage of balances outstanding at September 30, 2016 and December 31, 2015 by FICO score.

## Personal Banking Loans

|                    | % of Loan Category           |                            |           |                            |
|--------------------|------------------------------|----------------------------|-----------|----------------------------|
|                    | Real<br>Estate -<br>Personal | Consumer<br>Home<br>Equity | Revolving | Consumer<br>Credit<br>Card |
| September 30, 2016 |                              |                            |           |                            |
| FICO score:        |                              |                            |           |                            |
| Under 600          | 1.4                          | %4.2                       | % 1.2     | % 4.0                      |
| 600 - 659          | 3.0                          | 8.5                        | 3.8       | 11.9                       |
| 660 - 719          | 10.3                         | 21.0                       | 13.2      | 31.4                       |
| 720 - 779          | 24.8                         | 26.5                       | 28.1      | 28.4                       |
| 780 and over       | 60.5                         | 39.8                       | 53.7      | 24.3                       |
| Total              | 100.0%                       | 100.0                      | % 100.0   | % 100.0                    |
| December 31, 2015  |                              |                            |           |                            |
| FICO score:        |                              |                            |           |                            |
| Under 600          | 1.5                          | %4.5                       | % 1.5     | % 3.9                      |
| 600 - 659          | 3.0                          | 9.7                        | 3.9       | 12.0                       |
| 660 - 719          | 9.1                          | 21.8                       | 13.6      | 31.7                       |
| 720 - 779          | 25.0                         | 26.4                       | 28.4      | 27.9                       |
| 780 and over       | 61.4                         | 37.6                       | 52.6      | 24.5                       |

Total 100.0% 100.0 % 100.0 % 100.0 %

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## Troubled debt restructurings

As mentioned previously, the Company's impaired loans include loans which have been classified as troubled debt restructurings. Total restructured loans amounted to \$59.0 million at September 30, 2016. 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 \$9.6 million at September 30, 2016. Other performing restructured loans totaled \$49.5 million at September 30, 2016. These include certain business, construction and business real estate loans classified as substandard. Upon maturity, the loans renewed at interest rates judged not to be market rates for new debt with similar risk and as a result the loans were classified as troubled debt restructurings. These commercial loans totaled \$33.2 million at September 30, 2016. 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 \$7.7 million at September 30, 2016. 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 September 30, 2016, these loans totaled \$8.2 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 September 30, 2016, 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)                      | September 30,<br>2016 | Balance<br>90 days<br>past due<br>at any<br>time<br>during<br>previous<br>12<br>months |
|-------------------------------------|-----------------------|--|
| Commercial:                         |                       |  |
| Business                            | \$ 34,227             | \$ —   |
| Real estate - construction and land | 784                   | 676  |
| Real estate - business              | 5,742                 | 751  |
| Personal Banking:                   |                       |  |
| Real estate - personal              | 4,387                 | 358  |
| Consumer                            | 5,560                 | 62   |
| Revolving home equity               | 613                   | 67   |
| Consumer credit card                | 7,718                 | 537  |
| Total restructured loans            | \$ 59,031             | \$ 2,451   |

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 \$926 thousand on an annual, pre-tax basis, compared to amounts contractually owed.

The allowance for loan losses related to troubled debt restructurings on non-accrual status is determined by individual evaluation, including collateral adequacy, using the same process as loans on non-accrual status which are not classified as troubled debt restructurings. Those performing loans classified as troubled debt restructurings are accruing loans which management expects to collect under contractual terms. Performing commercial loans have had no other concessions granted other than being renewed at an interest rate judged not to be market. As such, they have similar risk characteristics as non-troubled debt commercial loans and are collectively evaluated based on internal risk rating, loan type, delinquency, historical experience and current economic factors. Performing personal banking loans classified as troubled debt restructurings resulted from the borrower not reaffirming the debt during bankruptcy and have had no other concession granted, other than the Bank's future limitations on collecting payment deficiencies or in pursuing foreclosure actions. As such, they have similar risk characteristics as non-troubled debt personal banking loans and are evaluated collectively based on loan type, delinquency, historical experience and current economic factors.

If a troubled debt restructuring defaults and is already on non-accrual status, the allowance for loan losses continues to be based on individual evaluation, using discounted expected cash flows or the fair value of collateral. If an accruing troubled debt



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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 \$11.5 million at September 30, 2016 to lend additional funds to borrowers with restructured loans.

**Loans held for sale**

Beginning January 1, 2015, certain long-term fixed rate personal real estate loan originations have been designated as held for sale, and the Company has elected the fair value option for these loans. The election of the fair value option aligns the accounting for these loans with the related economic hedges discussed in Note 10. At September 30, 2016, the fair value of these loans was \$4.4 million, and the unpaid principal balance was \$4.3 million.

Beginning in the third quarter of 2015, the Company has designated certain student loan originations as held for sale. The borrowers are credit-worthy students who are attending colleges and universities. The loans are intended to be sold in the secondary market, and the Company maintains contracts with Sallie Mae to sell the loans at various times while the student is attending school or shortly after graduation. At September 30, 2016, the balance of these loans was \$5.1 million. These loans are carried at lower of cost or fair value.

In March 2016, the Company designated certain loans secured by automobiles as held for sale in order to rebalance the auto loan portfolio in relation to the Company's other loan categories. The loans were sold in the second and third quarters and totaled \$33.6 million, resulting in a net gain of \$56 thousand. The group of loans were representative of the overall auto loan portfolio and were sold to other financial institutions.

At September 30, 2016, none of the loans held for sale were on non-accrual status or 90 days past due and still accruing. Interest income with respect to loans held for sale is accrued based on the principal amount outstanding and the loan's contractual interest rate. Gains and losses in fair value resulting from the application of the fair value option, or lower of cost or fair value accounting, are recognized in loan fees and sales in the consolidated statements of income.

**Foreclosed real estate/repossessed assets**

The Company's holdings of foreclosed real estate totaled \$950 thousand and \$2.8 million at September 30, 2016 and December 31, 2015, respectively. Personal property acquired in repossession, generally autos and marine and recreational vehicles, totaled \$2.5 million and \$3.3 million at September 30, 2016 and December 31, 2015, respectively. Upon acquisition, these assets are recorded at fair value less estimated selling costs at the date of foreclosure, establishing a new cost basis. They are subsequently carried at the lower of this cost basis or fair value less estimated selling costs.

**3. Investment Securities**

Investment securities, at fair value, consisted of the following at September 30, 2016 and December 31, 2015.

|                             | Sept. 30,<br>2016 | Dec. 31,<br>2015 |
|-----------------------------|-------------------|------------------|
| (In thousands)              |                   |                  |
| Available for sale          | \$9,438,871       | \$9,777,004      |
| Trading                     | 28,586            | 11,890           |
| Non-marketable              | 108,224           | 112,786          |
| Total investment securities | \$9,575,681       | \$9,901,680      |

Most of the Company's investment securities are classified as available for sale, and this portfolio is discussed in more detail below. The available for sale and the trading portfolios are carried at fair value. 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 \$46.9 million at September 30, 2016 and \$46.8 million at December 31, 2015. 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. These holdings are carried at cost. Non-marketable securities also include private equity investments, which amounted to \$61.0 million at September 30, 2016 and \$65.6 million at December 31, 2015. In the absence of readily ascertainable market values, these securities are carried at estimated fair value.

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A summary of the available for sale investment securities by maturity groupings as of September 30, 2016 is shown below. The investment portfolio includes agency mortgage-backed securities, which are guaranteed by agencies such as the FHLMC, FNMA, GNMA and FDIC, in addition to non-agency mortgage-backed securities, which have no guarantee but are collateralized by residential mortgages. Also included are certain other asset-backed securities, which are primarily collateralized by credit cards, automobiles, student loans, and commercial loans. These securities differ from traditional debt securities primarily in that they may have uncertain maturity dates and are priced based on estimated prepayment rates on the underlying collateral.

| (In thousands)                                       | Amortized<br>Cost | Fair Value  |
|--|-------------------|-------------|
| U.S. government and federal agency obligations:      |                   |             |
| Within 1 year  | \$59,068          | \$60,028    |
| After 1 but within 5 years                           | 500,823           | 514,620     |
| After 5 but within 10 years                          | 106,427           | 110,802     |
| After 10 years                                       | 72,340            | 70,199      |
| Total U.S. government and federal agency obligations | 738,658           | 755,649     |
| Government-sponsored enterprise obligations:         |                   |             |
| Within 1 year  | 11,589            | 11,627      |
| After 1 but within 5 years                           | 419,071           | 424,410     |
| After 5 but within 10 years                          | 14,988            | 15,205      |
| Total government-sponsored enterprise obligations    | 445,648           | 451,242     |
| State and municipal obligations:                     |                   |             |
| Within 1 year  | 153,968           | 155,078     |
| After 1 but within 5 years                           | 626,147           | 641,498     |
| After 5 but within 10 years                          | 941,494           | 983,236     |
| After 10 years                                       | 55,248            | 56,189      |
| Total state and municipal obligations                | 1,776,857         | 1,836,001   |
| Mortgage and asset-backed securities:                |                   |             |
| Agency mortgage-backed securities                    | 2,590,902         | 2,663,677   |
| Non-agency mortgage-backed securities                | 922,302           | 937,208     |
| Asset-backed securities                              | 2,403,019         | 2,409,324   |
| Total mortgage and asset-backed securities           | 5,916,223         | 6,010,209   |
| Other debt securities:                               |                   |             |
| Within 1 year  | 5,997             | 6,025       |
| After 1 but within 5 years                           | 97,136            | 98,939      |
| After 5 but within 10 years                          | 214,311           | 222,376     |
| After 10 years                                       | 11,588            | 11,472      |
| Total other debt securities                          | 329,032           | 338,812     |
| Equity securities                                    | 5,678             | 46,958      |
| Total available for sale investment securities       | \$9,212,096       | \$9,438,871 |

Investments in U.S. government and federal agency obligations include U.S. Treasury inflation-protected securities, which totaled \$437.9 million, at fair value, at September 30, 2016. Interest paid on these securities increases with inflation and decreases with deflation, as measured by the Consumer Price Index. Included in equity securities is common and preferred stock held by the holding company, Commerce Bancshares, Inc. (the Parent), with a fair value of \$46.9 million at September 30, 2016.



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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   |
|--|-------------------|------------------------------|-------------------------------|--------------|
| September 30, 2016                             |                   |                              |                               |              |
| U.S. government and federal agency obligations | \$738,658         | \$ 19,132                    | \$(2,141)                     | )\$755,649   |
| Government-sponsored enterprise obligations    | 445,648           | 5,637                        | (43)                          | )451,242     |
| State and municipal obligations                | 1,776,857         | 59,760                       | (616)                         | )1,836,001   |
| Mortgage and asset-backed securities:          |                   |                              |                               |              |
| Agency mortgage-backed securities              | 2,590,902         | 72,803                       | (28)                          | )2,663,677   |
| Non-agency mortgage-backed securities          | 922,302           | 15,145                       | (239)                         | )937,208     |
| Asset-backed securities                        | 2,403,019         | 14,026                       | (7,721)                       | )2,409,324   |
| Total mortgage and asset-backed securities     | 5,916,223         | 101,974                      | (7,988)                       | )6,010,209   |
| Other debt securities                          | 329,032           | 9,946                        | (166)                         | )338,812     |
| Equity securities                              | 5,678             | 41,280                       | —                             | 46,958       |
| Total  | \$9,212,096       | \$237,729                    | \$(10,954)                    | )\$9,438,871 |
| December 31, 2015                              |                   |                              |                               |              |
| U.S. government and federal agency obligations | \$729,846         | \$ 5,051                     | \$(7,821)                     | )\$727,076   |
| Government-sponsored enterprise obligations    | 794,912           | 2,657                        | (4,546)                       | )793,023     |
| State and municipal obligations                | 1,706,635         | 37,061                       | (1,739)                       | )1,741,957   |
| Mortgage and asset-backed securities:          |                   |                              |                               |              |
| Agency mortgage-backed securities              | 2,579,031         | 47,856                       | (8,606)                       | )2,618,281   |
| Non-agency mortgage-backed securities          | 879,186           | 8,596                        | (7,819)                       | )879,963     |
| Asset-backed securities                        | 2,660,201         | 1,287                        | (17,107)                      | )2,644,381   |
| Total mortgage and asset-backed securities     | 6,118,418         | 57,739                       | (33,532)                      | )6,142,625   |
| Other debt securities                          | 335,925           | 377                          | (4,982)                       | )331,320     |
| Equity securities                              | 5,678             | 35,325                       | —                             | 41,003       |
| Total  | \$9,691,414       | \$138,210                    | \$(52,620)                    | )\$9,777,004 |

The Company's impairment policy requires a review of all securities for which fair value is less than amortized cost. Special emphasis and analysis is placed on securities whose credit rating has fallen below A3 (Moody's) or A- (Standard & Poor's), whose fair values have fallen more than 20% below purchase price for an extended period of time, or have been identified based on management's judgment. These securities are placed on a watch list, and for all such securities, cash flow analyses are prepared. For more complex analyses, detailed cash flow models are prepared which use inputs specific to each security. Inputs to these models include factors such as cash flow received, contractual payments required, and various other information related to the underlying collateral (including current delinquencies), collateral loss severity rates (including loan to values), expected delinquency rates, credit support from other tranches, and prepayment speeds. Stress tests are performed at varying levels of delinquency rates, prepayment speeds and loss severities in order to gauge probable ranges of credit loss. At September 30, 2016, the fair value of securities on this watch list was \$103.7 million compared to \$95.8 million at December 31, 2015.

As of September 30, 2016, 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 \$34.6 million. The cumulative credit-related portion of the impairment on these securities, which was recorded in earnings, totaled \$14.2 million. The Company does not intend to sell these securities and believes it is not likely that it will be required to sell the securities before the recovery of their amortized cost.

The credit-related portion of the loss on these securities was based on the cash flows projected to be received over the estimated life of the securities, discounted to present value, and compared to the current amortized cost bases of the securities. Significant inputs to the cash flow models used to calculate the credit losses on these securities at September 30, 2016 included the following:

| Significant Inputs           | Range   |
|------------------------------|---------|
| Prepayment CPR               | 0% -25% |
| Projected cumulative default | 18%-51% |
| Credit support               | 0% -30% |
| Loss severity                | 17%-63% |

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

| (In thousands)  | For the Nine<br>Months Ended<br>September 30 |           |
|---|--|-----------|
|   | 2016   | 2015      |
| Cumulative OTTI credit losses at January 1  | \$ 14,129                                    | \$ 13,734 |
| Credit losses on debt securities for which impairment was not previously recognized | —  | 76        |
| Credit losses on debt securities for which impairment was previously recognized     | 270  | 407       |
| Increase in expected cash flows that are recognized over remaining life of security | (171)  | (73)      |
| Cumulative OTTI credit losses at September 30                                       | \$ 14,228                                    | \$ 14,144 |

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<br>Fair Value | Unrealized<br>Losses |
|--|---------------------|----------------------|---------------------|----------------------|---------------------|----------------------|
|  | Fair<br>Value       | Unrealized<br>Losses | Fair<br>Value       | Unrealized<br>Losses |                     |                      |
| September 30, 2016                             |                     |                      |                     |                      |                     |                      |
| U.S. government and federal agency obligations | \$ 36,586           | \$ 61                | \$ 33,613           | \$ 2,080             | \$ 70,199           | \$ 2,141             |
| Government-sponsored enterprise obligations    | 49,901              | 43                   | —                   | —                    | 49,901              | 43                   |
| State and municipal obligations                | 26,335              | 227                  | 16,276              | 389                  | 42,611              | 616                  |
| Mortgage and asset-backed securities:          |                     |                      |                     |                      |                     |                      |
| Agency mortgage-backed securities              | 24,564              | 23                   | 2,304               | 5                    | 26,868              | 28                   |
| Non-agency mortgage-backed securities          | 61,283              | 127                  | 39,070              | 112                  | 100,353             | 239                  |
| Asset-backed securities                        | 279,282             | 1,510                | 365,402             | 6,211                | 644,684             | 7,721                |
| Total mortgage and asset-backed securities     | 365,129             | 1,660                | 406,776             | 6,328                | 771,905             | 7,988                |
| Other debt securities                          | 7,936               | 36                   | 12,458              | 130                  | 20,394              | 166                  |
| Total  | \$ 485,887          | \$ 2,027             | \$ 469,123          | \$ 8,927             | \$ 955,010          | \$ 10,954            |
| December 31, 2015                              |                     |                      |                     |                      |                     |                      |
| U.S. government and federal agency obligations | \$ 491,998          | \$ 3,098             | \$ 31,012           | \$ 4,723             | \$ 523,010          | \$ 7,821             |
| Government-sponsored enterprise obligations    | 157,830             | 1,975                | 110,250             | 2,571                | 268,080             | 4,546                |
| State and municipal obligations                | 66,998              | 544                  | 31,120              | 1,195                | 98,118              | 1,739                |
| Mortgage and asset-backed securities:          |                     |                      |                     |                      |                     |                      |
| Agency mortgage-backed securities              | 530,035             | 2,989                | 291,902             | 5,617                | 821,937             | 8,606                |
| Non-agency mortgage-backed securities          | 653,603             | 7,059                | 54,536              | 760                  | 708,139             | 7,819                |
| Asset-backed securities                        | 2,207,922           | 12,492               | 223,311             | 4,615                | 2,431,233           | 17,107               |
| Total mortgage and asset-backed securities     | 3,391,560           | 22,540               | 569,749             | 10,992               | 3,961,309           | 33,532               |
| Other debt securities                          | 244,452             | 3,687                | 25,218              | 1,295                | 269,670             | 4,982                |
| Total  | \$ 4,352,838        | \$ 31,844            | \$ 767,349          | \$ 20,776            | \$ 5,120,187        | \$ 52,620            |

The total available for sale portfolio consisted of approximately 2,000 individual securities at September 30, 2016. The portfolio included 152 securities, having an aggregate fair value of \$955.0 million, that were in an unrealized loss position at September 30, 2016, compared to 466 securities, with a fair value of \$5.1 billion, at December 31, 2015. The total amount of unrealized losses on these securities decreased \$41.7 million to \$11.0 million at September 30, 2016, largely due to a lower rate environment. At September 30, 2016, the fair value of securities in an unrealized loss position for 12 months or longer totaled \$469.1 million, or 5.0% of the total portfolio value.

The Company's holdings of state and municipal obligations included gross unrealized losses of \$616 thousand at September 30, 2016, of which \$378 thousand related to auction rate securities. This portfolio totaled \$1.8 billion at fair value, or 19.5% of total available for sale securities. The average credit quality of the portfolio, excluding auction rate securities, is Aa2 as rated by Moody's. The portfolio is diversified in order to reduce risk, and 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.



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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 Nine<br>Months Ended<br>September 30 |           |
|---|--|-----------|
|   | 2016   | 2015      |
| Proceeds from sales of available for sale securities          | \$—  | \$675,870 |
| Proceeds from sales of non-marketable securities              | 7,946  | 9,023     |
| Total proceeds  | \$7,946                                      | \$684,893 |
| Available for sale:   |  |           |
| Gains realized on sales                                       | \$—  | \$2,813   |
| Other-than-temporary impairment recognized on debt securities | (270)  | (483)     |
| Non-marketable:   |  |           |
| Gains realized on sales                                       | 3,717  | 2,516     |
| Losses realized on sales                                      | (502)  | —         |
| Fair value adjustments, net                                   | (6,649)                                      | 2,954     |
| Investment securities gains (losses), net                     | \$(3,704)                                    | \$7,800   |

At September 30, 2016, securities totaling \$4.0 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 \$578.1 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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## 4. Goodwill and Other Intangible Assets

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

| (In thousands)                 | September 30, 2016    |                          |                     |            | December 31, 2015     |                          |                     |            |
|--------------------------------|-----------------------|--------------------------|---------------------|------------|-----------------------|--------------------------|---------------------|------------|
|                                | Gross Carrying Amount | Accumulated Amortization | Valuation Allowance | Net Amount | Gross Carrying Amount | Accumulated Amortization | Valuation Allowance | Net Amount |
| Amortizable intangible assets: |                       |                          |                     |            |                       |                          |                     |            |
| Core deposit premium           | \$31,270              | \$(27,182)               | \$ —                | \$ 4,088   | \$31,270              | \$(26,239)               | \$ —                | \$ 5,031   |
| Mortgage servicing rights      | 5,260                 | (2,691)                  | (36)                | 2,533      | 4,638                 | (2,971)                  | (29)                | 1,638      |
| Total                          | \$36,530              | \$(29,873)               | \$(36)              | \$ 6,621   | \$35,908              | \$(29,210)               | \$(29)              | \$ 6,669   |

Aggregate amortization expense on intangible assets was \$374 thousand and \$445 thousand for the three month periods ended September 30, 2016 and 2015, respectively, and \$1.2 million and \$1.4 million for the nine month periods ended September 30, 2016 and 2015, respectively. 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 September 30, 2016. 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) |         |
|----------------|---------|
| 2016           | \$1,584 |
| 2017           | 1,210   |
| 2018           | 931     |
| 2019           | 770     |
| 2020           | 630     |

Changes in the carrying amount of goodwill and net other intangible assets for the nine month period ended September 30, 2016 is as follows:

| (In thousands)             | Goodwill  | Core Deposit Premium | Mortgage Servicing Rights |
|----------------------------|-----------|----------------------|---------------------------|
| Balance January 1, 2016    | \$138,921 | \$5,031              | \$1,638                   |
| Originations               | —         | —                    | 1,127                     |
| Amortization               | —         | (943)                | (225)                     |
| Impairment                 | —         | —                    | (7)                       |
| Balance September 30, 2016 | \$138,921 | \$4,088              | \$2,533                   |

Goodwill allocated to the Company's operating segments at September 30, 2016 and December 31, 2015 is shown below.

| (In thousands)     |           |
|--------------------|-----------|
| Consumer segment   | \$70,721  |
| Commercial segment | 67,454    |
| Wealth segment     | 746       |
| Total goodwill     | \$138,921 |

## 5. 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 September 30, 2016, that net liability was \$2.4 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 \$352.1 million at September 30, 2016.

The Company periodically enters into credit 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 September 30, 2016, 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 3 to 11 years. At September 30, 2016, the fair value of the Company's guarantee liabilities for RPAs was \$272 thousand, and the notional amount of the underlying swaps was \$60.2 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.

## 6. Pension

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

|  | For the<br>Three<br>Months<br>Ended<br>September<br>30 |         | For the Nine<br>Months Ended<br>September 30 |          |
|--|--|---------|--|----------|
| (In thousands)                                   | 2016   | 2015    | 2016   | 2015     |
| Service cost - benefits earned during the period | \$ 135   | \$ 127  | \$ 406                                       | \$ 379   |
| Interest cost on projected benefit obligation    | 986  | 1,139   | 2,958  | 3,571    |
| Expected return on plan assets                   | (1,437)  | (1,523) | (4,313)                                      | (4,569)  |
| Amortization of prior service cost               | (68)   | (203)   | (203)  | (203)    |
| Amortization of unrecognized net loss            | 647  | 660     | 1,940  | 1,969    |
| Net periodic pension cost                        | \$ 263   | \$ 200  | \$ 788                                       | \$ 1,147 |

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 the first nine months of 2016, the Company made no funding contributions to its defined benefit pension plan and 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 2016.

Effective January 1, 2016, the Company changed the method used to estimate the interest cost component of net periodic pension cost for its defined benefit pension plan. Prior to the change, the interest cost component was estimated by utilizing a single weighted average discount rate derived from the yield curve used to measure the projected benefit obligation. Under the new method, the interest cost component is estimated by applying the specific annual spot rates along the yield curve used in the determination of the projected benefit obligation to the relevant

projected cash flows. This change provides a more precise measurement of the interest cost by improving the correlation between projected benefit cash flows and the corresponding spot yield curve rates. The Company accounted for this change prospectively as a change in accounting estimate. The change resulted in a decrease of approximately \$851 thousand in the estimated annual net periodic pension cost for 2016.

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## 7. Common and Preferred 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 12.

|   | For the Three<br>Months Ended<br>September 30 |          | For the Nine<br>Months Ended<br>September 30 |           |
|---|---|----------|--|-----------|
|   | 2016  | 2015     | 2016   | 2015      |
| (In thousands, except per share data)   |   |          |  |           |
| Basic income per common share:  |   |          |  |           |
| Net income available to common shareholders   | \$66,295                                      | \$62,362 | \$197,062                                    | \$193,270 |
| Less income allocated to nonvested restricted stock   | 913   | 884      | 2,747  | 2,677     |
| Net income allocated to common stock  | \$65,382                                      | \$61,478 | \$194,315                                    | \$190,593 |
| Weighted average common shares outstanding  | 95,426  | 96,589   | 95,458                                       | 98,568    |
| Basic income per common share   | \$.69   | \$.63    | \$2.04                                       | \$1.93    |
| Diluted income per common share:  |   |          |  |           |
| Net income available to common shareholders   | \$66,295                                      | \$62,362 | \$197,062                                    | \$193,270 |
| Less income allocated to nonvested restricted stock   | 912   | 883      | 2,743  | 2,672     |
| Net income allocated to common stock  | \$65,383                                      | \$61,479 | \$194,319                                    | \$190,598 |
| Weighted average common shares outstanding  | 95,426  | 96,589   | 95,458                                       | 98,568    |
| 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 | 243   | 293      | 236  | 315       |
| Weighted average diluted common shares outstanding  | 95,669  | 96,882   | 95,694                                       | 98,883    |
| Diluted income per common share   | \$.68   | \$.63    | \$2.03                                       | \$1.93    |

Unexercised stock options and stock appreciation rights of 84 thousand and 395 thousand were excluded in the computation of diluted income per common share for the nine month periods ended September 30, 2016 and 2015, respectively, because their inclusion would have been anti-dilutive.

The Company also has 6,000,000 depositary shares outstanding, representing 6,000 shares of 6.00% Series B Non-Cumulative Perpetual Preferred Stock, par value \$1.00 per share, having an aggregate liquidation preference of \$150.0 million ("Series B Preferred Stock"). Each depositary share has a liquidation preference of \$25.00 per share. Dividends on the Series B Preferred Stock, if declared, accrue and are payable quarterly, in arrears, at a rate of 6.00%. The Series B Preferred Stock qualifies as Tier 1 capital for the purposes of the regulatory capital calculations. In the event that the Company does not declare and pay dividends on the Series B Preferred Stock for the most recent dividend period, the ability of the Company to declare or pay dividends on, purchase, redeem or otherwise acquire shares of its common stock or any securities of the Company that rank junior to the Series B Preferred Stock is subject to certain restrictions under the terms of the Series B Preferred Stock.

\* All prior year share and per share amounts in this note have been restated for the 5% common stock dividend distributed in December 2015.

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## 8. 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<br>(Losses) on<br>Securities (1) |           | Pension<br>Loss (2) | Total<br>Accumulated<br>Other<br>Comprehensive<br>Income |
|--|---|-----------|---------------------|--|
|  | OTTI  | Other     |                     |  |
| Balance January 1, 2016  | \$3,316   | \$49,750  | \$(20,596)          | \$ 32,470  |
| Other comprehensive income (loss) before reclassifications                                   | (837)   | )141,752  | —                   | 140,915  |
| Amounts reclassified from accumulated other comprehensive income                             | 270   | —         | 1,737               | 2,007  |
| Current period other comprehensive income (loss), before tax                                 | (567)   | )141,752  | 1,737               | 142,922  |
| Income tax (expense) benefit   | 215   | (53,865)  | (660)               | (54,310)   |
| Current period other comprehensive income (loss), net of tax                                 | (352)   | )87,887   | 1,077               | 88,612   |
| Balance September 30, 2016   | \$2,964   | \$137,637 | \$(19,519)          | \$ 121,082   |
| Balance January 1, 2015  | \$3,791   | \$81,310  | \$(23,008)          | \$ 62,093  |
| Other comprehensive income (loss) before reclassifications                                   | (976)   | )7,255    | —                   | 6,279  |
| Amounts reclassified from accumulated other comprehensive income                             | 483   | (2,813)   | )1,766              | (564)  |
| Current period other comprehensive income (loss), before tax                                 | (493)   | )4,442    | 1,766               | 5,715  |
| Income tax (expense) benefit   | 187   | (1,688)   | (671)               | (2,172)  |
| Current period other comprehensive income (loss), net of tax                                 | (306)   | )2,754    | 1,095               | 3,543  |
| Transfer of unrealized gain on securities for which impairment was not previously recognized | 43  | (43)      | )—                  | —  |
| Balance September 30, 2015   | \$3,528   | \$84,021  | \$(21,913)          | \$ 65,636  |

(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 prior service cost" and "amortization of unrecognized net loss" (see Note 6), for inclusion in the consolidated statements of income.

## 9. 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 change are reflected in prior year information presented below.

| (In thousands)                        | Consumer  | Commercial | Wealth   | Segment<br>Totals | Other/Elimination | Consolidated<br>Totals |
|---------------------------------------|-----------|------------|----------|-------------------|-------------------|------------------------|
| Three Months Ended September 30, 2016 |           |            |          |                   |                   |                        |
| Net interest income                   | \$67,375  | \$78,537   | \$10,782 | \$156,694         | \$14,549          | \$171,243              |
| Provision for loan losses             | (9,033)   | 2,432      | (5)      | (6,606)           | (657)             | (7,263)                |
| Non-interest income                   | 34,229    | 49,832     | 36,675   | 120,736           | (1,417)           | 119,319                |
| Investment securities losses, net     | —         | —          | —        | —                 | (1,965)           | (1,965)                |
| Non-interest expense                  | (70,113)  | (71,425)   | (28,185) | (169,723)         | (11,519)          | (181,242)              |
| Income before income taxes            | \$22,458  | \$59,376   | \$19,267 | \$101,101         | \$ (1,009)        | \$100,092              |
| Nine Months Ended September 30, 2016  |           |            |          |                   |                   |                        |
| Net interest income                   | \$201,166 | \$231,552  | \$32,604 | \$465,322         | \$41,525          | \$506,847              |
| Provision for loan losses             | (26,533)  | 3,919      | (120)    | (22,734)          | (3,184)           | (25,918)               |
| Non-interest income                   | 97,165    | 149,240    | 107,696  | 354,101           | 812               | 354,913                |
| Investment securities losses, net     | —         | —          | —        | —                 | (3,704)           | (3,704)                |
| Non-interest expense                  | (209,649) | (211,961)  | (85,025) | (506,635)         | (29,169)          | (535,804)              |
| Income before income taxes            | \$62,149  | \$172,750  | \$55,155 | \$290,054         | \$6,280           | \$296,334              |
| Three Months Ended September 30, 2015 |           |            |          |                   |                   |                        |
| Net interest income                   | \$67,085  | \$74,476   | \$10,427 | \$151,988         | \$10,050          | \$162,038              |
| Provision for loan losses             | (8,605)   | 166        | 106      | (8,333)           | (31)              | (8,364)                |
| Non-interest income                   | 31,099    | 47,486     | 33,980   | 112,565           | (1,277)           | 111,288                |
| Investment securities losses, net     | —         | —          | —        | —                 | (378)             | (378)                  |
| Non-interest expense                  | (69,158)  | (68,713)   | (27,182) | (165,053)         | (6,349)           | (171,402)              |
| Income before income taxes            | \$20,421  | \$53,415   | \$17,331 | \$91,167          | \$2,015           | \$93,182               |
| Nine Months Ended September 30, 2015  |           |            |          |                   |                   |                        |
| Net interest income                   | \$199,265 | \$218,699  | \$31,921 | \$449,885         | \$21,948          | \$471,833              |
| Provision for loan losses             | (25,500)  | 842        | 114      | (24,544)          | 5,003             | (19,541)               |
| Non-interest income                   | 87,462    | 144,685    | 102,517  | 334,664           | (2,567)           | 332,097                |
| Investment securities gains, net      | —         | —          | —        | —                 | 7,800             | 7,800                  |
| Non-interest expense                  | (203,440) | (199,097)  | (81,432) | (483,969)         | (16,741)          | (500,710)              |
| Income before income taxes            | \$57,787  | \$165,129  | \$53,120 | \$276,036         | \$15,443          | \$291,479              |

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 procedures and methods, which have been developed to reflect the underlying economics of the businesses. The methodologies are 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.

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## 10. 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 Company's derivative instruments are accounted for as free-standing derivatives, and changes in their fair value are recorded in current earnings.

| (In thousands)                       | September 30, December 31, |              |
|--------------------------------------|----------------------------|--------------|
|                                      | 2016                       | 2015         |
| Interest rate swaps                  | \$ 1,320,674               | \$ 1,020,310 |
| Interest rate caps                   | 60,954                     | 66,118       |
| Credit risk participation agreements | 63,117                     | 62,456       |
| Foreign exchange contracts           | 3,792                      | 15,535       |
| Mortgage loan commitments            | 24,301                     | 8,605        |
| Mortgage loan forward sale contracts | 518                        | 642          |
| Forward TBA contracts                | 25,500                     | 11,000       |
| Total notional amount                | \$ 1,498,856               | \$ 1,184,666 |

The largest group of notional amounts relate to interest rate swap contracts sold to commercial customers who wish to modify their interest rate sensitivity. These swaps are offset by matching contracts purchased by the Company from other financial dealer institutions. Contracts with dealers that require central clearing are novated to a clearing agency who becomes the Company's counterparty. 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.

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 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 and building materials, manufacturing, education, communications, retail product distribution, and retirement communities. At September 30, 2016, the largest potential loss exposures were in the groups related to real estate, distribution, and retirement communities. 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 \$15.7 million (real estate), \$3.5 million (retirement communities), and \$3.4 million (distribution) at September 30, 2016.

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 5 on Guarantees. In addition, the Company enters into foreign exchange contracts, which are mainly comprised of contracts to purchase or deliver foreign currencies for customers at specific future dates.

In 2015, the Company initiated a program of secondary market sales of residential mortgage loans and has designated certain newly-originated residential mortgage loans as held for sale. Derivative instruments arising from this activity include mortgage loan commitments and forward loan sale commitments. Changes in the fair values of the loan commitments and funded loans prior to sale that are due to changes in interest rates are economically hedged with

forward contracts to sell residential mortgage-backed securities in the to-be-announced (TBA) market. These forward TBA contracts are also considered to be derivatives and are settled in cash at the security settlement date.

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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. Derivative instruments with a positive fair value (asset derivatives) are reported in other assets in the consolidated balance sheets, while derivative instruments with a negative fair value (liability derivatives) are reported in other liabilities in the consolidated balance sheets. Information about the valuation methods used to determine fair value is provided in Note 13 on Fair Value Measurements.

|                                      | Asset Derivatives |               | Liability Derivatives |               |
|--------------------------------------|-------------------|---------------|-----------------------|---------------|
|                                      | Sept. 30, 2016    | Dec. 31, 2015 | Sept. 30, 2016        | Dec. 31, 2015 |
| (In thousands)                       | Fair Value        |               | Fair Value            |               |
| Derivative instruments:              |                   |               |                       |               |
| Interest rate swaps                  | \$31,135          | \$11,993      | \$(31,343)            | \$(11,993)    |
| Interest rate caps                   | 36                | 73            | (36)                  | (73)          |
| Credit risk participation agreements | 1                 | 1             | (272)                 | (195)         |
| Foreign exchange contracts           | 5                 | 437           | (10)                  | (430)         |
| Mortgage loan commitments            | 876               | 263           | —                     | —             |
| Mortgage loan forward sale contracts | 1                 | —             | —                     | —             |
| Forward TBA contracts                | 2                 | 4             | (111)                 | (38)          |
| Total                                | \$32,056          | \$12,771      | \$(31,772)            | \$(12,729)    |

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

|                                      | 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 September 30                      |       | For the Nine Months Ended September 30 |         |
| (In thousands)                       |  | 2016   | 2015  | 2016                                   | 2015    |
| Derivative instruments:              |  |  |       |  |         |
| Interest rate swaps                  | Other non-interest income                                      | \$203  | \$741 | \$3,198                                | \$3,551 |
| Credit risk participation agreements | Other non-interest income                                      | 50   | (57)  | (8)                                    | (9)     |
| Foreign exchange contracts           | Other non-interest income                                      | (20)   | (55)  | (12)                                   | 267     |
| Mortgage loan commitments            | Loan fees and sales  | 86   | 106   | 613                                    | 451     |
| Mortgage loan forward sale contracts | Loan fees and sales  | 1  | (6)   | 1                                      | (5)     |
| Forward TBA contracts                | Loan fees and sales  | (172)  | (370) | (898)                                  | 15      |
| Total                                |  | \$148  | \$359 | \$2,894                                | \$4,270 |

The following table shows the extent to which assets and liabilities relating to derivative instruments have been offset in the consolidated balance sheets. It also provides 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 is generally cash or marketable securities. The collateral amounts in this table are limited to the

outstanding balances of the related asset or liability (after netting is applied); thus amounts of excess collateral are not shown. Most of the derivatives in the following table were transacted under master netting arrangements that contain a conditional right of offset, such as close-out netting, upon default.

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The Company is party to master netting arrangements with most of its swap derivative counterparties; however, the Company does not offset derivative assets and liabilities under these arrangements on its consolidated balance sheet. Collateral, usually in the form of marketable securities, is exchanged between the Company and dealer bank counterparties and 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. For those swap transactions requiring central clearing, the Company posts cash and securities to its clearing agency. At September 30, 2016, the Company had a net liability position with dealer bank and clearing agency counterparties totaling \$31.3 million, and had posted securities with a fair value of \$5.1 million and cash totaling \$36.8 million. Collateral positions are valued daily, and adjustments to amounts received and pledged by the Company are made as appropriate to maintain proper collateralization for these transactions. Swap derivative transactions with customers are generally secured by rights to non-financial collateral, such as real and personal property, which is not shown in the table below.

| (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 |                             | Net Amount |
|--|-------------------------|---|--|---|-----------------------------|------------|
|  |                         |   |  | Financial Instruments Available for Offset    | Collateral Received/Pledged |            |
| September 30, 2016                                   |                         |   |  |   |                             |            |
| Assets:  |                         |   |  |   |                             |            |
| Derivatives subject to master netting agreements     | \$ 31,174               | \$  | -\$ 31,174                                 | \$(38)\$                                      | —                           | \$ 31,136  |
| Derivatives not subject to master netting agreements | 882                     | —   | 882  |   |                             |            |
| Total derivatives                                    | 32,056                  | —   | 32,056                                     |   |                             |            |
| Liabilities:   |                         |   |  |   |                             |            |
| Derivatives subject to master netting agreements     | \$ 31,762               | \$  | -\$ 31,762                                 | \$(38)\$                                      | (30,319)                    | ) \$ 1,405 |
| Derivatives not subject to master netting agreements | 10                      | —   | 10   |   |                             |            |
| Total derivatives                                    | 31,772                  | —   | 31,772                                     |   |                             |            |
| December 31, 2015                                    |                         |   |  |   |                             |            |
| Assets:  |                         |   |  |   |                             |            |
| Derivatives subject to master netting agreements     | \$ 12,071               | \$  | -\$ 12,071                                 | \$(94)\$                                      | —                           | \$ 11,977  |
| Derivatives not subject to master netting agreements | 700                     | —   | 700  |   |                             |            |
| Total derivatives                                    | 12,771                  | —   | 12,771                                     |   |                             |            |
| Liabilities:   |                         |   |  |   |                             |            |
| Derivatives subject to master netting agreements     | \$ 12,299               | \$  | -\$ 12,299                                 | \$(94)\$                                      | (10,927)                    | ) \$ 1,278 |
| Derivatives not subject to master netting agreements | 430                     | —   | 430  |   |                             |            |
| Total derivatives                                    | 12,729                  | —   | 12,729                                     |   |                             |            |

## 11. Resale and Repurchase Agreements

The following table shows the extent to which assets and liabilities relating to securities purchased under agreements to resell (resale agreements) and securities sold under agreements to repurchase (repurchase agreements) have been offset in the consolidated balance sheets, in addition to the extent to which they could potentially be offset. Also

shown is collateral received or pledged, which consists of marketable securities. The collateral amounts in the table are limited to the outstanding balances of the related asset or liability (after netting is applied); thus amounts of excess collateral are not shown. The agreements in the following table were transacted under master netting arrangements that contain a conditional right of offset, such as close-out netting, upon default.

Resale and repurchase agreements are agreements to purchase/sell securities subject to an obligation to resell/repurchase the same or similar securities. They are accounted for as collateralized financing transactions, not as sales and purchases of the securities portfolio. The securities collateral accepted or pledged in resale 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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The Company is party to several agreements commonly known as collateral swaps. These agreements involve the exchange of collateral under simultaneous repurchase and resale agreements with the same financial institution counterparty. These repurchase and resale agreements have the same principal amounts, inception dates, and maturity dates and have been offset against each other in the consolidated balance sheets, as permitted under the netting provisions of ASC 210-20-45. The collateral swaps totaled \$550.0 million at both September 30, 2016 and December 31, 2015. At September 30, 2016, the Company had posted collateral of \$572.9 million in marketable securities, consisting of agency mortgage-backed bonds and treasuries, and had accepted \$564.7 million in investment grade asset-backed, commercial mortgage-backed, and corporate bonds.

| (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 Available for Received/Pledged Offset | Net Amount |
| September 30, 2016  |                         |   |  |   |            |
| Total resale agreements, subject to master netting arrangements     | \$ 1,275,000            | \$(550,000)                               | \$ 725,000                                 | \$ \$(725,000)  | ) \$ —     |
| Total repurchase agreements, subject to master netting arrangements | 1,746,251               | (550,000)                                 | 1,196,251                                  | —(1,196,251)  | ) —        |
| December 31, 2015   |                         |   |  |   |            |
| Total resale agreements, subject to master netting arrangements     | \$ 1,425,000            | \$(550,000)                               | \$ 875,000                                 | \$ \$(875,000)  | ) \$ —     |
| Total repurchase agreements, subject to master netting arrangements | 1,956,582               | (550,000)                                 | 1,406,582                                  | —(1,406,582)  | ) —        |

The table below shows the remaining contractual maturities of repurchase agreements outstanding at September 30, 2016 and December 31, 2015, in addition to the various types of marketable securities that have been pledged as collateral for these borrowings.

| (In thousands)                                       | Remaining Contractual Maturity of the Agreements |               |                      |              |
|--|--|---------------|----------------------|--------------|
|  | Overnight and continuous                         | Up to 90 days | Greater than 90 days | Total        |
| September 30, 2016                                   |  |               |                      |              |
| Repurchase agreements, secured by:                   |  |               |                      |              |
| U.S. government and federal agency obligations       | \$ 228,435                                       | \$ —          | \$ 300,000           | \$ 528,435   |
| Government-sponsored enterprise obligations          | 185,224  | —             | 2,728                | 187,952      |
| Agency mortgage-backed securities                    | 367,145  | 2,908         | 252,982              | 623,035      |
| Asset-backed securities                              | 306,829  | 100,000       | —                    | 406,829      |
| Total repurchase agreements, gross amount recognized | \$ 1,087,633                                     | \$ 102,908    | \$ 555,710           | \$ 1,746,251 |
| December 31, 2015                                    |  |               |                      |              |
| Repurchase agreements, secured by:                   |  |               |                      |              |
| U.S. government and federal agency obligations       | \$ 210,346                                       | \$ —          | \$ 300,000           | \$ 510,346   |
| Government-sponsored enterprise obligations          | 356,970  | —             | 24,096               | 381,066      |

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|  |             |          |           |             |
|--|-------------|----------|-----------|-------------|
| Agency mortgage-backed securities                    | 579,974     | 2,292    | 225,904   | 808,170     |
| Asset-backed securities                              | 212,000     | 45,000   | —         | 257,000     |
| Total repurchase agreements, gross amount recognized | \$1,359,290 | \$47,292 | \$550,000 | \$1,956,582 |

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## 12. Stock-Based Compensation

The Company issues stock-based compensation in the form of nonvested restricted stock and stock appreciation rights (SARs). Most of the awards are issued during the first quarter of each year. The stock-based compensation expense that has been charged against income was \$2.6 million and \$2.4 million in the three month periods ended September 30, 2016 and 2015, respectively, and \$8.9 million and \$7.7 million in the nine months ended September 30, 2016 and 2015, 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 September 30, 2016, and changes during the nine month period then ended, is presented below.

|                                 | Shares    | Weighted Average Grant Date Fair Value |
|---------------------------------|-----------|--|
| Nonvested at January 1, 2016    | 1,384,417 | \$34.38                                |
| Granted                         | 221,222   | 42.17                                  |
| Vested                          | (249,953) | 30.51                                  |
| Forfeited                       | (28,618)  | 36.52                                  |
| Nonvested at September 30, 2016 | 1,327,068 | \$36.36                                |

SARs 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. In determining compensation cost, the Black-Scholes option-pricing model is used to estimate the fair value of SARs 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 | \$7.49    |
| Assumptions:  |           |
| Dividend yield                                      | 2.2 %     |
| Volatility  | 21.2 %    |
| Risk-free interest rate                             | 1.8 %     |
| Expected term                                       | 7.2 years |

A summary of SAR activity during the first nine months of 2016 is presented below.

| (Dollars in thousands, except per share data) | Rights    | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term | Aggregate Intrinsic Value |
|---|-----------|---------------------------------|---|---------------------------|
| Outstanding at January 1, 2016                | 1,588,457 | \$33.74                         |   |                           |
| Granted                                       | 251,982   | 41.35                           |   |                           |
| Forfeited                                     | (13,916)  | 38.06                           |   |                           |
| Expired                                       | (1,375)   | 37.19                           |   |                           |
| Exercised                                     | (469,903) | 31.37                           |   |                           |

Outstanding at September 30, 2016      1,355,245   \$35.93   5.6 years      \$ 18,068

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13. 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 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. The valuation methodologies for assets and liabilities measured at fair value on a recurring and non-recurring basis are described in the Fair Value Measurements note in the Company's 2015 Annual Report on Form 10-K. There have been no significant changes in these methodologies since then.

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## Instruments Measured at Fair Value on a Recurring Basis

The table below presents the September 30, 2016 and December 31, 2015 carrying values of assets and liabilities measured at fair value on a recurring basis. There were no transfers among levels during the first nine months of 2016 or the year ended December 31, 2015.

| (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) |
| September 30, 2016                                       |                  |  |   |   |
| Assets:  |                  |  |   |   |
| Residential mortgage loans held for sale                 | \$ 4,447         | \$—  | \$ 4,447                                      | \$ —                                      |
| Available for sale securities:                           |                  |  |   |   |
| U.S. government and federal agency obligations           | 755,649          | 755,649  | —   | —   |
| Government-sponsored enterprise obligations              | 451,242          | —  | 451,242                                       | —   |
| State and municipal obligations                          | 1,836,001        | —  | 1,819,093                                     | 16,908                                    |
| Agency mortgage-backed securities                        | 2,663,677        | —  | 2,663,677                                     | —   |
| Non-agency mortgage-backed securities                    | 937,208          | —  | 937,208                                       | —   |
| Asset-backed securities                                  | 2,409,324        | —  | 2,409,324                                     | —   |
| Other debt securities                                    | 338,812          | —  | 338,812                                       | —   |
| Equity securities  | 46,958           | 23,045   | 23,913  | —   |
| Trading securities                                       | 28,586           | —  | 28,586  | —   |
| Private equity investments                               | 59,486           | —  | —   | 59,486                                    |
| Derivatives *  | 32,056           | —  | 31,179  | 877                                       |
| Assets held in trust for deferred compensation plan      | 10,028           | 10,028   | —   | —   |
| Total assets   | 9,573,474        | 788,722  | 8,707,481                                     | 77,271                                    |
| Liabilities:   |                  |  |   |   |
| Derivatives *  | 31,772           | —  | 31,500  | 272                                       |
| Liabilities held in trust for deferred compensation plan | 10,028           | 10,028   | —   | —   |
| Total liabilities  | \$ 41,800        | \$ 10,028  | \$ 31,500                                     | \$ 272                                    |
| December 31, 2015  |                  |  |   |   |
| Assets:  |                  |  |   |   |
| Residential mortgage loans held for sale                 | \$ 4,981         | \$—  | \$ 4,981                                      | \$ —                                      |
| Available for sale securities:                           |                  |  |   |   |
| U.S. government and federal agency obligations           | 727,076          | 727,076  | —   | —   |
| Government-sponsored enterprise obligations              | 793,023          | —  | 793,023                                       | —   |
| State and municipal obligations                          | 1,741,957        | —  | 1,724,762                                     | 17,195                                    |
| Agency mortgage-backed securities                        | 2,618,281        | —  | 2,618,281                                     | —   |
| Non-agency mortgage-backed securities                    | 879,963          | —  | 879,963                                       | —   |
| Asset-backed securities                                  | 2,644,381        | —  | 2,644,381                                     | —   |
| Other debt securities                                    | 331,320          | —  | 331,320                                       | —   |

|  |           |          |           |        |
|--|-----------|----------|-----------|--------|
| Equity securities  | 41,003    | 20,263   | 20,740    | —      |
| Trading securities                                       | 11,890    | —        | 11,890    | —      |
| Private equity investments                               | 63,032    | —        | —         | 63,032 |
| Derivatives *  | 12,771    | —        | 12,507    | 264    |
| Assets held in trust for deferred compensation plan      | 9,278     | 9,278    | —         | —      |
| Total assets   | 9,878,956 | 756,617  | 9,041,848 | 80,491 |
| Liabilities:   |           |          |           |        |
| Derivatives *  | 12,729    | —        | 12,534    | 195    |
| Liabilities held in trust for deferred compensation plan | 9,278     | 9,278    | —         | —      |
| Total liabilities  | \$ 22,007 | \$ 9,278 | \$ 12,534 | \$ 195 |

\* The fair value of each class of derivative is shown in Note 10.

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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 Private<br>Municipal<br>Obligations                                 | Equity<br>Investments | Derivatives | Total       |
| (In thousands)   |   |                       |             |             |
| For the three months ended September 30, 2016  |   |                       |             |             |
| Balance June 30, 2016  | \$ 17,679   | \$ 62,813             | \$ 502      | \$ 80,994   |
| Total gains or losses (realized/unrealized):   |   |                       |             |             |
| Included in earnings   | —   | (2,921 )              | 136         | (2,785 )    |
| Included in other comprehensive income *   | 317   | —                     | —           | 317         |
| Investment securities called   | (1,100 )  | —                     | —           | (1,100 )    |
| Discount accretion   | 12  | —                     | —           | 12          |
| Purchases of private equity investments  | —   | 2,894                 | —           | 2,894       |
| Sale/pay down of private equity investments  | —   | (3,315 )              | —           | (3,315 )    |
| Capitalized interest/dividends   | —   | 15                    | —           | 15          |
| Sale of risk participation agreement   | —   | —                     | (33 )       | (33 )       |
| Balance September 30, 2016   | \$ 16,908   | \$ 59,486             | \$ 605      | \$ 76,999   |
| Total gains or losses for the three months included in earnings attributable to the change in unrealized gains or losses relating to assets still held at September 30, 2016 | \$ —  | \$ (2,921 )           | \$ 926      | \$ (1,995 ) |
| For the nine months ended September 30, 2016   |   |                       |             |             |
| Balance January 1, 2016  | \$ 17,195   | \$ 63,032             | \$ 69       | \$ 80,296   |
| Total gains or losses (realized/unrealized):   |   |                       |             |             |
| Included in earnings   | —   | (6,645 )              | 605         | (6,040 )    |
| Included in other comprehensive income *   | 819   | —                     | —           | 819         |
| Investment securities called   | (1,200 )  | —                     | —           | (1,200 )    |
| Discount accretion   | 94  | —                     | —           | 94          |
| Purchases of private equity investments  | —   | 8,735                 | —           | 8,735       |
| Sale/pay down of private equity investments  | —   | (5,713 )              | —           | (5,713 )    |
| Capitalized interest/dividends   | —   | 77                    | —           | 77          |
| Sale of risk participation agreement   | —   | —                     | (69 )       | (69 )       |
| Balance September 30, 2016   | \$ 16,908   | \$ 59,486             | \$ 605      | \$ 76,999   |
| Total gains or losses for the nine months included in earnings attributable to the change in unrealized gains or losses relating to assets still held at September 30, 2016  | \$ —  | \$ (6,545 )           | \$ 868      | \$ (5,677 ) |
| For the three months ended September 30, 2015  |   |                       |             |             |
| Balance June 30, 2015  | \$ 92,940   | \$ 58,726             | \$ 170      | \$ 151,836  |
| Total gains or losses (realized/unrealized):   |   |                       |             |             |
| Included in earnings   | —   | (1,221 )              | 49          | (1,172 )    |
| Included in other comprehensive income *   | 227   | —                     | —           | 227         |
| Discount accretion   | 22  | —                     | —           | 22          |
| Purchases of private equity investments  | —   | 9,370                 | —           | 9,370       |
| Balance September 30, 2015   | \$ 93,189   | \$ 66,875             | \$ 219      | \$ 160,283  |
| Total gains or losses for the three months included in earnings attributable to the change in unrealized gains or losses relating to assets still held at                    | \$ —  | \$ (1,221 )           | \$ 394      | \$ (827 )   |



September 30, 2015

For the nine months ended September 30, 2015

|   |          |           |           |           |
|---|----------|-----------|-----------|-----------|
| Balance January 1, 2015   | \$95,143 | \$ 57,581 | \$ (223 ) | \$152,501 |
| Total gains or losses (realized/unrealized):  |          |           |           |           |
| Included in earnings  | —        | 2,954     | 442       | 3,396     |
| Included in other comprehensive income *  | (127 )   | —         | —         | (127 )    |
| Investment securities called  | (2,000 ) | —         | —         | (2,000 )  |
| Discount accretion  | 173      | —         | —         | 173       |
| Purchases of private equity investments   | —        | 11,023    | —         | 11,023    |
| Sale/pay down of private equity investments   | —        | (4,800 )  | —         | (4,800 )  |
| Capitalized interest/dividends  | —        | 117       | —         | 117       |
| Balance September 30, 2015  | \$93,189 | \$ 66,875 | \$ 219    | \$160,283 |
| Total gains or losses for the nine months included in earnings attributable to the change in unrealized gains or losses relating to assets still held at September 30, 2015 | \$—      | \$ 2,954  | \$ 442    | \$3,396   |

\* 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<br>Fees<br>and<br>Sales | Other<br>Non-Interest<br>Income | Investment<br>Securities<br>Gains<br>(Losses),<br>Net | Total     |
|--|------------------------------|---------------------------------|---|-----------|
| For the three months ended September 30, 2016  |                              |                                 |   |           |
| Total gains or losses included in earnings   | \$ 86                        | \$ 50                           | \$ (2,921 )   | \$(2,785) |
| Change in unrealized gains or losses relating to assets still held at September 30, 2016 | \$ 876                       | \$ 50                           | \$ (2,921 )   | \$(1,995) |
| For the nine months ended September 30, 2016   |                              |                                 |   |           |
| Total gains or losses included in earnings   | \$ 613                       | \$ (8 )                         | \$ (6,645 )   | \$(6,040) |
| Change in unrealized gains or losses relating to assets still held at September 30, 2016 | \$ 876                       | \$ (8 )                         | \$ (6,545 )   | \$(5,677) |
| For the three months ended September 30, 2015  |                              |                                 |   |           |
| Total gains or losses included in earnings   | \$ 106                       | \$ (57 )                        | \$ (1,221 )   | \$(1,172) |
| Change in unrealized gains or losses relating to assets still held at September 30, 2015 | \$ 451                       | \$ (57 )                        | \$ (1,221 )   | \$(827 )  |
| For the nine months ended September 30, 2015   |                              |                                 |   |           |
| Total gains or losses included in earnings   | \$ 451                       | \$ (9 )                         | \$ 2,954  | \$3,396   |
| Change in unrealized gains or losses relating to assets still held at September 30, 2015 | \$ 451                       | \$ (9 )                         | \$ 2,954  | \$3,396   |

## Level 3 Inputs

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, investments in portfolio concerns held by the Company's private equity subsidiaries, and held for sale residential mortgage loan commitments. ARS are included in state and municipal securities and totaled \$16.9 million at September 30, 2016, while private equity investments, included in non-marketable securities, totaled \$59.5 million.

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

| Quantitative Information about Level 3 Fair Value Measurements |                             |                                  |             | Weighted<br>Average |
|--|-----------------------------|----------------------------------|-------------|---------------------|
|  | Valuation Technique         | Unobservable Input               | Range       |                     |
| Auction rate securities  | Discounted cash flow        | Estimated market recovery period | 5 years     |                     |
|  |                             | Estimated market rate            | 2.4% -3.3%  |                     |
| Private equity investments                                     | Market comparable companies | EBITDA multiple                  | 4.0 -5.5    |                     |
| Mortgage loan commitments                                      | Discounted cash flow        | Probability of funding           | 55.3%-97.7% | 76.8%               |
|  |                             | Embedded servicing value         | .9% -1.0%   | 1.0%                |

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## Instruments Measured at Fair Value on a Nonrecurring Basis

For assets measured at fair value on a nonrecurring basis during the first nine months of 2016 and 2015, and still held as of September 30, 2016 and 2015, 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 September 30, 2016 and 2015.

| (In thousands)                      | Fair Value | Fair Value Measurements Using                                  |   | Total Gains (Losses) Recognized During the Nine Months Ended September 30, 2016 |
|-------------------------------------|------------|--|---|---|
|                                     |            | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) |   |
| <b>September 30, 2016</b>           |            |  |   |   |
| Collateral dependent impaired loans | \$1,756    | \$-  | -\$ 1,756                                     | \$ (1,626 )   |
| Mortgage servicing rights           | 2,533      | —  | 2,533   | (7 )  |
| Foreclosed assets                   | 47         | —  | 47  | (66 )   |
| Long-lived assets                   | 2,232      | —  | 2,232   | (1,001 )  |
| <b>September 30, 2015</b>           |            |  |   |   |
| Collateral dependent impaired loans | \$6,860    | \$-  | -\$ 6,860                                     | \$ (1,794 )   |
| Mortgage servicing rights           | 1,461      | —  | 1,461   | 59  |
| Foreclosed assets                   | 479        | —  | 479   | (193 )  |
| Long-lived assets                   | 937        | —  | 937   | (1,366 )  |

## 14. 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 Fair Value Measurements and the Fair Value of Financial Instruments notes in the Company's 2015 Annual Report on Form 10-K. There have been no significant changes in these methods and inputs since December 31, 2015.



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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 Hierarchy Level | September 30, 2016 |                      | December 31, 2015 |                      |
|--|----------------------------|--------------------|----------------------|-------------------|----------------------|
|  |                            | Carrying Amount    | Estimated Fair Value | Carrying Amount   | Estimated Fair Value |
| <b>Financial Assets</b>                                  |                            |                    |                      |                   |                      |
| <b>Loans:</b>  |                            |                    |                      |                   |                      |
| Business   | Level 3                    | \$4,770,883        | \$4,819,577          | \$4,397,893       | \$4,421,237          |
| Real estate - construction and land                      | Level 3                    | 800,545            | 810,403              | 624,070           | 633,083              |
| Real estate - business                                   | Level 3                    | 2,520,528          | 2,561,306            | 2,355,544         | 2,387,101            |
| Real estate - personal                                   | Level 3                    | 1,968,005          | 1,998,235            | 1,915,953         | 1,940,863            |
| Consumer   | Level 3                    | 1,972,969          | 1,972,559            | 1,924,365         | 1,916,747            |
| Revolving home equity                                    | Level 3                    | 417,591            | 419,543              | 432,981           | 434,607              |
| Consumer credit card                                     | Level 3                    | 760,022            | 780,059              | 779,744           | 793,428              |
| Overdrafts   | Level 3                    | 19,698             | 19,698               | 6,142             | 6,142                |
| Loans held for sale                                      | Level 2                    | 9,511              | 9,511                | 7,607             | 7,607                |
| <b>Investment securities:</b>                            |                            |                    |                      |                   |                      |
| Available for sale                                       | Level 1                    | 778,694            | 778,694              | 747,339           | 747,339              |
| Available for sale                                       | Level 2                    | 8,643,269          | 8,643,269            | 9,012,470         | 9,012,470            |
| Available for sale                                       | Level 3                    | 16,908             | 16,908               | 17,195            | 17,195               |
| Trading  | Level 2                    | 28,586             | 28,586               | 11,890            | 11,890               |
| Non-marketable   | Level 3                    | 108,224            | 108,224              | 112,786           | 112,786              |
| Federal funds sold                                       | Level 1                    | 13,415             | 13,415               | 14,505            | 14,505               |
| Securities purchased under agreements to resell          | Level 3                    | 725,000            | 731,362              | 875,000           | 879,546              |
| Interest earning deposits with banks                     | Level 1                    | 56,767             | 56,767               | 23,803            | 23,803               |
| Cash and due from banks                                  | Level 1                    | 396,938            | 396,938              | 464,411           | 464,411              |
| Derivative instruments                                   | Level 2                    | 31,179             | 31,179               | 12,507            | 12,507               |
| Derivative instruments                                   | Level 3                    | 877                | 877                  | 264               | 264                  |
| Assets held in trust for deferred compensation plan      | Level 1                    | 10,028             | 10,028               | 9,278             | 9,278                |
| <b>Financial Liabilities</b>                             |                            |                    |                      |                   |                      |
| Non-interest bearing deposits                            | Level 1                    | \$7,130,415        | \$7,130,415          | \$7,146,398       | \$7,146,398          |
| Savings, interest checking and money market deposits     | Level 1                    | 11,023,526         | 11,023,526           | 10,834,746        | 10,834,746           |
| Time open and certificates of deposit                    | Level 3                    | 2,012,219          | 2,009,071            | 1,997,709         | 1,993,521            |
| Federal funds purchased                                  | Level 1                    | 293,640            | 293,640              | 556,970           | 556,970              |
| Securities sold under agreements to repurchase           | Level 3                    | 1,196,251          | 1,196,339            | 1,406,582         | 1,406,670            |
| Other borrowings   | Level 3                    | 101,415            | 104,490              | 103,818           | 108,542              |
| Derivative instruments                                   | Level 2                    | 31,500             | 31,500               | 12,534            | 12,534               |
| Derivative instruments                                   | Level 3                    | 272                | 272                  | 195               | 195                  |
| Liabilities held in trust for deferred compensation plan | Level 1                    | 10,028             | 10,028               | 9,278             | 9,278                |

## 15. Legal and Regulatory Proceedings

On August 15, 2014, a customer filed a class action complaint against the Bank in the Circuit Court, Jackson County, Missouri. The case is Cassandra Warren, et al v. Commerce Bank (Case No. 1416-CV19197). In the case, the

customer alleges violation of the Missouri usury statute in connection with the Bank charging overdraft fees in connection with point-of-sale/debit and automated-teller machine cards. The class was certified and consists of Missouri customers of the Bank who may have been similarly affected. The case has been stayed pending the final outcome of a similar case in which a ruling has been made in favor of the bank defendant. The Company believes that the stay will remain in effect until any appeals in the similar case have run their course. The Company believes the Warren complaint lacks merit and will defend itself vigorously. The amount of any ultimate exposure cannot be determined with certainty at this time.

The Company is in ongoing discussions with the U.S. Department of Labor concerning an investigation involving ERISA regulations related to a managed trust account. Currently, no assurances can be given as to the timing for the resolution of the investigation or its outcome, including any ultimate liability.

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The Company has various other legal proceedings pending at September 30, 2016, 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 and regulatory matters for which it deems a loss is probable and can be reasonably estimated. Some matters, which are in the early stages, have not yet progressed to the point where a loss amount can be determined to be probable and estimable.

### 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 2015 Annual Report on Form 10-K. Results of operations for the three and nine month periods ended September 30, 2016 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, changes in accounting and tax principles, estimates made on income taxes, competition with other entities that offer financial services, and such other factors as discussed in Part I Item 1A - "Risk Factors" and Part II Item 7 - "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Company's 2015 Annual Report on Form 10-K.

#### 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 2015 Annual Report on Form 10-K. There have been no changes in the Company's application of critical accounting policies since December 31, 2015.





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## Selected Financial Data

|  | Three Months Ended |         | Nine Months Ended |          |
|--|--------------------|---------|-------------------|----------|
|  | September 30       |         | September 30      |          |
|  | 2016               | 2015    | 2016              | 2015     |
| <b>Per Share Data</b>  |                    |         |                   |          |
| Net income per common share — basic                            | \$.69              | \$.63 * | \$2.04            | \$1.93 * |
| Net income per common share — diluted                          | .68                | .63 *   | 2.03              | 1.93 *   |
| Cash dividends on common stock                                 | .225               | .214 *  | .675              | .643 *   |
| Book value per common share                                    |                    |         | 25.01             | 22.83 *  |
| Market price   |                    |         | 49.26             | 43.39 *  |
| <b>Selected Ratios</b>   |                    |         |                   |          |
| (Based on average balance sheets)                              |                    |         |                   |          |
| Loans to deposits <sup>(1)</sup>                               | 64.33%             | 62.44%  | 63.53 %           | 60.97 %  |
| Non-interest bearing deposits to total deposits                | 35.02              | 35.44   | 34.43             | 34.89    |
| Equity to loans <sup>(1)</sup>                                 | 19.56              | 19.62   | 19.29             | 20.18    |
| Equity to deposits   | 12.58              | 12.25   | 12.26             | 12.31    |
| Equity to total assets   | 10.46              | 9.97    | 10.15             | 10.02    |
| Return on total assets   | 1.12               | 1.09    | 1.11              | 1.13     |
| Return on common equity  | 10.97              | 11.25   | 11.28             | 11.62    |
| (Based on end-of-period data)                                  |                    |         |                   |          |
| Non-interest income to revenue <sup>(2)</sup>                  | 41.06              | 40.72   | 41.18             | 41.31    |
| Efficiency ratio <sup>(3)</sup>                                | 62.25              | 62.55   | 62.04             | 62.12    |
| Tier I common risk-based capital ratio                         |                    |         | 11.66             | 11.54    |
| Tier I risk-based capital ratio                                |                    |         | 12.44             | 12.37    |
| Total risk-based capital ratio                                 |                    |         | 13.39             | 13.33    |
| Tangible common equity to tangible assets ratio <sup>(4)</sup> |                    |         | 9.22              | 8.72     |
| Tier I leverage ratio  |                    |         | 9.58              | 9.31     |

\* Restated for the 5% stock dividend distributed in December 2015.

(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 to tangible assets ratio is a measurement which management believes is a useful indicator of capital adequacy and utilization. It provides a meaningful basis for period to period and company to company comparisons, and also assists regulators, investors and analysts in analyzing the financial position of the Company. Tangible common equity and tangible assets are non-GAAP measures and should not be viewed as substitutes for, or superior to, data prepared in accordance with GAAP.

The following table is a reconciliation of the GAAP financial measures of total equity and total assets to the non-GAAP measures of total tangible common equity and total tangible assets.

|                               | September 30 |             |
|-------------------------------|--------------|-------------|
| (Dollars in thousands)        | 2016         | 2015        |
| Total equity                  | \$2,560,813  | \$2,371,043 |
| Less non-controlling interest | 5,392        | 5,738       |
| Less preferred stock          | 144,784      | 144,784     |
| Less goodwill                 | 138,921      | 138,921     |

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|   |              |              |   |
|---|--------------|--------------|---|
| Less core deposit premium                               | 4,088        | 5,365        |   |
| Total tangible common equity (a)                        | \$2,267,628  | \$2,076,235  |   |
| Total assets  | \$24,734,468 | \$23,967,648 |   |
| Less goodwill   | 138,921      | 138,921      |   |
| Less core deposit premium                               | 4,088        | 5,365        |   |
| Total tangible assets (b)                               | \$24,591,459 | \$23,823,362 |   |
| Tangible common equity to tangible assets ratio (a)/(b) | 9.22         | %8.72        | % |

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## Results of Operations

## Summary

| (Dollars in thousands)                               | Three Months Ended<br>September 30 |            |             | Nine Months Ended<br>September 30 |            |             |
|--|------------------------------------|------------|-------------|-----------------------------------|------------|-------------|
|  | 2016                               | 2015       | %<br>change | 2016                              | 2015       | %<br>change |
| Net interest income                                  | \$ 171,243                         | \$ 162,038 | 5.7 %       | \$ 506,847                        | \$ 471,833 | 7.4 %       |
| Provision for loan losses                            | (7,263)                            | (8,364)    | (13.2)      | (25,918)                          | (19,541)   | 32.6        |
| Non-interest income                                  | 119,319                            | 111,288    | 7.2         | 354,913                           | 332,097    | 6.9         |
| Investment securities gains (losses), net            | (1,965)                            | (378)      | N.M.        | (3,704)                           | 7,800      | N.M.        |
| Non-interest expense                                 | (181,242)                          | (171,402)  | 5.7         | (535,804)                         | (500,710)  | 7.0         |
| Income taxes   | (30,942)                           | (27,969)   | 10.6        | (91,854)                          | (88,929)   | 3.3         |
| Non-controlling interest expense                     | (605)                              | (601)      | .7          | (668)                             | (2,530)    | (73.6)      |
| Net income attributable to Commerce Bancshares, Inc. | 68,545                             | 64,612     | 6.1         | 203,812                           | 200,020    | 1.9         |
| Preferred stock dividends                            | (2,250)                            | (2,250)    | —           | (6,750)                           | (6,750)    | —           |
| Net income available to common shareholders          | \$ 66,295                          | \$ 62,362  | 6.3 %       | \$ 197,062                        | \$ 193,270 | 2.0 %       |

For the quarter ended September 30, 2016, net income attributable to Commerce Bancshares, Inc. (net income) amounted to \$68.5 million, an increase of \$3.9 million, or 6.1%, compared to the third quarter of the previous year, and a decrease of \$1.3 million, or 1.9%, compared to the previous quarter. For the current quarter, the annualized return on average assets was 1.12%, the annualized return on average common equity was 10.97%, and the efficiency ratio was 62.25%. Diluted earnings per common share was \$.68, an increase of 7.9% compared to \$.63 per share in the third quarter of 2015 and a decrease of 2.9% compared to \$.70 per share in the previous quarter.

Compared to the third quarter of last year, net interest income increased \$9.2 million, or 5.7%, mainly due to growth of \$8.8 million in interest income on loans and \$945 thousand in investment securities, partly offset by an increase of \$792 thousand in deposit interest expense. The provision for loan losses totaled \$7.3 million for the current quarter, representing a decrease of \$1.1 million from the third quarter of 2015. Non-interest income increased \$ 8.0 million, or 7.2%, with the largest increases occurring in bank card, deposit, trust, cash sweep, tax credit sales and loan fees, partly offset by lower swap fees. Non-interest expense increased \$9.8 million, or 5.7%, over the third quarter of 2015, primarily due to increases in salaries and benefits, occupancy costs, data processing, and FDIC insurance expense. Net investment securities losses totaled \$2.0 million in the current quarter compared to losses of \$378 thousand in the same quarter last year. The current quarter losses were mainly comprised of fair value adjustments to the Company's private equity portfolio.

Net income for the first nine months of 2016 was \$203.8 million, an increase of \$3.8 million over the same period last year. Diluted earnings per common share was \$2.03, an increase of 5.2% compared to \$1.93 per share in the same period last year. For the first nine months of 2016, the annualized return on average assets was 1.11%, the annualized return on average common equity was 11.25%, and the efficiency ratio was 62.04%. Net interest income increased \$35.0 million, or 7.4%, over the same period last year. This growth was largely due to increases of \$24.5 million in loan interest income and \$12.8 million in investment securities interest income, offset by a \$2.4 million increase in deposit interest expense. The provision for loan losses was \$25.9 million for the first nine months of 2016, up \$6.4 million over the same period last year. Non-interest income increased \$22.8 million, or 6.9%, over the first nine months of last year largely due to growth in deposit, bank card, cash sweep and loan fees. Non-interest expense increased \$35.1 million, or 7.0%, mainly due to higher salaries and benefits expense, data processing and software costs, and bank card rewards expense, in addition to a letter of credit recovery in the previous year that did not recur. Net investment securities losses totaled \$3.7 million in the first nine months of 2016 compared to net gains of \$7.8

million in the first nine months of 2015, with the majority of these pertaining to the private equity portfolio.

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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<br>September 30, 2016 vs.<br>2015 |                 |         | Nine Months Ended<br>September 30, 2016 vs.<br>2015 |                 |          |
|---|--|-----------------|---------|---|-----------------|----------|
|   | 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:  |  |                 |         |   |                 |          |
| Business  | \$3,306  | \$1,517         | \$4,823 | \$10,428  | \$3,487         | \$13,915 |
| Real estate - construction and land   | 3,053  | (96)            | 2,957   | 8,834   | (948)           | 7,886    |
| Real estate - business  | 1,375  | (548)           | 827     | 3,278   | (1,448)         | 1,830    |
| Real estate - personal  | 305  | (17)            | 288     | 747   | (263)           | 484      |
| Consumer  | 868  | (532)           | 336     | 3,990   | (1,874)         | 2,116    |
| Revolving home equity   | (197)  | 58              | (139)   | (355)   | (43)            | (398)    |
| Consumer credit card  | 127  | (120)           | 7       | 335   | (739)           | (404)    |
| Total interest on loans   | 8,837  | 262             | 9,099   | 27,257  | (1,828)         | 25,429   |
| Loans held for sale   | 282  | 4               | 286     | 1,046   | 7               | 1,053    |
| Investment securities:  |  |                 |         |   |                 |          |
| U.S. government and federal agency securities                                     | 3,574  | (3,591)         | (17)    | 3,250   | 2,998           | 6,248    |
| Government-sponsored enterprise obligations                                       | (1,807)  | 568             | (1,239) | (4,607)   | 2,650           | (1,957)  |
| State and municipal obligations   | (503)  | 648             | 145     | (1,177)   | 1,709           | 532      |
| Mortgage-backed securities  | 923  | (877)           | 46      | 5,525   | (4,285)         | 1,240    |
| Asset-backed securities   | (596)  | 1,906           | 1,310   | (3,188)   | 7,801           | 4,613    |
| Other securities  | 172  | 623             | 795     | 2,241   | 236             | 2,477    |
| Total interest on investment securities   | 1,763  | (723)           | 1,040   | 2,044   | 11,109          | 13,153   |
| Federal funds sold and short-term securities purchased under agreements to resell | (8)  | 7               | (1)     | (4)   | 22              | 18       |
| Long-term securities purchased under agreements to resell                         | (782)  | 837             | 55      | (2,144)   | 2,307           | 163      |
| Interest earning deposits with banks  | 30   | 135             | 165     | (58)  | 343             | 285      |
| Total interest income   | 10,122   | 522             | 10,644  | 28,141  | 11,960          | 40,101   |
| Interest expense:   |  |                 |         |   |                 |          |
| Deposits:   |  |                 |         |   |                 |          |
| Savings   | 13   | (11)            | 2       | 44  | (1)             | 43       |
| Interest checking and money market  | 152  | 109             | 261     | 338   | 319             | 657      |
| Time open & C.D.'s of less than \$100,000   | (76)   | (27)            | (103)   | (248)   | (102)           | (350)    |
| Time open & C.D.'s of \$100,000 and over  | 66   | 566             | 632     | 164   | 1,887           | 2,051    |
| Total interest on deposits  | 155  | 637             | 792     | 298   | 2,103           | 2,401    |
| Federal funds purchased and securities sold under agreements to repurchase        | (150)  | 391             | 241     | (287)   | 1,353           | 1,066    |
| Other borrowings  | (18)   | 26              | 8       | 2,352   | (1,953)         | 399      |
| Total interest expense  | (13)   | 1,054           | 1,041   | 2,363   | 1,503           | 3,866    |

|   |          |         |         |          |          |          |
|---|----------|---------|---------|----------|----------|----------|
| Net interest income, tax equivalent basis | \$10,135 | \$(532) | \$9,603 | \$25,778 | \$10,457 | \$36,235 |
|---|----------|---------|---------|----------|----------|----------|

Net interest income in the third quarter of 2016 was \$171.2 million, an increase of \$9.2 million over the third quarter of 2015. On a tax equivalent (T/E) basis, net interest income totaled \$179.1 million in the third quarter of 2016, up \$9.6 million over the same period last year and down \$477 thousand from the previous quarter. The increase in net interest income compared to the third quarter of 2015 was mainly due to higher interest on loans of \$9.4 million, coupled with higher interest income on investment securities of \$1.0 million. The increase in securities interest was mainly due to \$938 thousand received in the third quarter of 2016 on a private equity debt investment which had previously been on non-accrual status. Securities interest also includes inflation-

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related interest on the Company's holdings of U.S. Treasury inflation-protected securities (TIPS), which is tied to the Consumer Price Index. Interest income related to TIPS increased \$3.1 million in the first nine months of 2016 compared to the same period in 2015, and totaled \$2.2 million in the current quarter, \$3.7 million in the prior quarter and \$3.3 million in the third quarter of 2015. The Company's net yield on earning assets (T/E) was 3.08% in the current quarter, compared to 3.11% in the previous quarter and 3.00% in the third quarter of 2015. Excluding the effects of inflation income and the additional earnings on the private equity debt investment, the net yield on earning assets would have been 3.02% in the current quarter, 3.01% in the previous quarter and 2.94% in the third quarter of 2015.

Total interest income (T/E) increased \$10.6 million over the third quarter of 2015. Interest income on loans (T/E), including loans held for sale, increased \$9.4 million due to an increase of \$1.1 billion, or 9.1%, in average loan balances, partly offset by a three basis point decrease in average rates earned. Most of the increase in interest income occurred in the business, construction, and business real estate loan categories. The largest increase to interest income occurred in business loan interest, which grew \$4.8 million due to higher average balances of \$472.9 million, or 11.2%, coupled with a 14 basis point increase in the average rate earned. Construction loan interest grew \$3.0 million, as average balances increased \$345.1 million, or 72.4%, and the average rate earned decreased four basis points. Business real estate loan interest increased \$827 thousand due to an increase in average balances of \$147.4 million, or 6.5%, partly offset by a decline of eight basis points in the average rate earned. Interest on consumer loans, including held for sale, totaled \$19.4 million, an increase of \$616 thousand over the the same period last year. The average balance of consumer loans grew \$107.8 million, or 5.8%, partly offset by a decline of eight basis points in the average rate earned. Most of the increase in average consumer loan balances resulted from growth of \$139.7 million in auto loans and other consumer loans, partly offset by a decrease of \$42.7 million in marine and recreational vehicle (RV) loans, as that portfolio continues to pay down.

Interest income on investment securities (T/E) was \$57.1 million during the third quarter of 2016, which was an increase of \$1.0 million over the same quarter last year. The increase resulted mainly from higher interest income on asset-backed securities, corporate debt securities, and non-marketable investments, partly offset by lower earnings on government-sponsored enterprise obligations. Higher interest income on asset-backed securities resulted from an increase of 33 basis points in the average rate earned, partly offset by lower balances of \$206.2 million, while growth in interest income on corporate debt securities resulted from both higher balances and rates earned. The increase in interest income on non-marketable investments resulted largely from the \$938 thousand interest receipt on the private equity investment mentioned above. Partly offsetting these increases was a decline in the average balances invested in government-sponsored enterprise obligations of \$406.1 million, or 45.7%, and a decline in TIPS interest of \$1.1 million. Adjustments to premium amortization expense, due to slowing prepayment speeds on various mortgage-backed and asset-backed securities, increased interest income by \$746 thousand in the current quarter, compared to adjustments of \$275 thousand in the same quarter last year. The average balance of the total investment portfolio (excluding unrealized fair value adjustments) was \$9.1 billion in the third quarter of 2016, compared to \$9.3 billion in the third quarter of 2015.

Interest income on long-term securities purchased under agreements to resell increased \$55 thousand over the third quarter of 2015, due to an increase in the average rate earned of 44 basis points, partly offset by lower balances invested of \$241.3 million. Additionally, interest earning balances at the Federal Reserve increased \$165 thousand over the third quarter of 2015, due to a 26 basis point increase in the average rate earned.

The average tax equivalent yield on total interest earning assets was 3.22% in the third quarter of 2016, up from 3.12% in the third quarter of 2015.

Total interest expense increased \$1.0 million compared to the third quarter of 2015, due to a \$792 thousand increase in interest expense on interest bearing deposits and a \$249 thousand increase in interest expense on borrowings. The increase in deposit expense mainly resulted from a slight increase in overall average rates paid, including a 33 basis point increase in average rates paid on short-term jumbo C.D. balances. Increases of \$589.7 million in average money market account balances and \$283.1 million in short-term jumbo C.D. balances also contributed to higher deposit expense. Interest expense on borrowings increased due to higher rates paid on federal funds purchased and repurchase agreements, partly offset by lower average balances of repurchase agreements. The overall average rate incurred on all interest bearing liabilities was .22% and .20% in the third quarters of 2016 and 2015, respectively.

Net interest income (T/E) for the first nine months of 2016 was \$530.1 million compared to \$493.9 million for the same period in 2015. For the first nine months of 2016, the net interest margin was 3.05% compared to 2.93% for the first nine months of 2015.

Total interest income (T/E) for the first nine months of 2016 increased \$40.1 million over the same period last year, due to higher interest income on loans and investment securities. Loan interest income (T/E), including loans held for sale, rose \$26.5



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million due to a \$1.1 billion increase in total average loan balances, but was partly offset by a seven basis point decline in the average rate earned. Most of the increase in loan interest occurred in the business, construction and consumer loan categories. The growth in interest income on investment securities (T/E) was mainly due to a 21 basis point increase in the average rate earned. Increased earnings were recorded for U.S. government and federal agency securities, due to higher TIPS interest of \$3.1 million. In addition, interest earned on asset-backed, corporate debt and mortgage-backed securities increased \$4.6 million, \$2.2 million, and \$1.2 million, respectively. Interest income on long-term resell agreements grew \$163 thousand due to higher average rates earned, partly offset by lower average balances.

Total interest expense for the first nine months of 2016 increased \$3.9 million compared to last year. Interest expense on interest bearing deposits increased \$2.4 million, mainly due to a slight increase in overall average rates paid, in addition to higher average money market account balances and short-term jumbo C.D. balances. Interest expense on borrowings also increased \$1.5 million, mainly due to higher rates paid on federal funds purchased and repurchase agreements, partly offset by lower average balances of repurchase agreements. Interest expense on FHLB borrowings also increased, due to higher short-term borrowings outstanding during the first quarter of 2016. The overall cost of total interest bearing liabilities increased to .22% compared to .20% 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.

## Non-Interest Income

| (Dollars in thousands)                       | Three Months Ended<br>September 30 |           |             | Nine Months Ended September<br>30 |           |             |
|--|------------------------------------|-----------|-------------|-----------------------------------|-----------|-------------|
|  | 2016                               | 2015      | %<br>change | 2016                              | 2015      | %<br>change |
| Bank card transaction fees                   | \$47,006                           | \$44,635  | 5.3 %       | \$136,541                         | \$132,606 | 3.0 %       |
| Trust fees                                   | 30,951                             | 29,302    | 5.6         | 90,435                            | 88,815    | 1.8         |
| Deposit account charges and other fees       | 22,241                             | 20,674    | 7.6         | 64,260                            | 58,810    | 9.3         |
| Capital market fees                          | 2,751                              | 2,620     | 5.0         | 7,976                             | 8,360     | (4.6 )      |
| Consumer brokerage services                  | 3,375                              | 3,687     | (8.5 )      | 10,375                            | 10,530    | (1.5 )      |
| Loan fees and sales                          | 3,123                              | 1,855     | 68.4        | 8,829                             | 6,127     | 44.1        |
| Other  | 9,872                              | 8,515     | 15.9        | 36,497                            | 26,849    | 35.9        |
| Total non-interest income                    | \$119,319                          | \$111,288 | 7.2 %       | \$354,913                         | \$332,097 | 6.9 %       |
| Non-interest income as a % of total revenue* | 41.1                               | %40.7     | %           | 41.2                              | %41.3     | %           |

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

For the third quarter of 2016, total non-interest income amounted to \$119.3 million compared with \$111.3 million in the same quarter last year, which was an increase of \$8.0 million, or 7.2%. This increase was mainly due to growth in bank card, deposit, trust, sweep, tax credit sales and loan fees and sales income, partly offset by lower swap fee income.

Bank card transaction fees for the current quarter increased \$2.4 million, or 5.3%, over the same period last year. The increase was mainly the result of growth in corporate card fees of \$2.0 million, or 9.2%, as a result of a higher volume of transactions this quarter. The table below is a summary of bank card transaction fees for the three and nine month periods ended September 30, 2016 and 2015.

| (Dollars in thousands) | Three Months Ended<br>September 30 |      | Nine Months Ended<br>September 30 |      |
|------------------------|------------------------------------|------|-----------------------------------|------|
|                        | 2016                               | 2015 | 2016                              | 2015 |

|                                  |          |          | %   | change |           |           | %   | change |
|----------------------------------|----------|----------|-----|--------|-----------|-----------|-----|--------|
| Debit card fees                  | \$9,913  | \$9,732  | 1.9 | %      | \$29,330  | \$28,385  | 3.3 | %      |
| Credit card fees                 | 6,245    | 6,213    | .5  |        | 18,192    | 17,721    | 2.7 |        |
| Merchant fees                    | 6,828    | 6,689    | 2.1 |        | 20,857    | 19,552    | 6.7 |        |
| Corporate card fees              | 24,020   | 22,001   | 9.2 |        | 68,162    | 66,948    | 1.8 |        |
| Total bank card transaction fees | \$47,006 | \$44,635 | 5.3 | %      | \$136,541 | \$132,606 | 3.0 | %      |

Trust fees for the quarter increased \$1.6 million, or 5.6%, over the same quarter last year, resulting mainly from continued growth in personal (up 4.0%) and institutional (up 5.6%) trust fees. Deposit account fees increased \$1.6 million, or 7.6%, over the same period last year, as deposit account service charges increased \$1.2 million, or 28.6%, and corporate cash management fees increased \$522 thousand, or 6.0%. Capital market fees increased 5.0% over the same quarter last year on higher sales volumes, while consumer brokerage services revenue declined \$312 thousand, or 8.5%, on lower variable annuity fees. Loan fees and sales increased \$1.3 million this quarter mainly due to higher mortgage banking revenue, which resulted from higher sales of newly originated residential mortgages under the Company's sale program that began in 2015. Other non-interest income increased \$1.4

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million compared to the same quarter last year. This increase included growth in cash sweep commissions and fees on sales of tax credits, which increased by \$1.3 million and \$358 thousand, respectively, this quarter compared to the same period last year. These increases were partly offset by a decrease of \$432 thousand in fees from the sales of interest rate swaps as a result of lower sales volumes in the current quarter.

Non-interest income for the first nine months of 2016 was \$354.9 million compared to \$332.1 million in the first nine months of 2015, resulting in an increase of \$22.8 million, or 6.9%. Bank card fees increased \$3.9 million, or 3.0%, as a result of growth in merchant fees of \$1.3 million, corporate card fees of \$1.2 million, debit card fees of \$945 thousand and credit card fees of \$471 thousand, all due to higher sales volumes. Trust fee income increased \$1.6 million, or 1.8%, as a result of growth in personal and institutional trust fees. Deposit account fees increased \$5.5 million, or 9.3%, due to growth in deposit account service charges and corporate cash management fees. Loan fees and sales increased \$2.7 million, or 44.1%, due to higher mortgage banking revenue. Other non-interest income increased \$9.6 million, or 35.9%, due in part to a \$3.3 million gain on the sale of a former branch property recorded in the first quarter of 2016, while net losses on other branch properties sold or held for sale declined \$1.2 million. In addition, an accrual for a trust related settlement of \$897 thousand was recorded in the second quarter of 2016, while cash sweep commissions and fees from sales of tax credits increased \$3.9 million and \$756 thousand, respectively. These increases in current income were partly offset by lower leasing revenue of \$979 thousand.

## Investment Securities Gains (Losses), Net

|   | Three Months |          | Nine Months  |         |
|---|--------------|----------|--------------|---------|
|   | Ended        |          | Ended        |         |
| (In thousands)                                  | September 30 |          | September 30 |         |
|   | 2016         | 2015     | 2016         | 2015    |
| Available for sale                              | \$—          | \$—      | \$(270 )     | \$2,330 |
| Non-marketable                                  | (1,965 )     | (378 )   | (3,434 )     | 5,470   |
| Total investment securities gains (losses), net | \$(1,965 )   | \$(378 ) | \$(3,704 )   | \$7,800 |

Net gains and losses on investment securities which were recognized in earnings during the three and nine months ended September 30, 2016 and 2015 are shown in the table above. Net securities losses amounted to \$2.0 million in the third quarter of 2016 and \$3.7 million in the first nine months of 2016. 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 \$34.6 million at September 30, 2016. During the current quarter, no additional credit-related impairment losses were recorded. The total losses for the first nine months of 2016 amounted to \$270 thousand.

Gains and losses on non-marketable investment securities include those relating to private equity investments, which are primarily held by the Parent's majority-owned private equity subsidiaries. These gains and losses include fair value adjustments, which totaled \$6.6 million in net losses in the first nine months of 2016. In addition, a \$1.3 million gain on sale was recorded in the current quarter, and a \$1.8 million gain was realized in the previous quarter upon the Parent's withdrawal from a private equity fund, as required under the Volcker Rule investment prohibitions. 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 \$144 thousand during the first nine months of 2016 and expense of \$1.9 million during the first nine months of 2015.

During the first nine months of 2015, the Company sold from the available for sale portfolio \$114.6 million of municipal bonds, \$48.1 million of U.S. Treasury inflation-protected bonds and \$506.4 million of asset-backed bonds, realizing gains of \$2.8 million. Most of these sales were part of plan to extend the duration of the securities portfolio and improve net interest margins.



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## Non-Interest Expense

| (Dollars in thousands)         | Three Months Ended<br>September 30 |            |             | Nine Months Ended<br>September 30 |            |             |
|--------------------------------|------------------------------------|------------|-------------|-----------------------------------|------------|-------------|
|                                | 2016                               | 2015       | %<br>change | 2016                              | 2015       | %<br>change |
| Salaries and employee benefits | \$ 107,004                         | \$ 100,874 | 6.1 %       | \$ 318,671                        | \$ 298,603 | 6.7 %       |
| Net occupancy                  | 12,366                             | 11,247     | 9.9         | 34,761                            | 33,807     | 2.8         |
| Equipment                      | 4,842                              | 4,789      | 1.1         | 14,257                            | 14,171     | .6          |
| Supplies and communication     | 5,968                              | 5,609      | 6.4         | 18,490                            | 16,416     | 12.6        |
| Data processing and software   | 23,663                             | 21,119     | 12.0        | 69,332                            | 61,670     | 12.4        |
| Marketing                      | 4,399                              | 4,343      | 1.3         | 12,601                            | 12,568     | .3          |
| Deposit insurance              | 3,576                              | 2,981      | 20.0        | 9,884                             | 9,001      | 9.8         |
| Other                          | 19,424                             | 20,440     | (5.0 )      | 57,808                            | 54,474     | 6.1         |
| Total non-interest expense     | \$ 181,242                         | \$ 171,402 | 5.7 %       | \$ 535,804                        | \$ 500,710 | 7.0 %       |

Non-interest expense for the third quarter of 2016 amounted to \$181.2 million, an increase of \$9.8 million, or 5.7%, compared with \$171.4 million in the third quarter of last year. Salaries expense increased \$4.4 million, or 5.1%, mainly due to higher full-time salaries and incentive compensation costs. Employee benefits expense also increased \$1.7 million, or 11.6%, mostly due to higher medical costs. Growth in salaries expense resulted partly from higher staffing costs, mainly in the areas of residential lending, commercial card, trust, information technology and other supporting units, partially offset by lower staffing in branches. Full-time equivalent employees totaled 4,778 at September 30, 2016 compared to 4,770 at September 30, 2015. Compared to the third quarter of last year, data processing and software costs and occupancy expense grew \$2.5 million and \$1.1 million, respectively, while costs for marketing and equipment remained relatively flat. The increase in data processing and software costs resulted from higher bank card processing costs of \$1.1 million, coupled with higher software expense and fees paid to outsourced data providers. Higher occupancy costs were the result of increased rental of disaster recover facilities and demolition costs of a branch facility being replaced. Cost for supplies and communication increased \$359 thousand, or 6.4%, mainly on higher costs related to the reissuance of EMV chip cards and increased data network expense. FDIC insurance costs increased \$595 thousand compared to the same quarter last year due to higher deposit balances and higher insurance rates that were effective July 1, 2016. Other non-interest expense decreased \$1.0 million, or 5.0%, compared to the previous year. This decrease was mainly due to a decline of \$1.1 million in operating losses, mainly due to lower bank card related fraud losses.

For the first nine months of 2016, non-interest expense amounted to \$535.8 million, an increase of \$35.1 million, or 7.0%, compared with \$500.7 million in the same period last year. Salaries and benefits increased \$20.1 million, or 6.7%, mainly due to higher full-time salaries, incentives and medical expense. Supplies and communication expense increased \$2.1 million, or 12.6%, mainly due to the higher chip card reissuance costs mentioned above and higher data network expense. Occupancy expense increased \$954 thousand, or 2.8%, while deposit insurance increased \$883 thousand, or 9.8%, both due to the trends mentioned above. Data processing and software expense increased \$7.7 million, or 12.4%, mainly due to higher bank card processing costs and outsourced data provider fees. Other expense increased \$3.3 million, or 6.1%, mainly due to a recovery of \$2.8 million in 2015 related to a letter of credit exposure which had been drawn upon and subsequently paid off. In addition, higher costs were recorded for bank card rewards expense (up \$2.5 million) and charitable contribution expense (up \$750 thousand). These increases were partly offset by lower depreciation on operating lease assets and lower bank card related fraud losses, which declined \$1.1 million and \$2.2 million, respectively.

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## Provision and Allowance for Loan Losses

| (In thousands)                     | Three Months Ended |               |                | Nine Months Ended September 30 |          |
|------------------------------------|--------------------|---------------|----------------|--------------------------------|----------|
|                                    | Sept. 30, 2016     | June 30, 2016 | Sept. 30, 2015 | 2016                           | 2015     |
| Provision for loan losses          | \$7,263            | \$9,216       | \$8,364        | \$25,918                       | \$19,541 |
| Net loan charge-offs (recoveries): |                    |               |                |                                |          |
| Commercial:                        |                    |               |                |                                |          |
| Business                           | (50 )              | (65 )         | (175 )         | 348                            | (255 )   |
| Real estate-construction and land  | (2,312 )           | (507 )        | (67 )          | (2,830 )                       | (1,322 ) |
| Real estate-business               | (106 )             | (1,030 )      | (22 )          | (1,378 )                       | 493      |
|                                    | (2,468 )           | (1,602 )      | (264 )         | (3,860 )                       | (1,084 ) |
| Personal Banking:                  |                    |               |                |                                |          |
| Real estate-personal               | (78 )              | 305           | (69 )          | 32                             | (17 )    |
| Consumer                           | 2,240              | 1,781         | 2,435          | 6,620                          | 6,027    |
| Revolving home equity              | 79                 | 75            | 49             | 242                            | 192      |
| Consumer credit card               | 6,356              | 6,650         | 5,784          | 18,924                         | 18,560   |
| Overdrafts                         | 434                | 307           | 429            | 960                            | 863      |
|                                    | 9,031              | 9,118         | 8,628          | 26,778                         | 25,625   |
| Total net loan charge-offs         | \$6,563            | \$7,516       | \$8,364        | \$22,918                       | \$24,541 |

|  | Three Months Ended |               |                | Nine Months Ended September 30 |           |
|--|--------------------|---------------|----------------|--------------------------------|-----------|
|  | Sept. 30, 2016     | June 30, 2016 | Sept. 30, 2015 | 2016                           | 2015      |
| Annualized net loan charge-offs (recoveries)*: |                    |               |                |                                |           |
| Commercial:                                    |                    |               |                |                                |           |
| Business                                       | —                  | %(0.01 )%     | %(0.02 )%      | .01                            | %(0.01 )% |
| Real estate-construction and land              | (1.12 )            | (.26 )        | (.06 )         | (.49 )                         | (.40 )    |
| Real estate-business                           | (.02 )             | (.17 )        | —              | (.08 )                         | .03       |
|  | (.12 )             | (.08 )        | (.01 )         | (.07 )                         | (.02 )    |
| Personal Banking:                              |                    |               |                |                                |           |
| Real estate-personal                           | (.02 )             | .06           | (.01 )         | —                              | —         |
| Consumer                                       | .46                | .37           | .52            | .46                            | .45       |
| Revolving home equity                          | .08                | .07           | .04            | .08                            | .06       |
| Consumer credit card                           | 3.37               | 3.62          | 3.08           | 3.38                           | 3.34      |
| Overdrafts                                     | 37.11              | 31.53         | 32.52          | 28.84                          | 22.55     |
|  | .71                | .74           | .69            | .71                            | .70       |
| Total annualized net loan charge-offs          | .20                | %.24          | %.28           | %.24                           | %.28      |

\* 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 and collateral. 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

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include certain troubled debt restructurings with similar risk characteristics. Allowances for both personal banking and commercial loans use methods which consider historical and current loss trends, loss emergence periods, delinquencies, industry concentrations and unique risks. Economic conditions throughout the Company's market place, as monitored by Company credit officers, are also considered in the allowance determination process. The Company's estimate of the allowance for loan losses and the corresponding provision for loan losses rest upon various judgments and assumptions made by management. In addition to past loan loss experience, various qualitative factors are considered, such as current loan portfolio composition and characteristics, trends in delinquencies, portfolio risk ratings, levels of non-performing assets, credit concentrations, collateral values, 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 2015 Annual Report on Form 10-K contains additional discussion on the allowance and charge-off policies.

Net loan charge-offs in the third quarter of 2016 amounted to \$6.6 million, compared with \$7.5 million in the prior quarter and \$8.4 million in the third quarter of last year. The decrease in current quarter net loan charge-offs compared to the previous quarter was mainly the result of higher construction loan recoveries recorded this quarter, offset by lower business real estate recoveries recorded this quarter. In the current quarter, net recoveries of \$2.3 million were recorded on construction loans, while in the prior quarter, recoveries of \$1.0 million were recorded on business real estate loans. For the three months ended September 30, 2016, annualized net loan charge-offs on average consumer credit card loans totaled 3.37%, compared with 3.62% in the previous quarter and 3.08% in the same period last year. Consumer loan annualized net charge-offs in the current quarter amounted to .46%, compared to .37% in the prior quarter and .52% in the same period last year. Annualized net charge-offs on personal real estate loans also remained low this quarter. In the third quarter of 2016, total annualized net loan charge-offs were .20%, compared to .24% in the previous quarter and .28% in the same period last year.

In the current quarter, the provision for loan losses totaled \$7.3 million and exceeded net loan charge-offs by \$700 thousand, growing the allowance for loan losses. In the same period last year, the provision for loan losses totaled \$8.4 million and equaled net loan charge-offs. The provision for loan losses in the current quarter decreased by \$2.0 million compared to the previous quarter.

For the nine months ended September 30, 2016, net loan charge-offs totaled \$22.9 million, compared to \$24.5 million during the same period in 2015. The \$1.6 million decrease in net loan charge-offs resulted from higher recoveries on construction and business real estate loans, which increased by \$3.4 million, offset by higher net loan charge-offs on business, consumer, and consumer credit card loans. The provision for loan losses for the first nine months of 2016 was \$25.9 million and increased by \$6.4 million compared to the previous year. The provision expense for the first nine months of 2016 was \$3.0 million higher than net charge-offs during this period, resulting in an increase in the allowance for loan losses. In the comparable prior period, the provision was \$5.0 million less than net loan charge-offs, accordingly, reducing the allowance for loan losses.

At September 30, 2016, the allowance for loan losses amounted to \$154.5 million and was 1.17% of total loans and 988% of total non-accrual loans. At December 31, 2015, the allowance for loan losses amounted to \$151.5 million and was 1.22% of total loans and 570% of total non-accrual loans.





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## 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)                                   | September 30, December 31, |           |   |
|--|----------------------------|-----------|---|
|  | 2016                       | 2015      |   |
| Non-accrual loans  | \$ 15,645                  | \$ 26,575 |   |
| Foreclosed real estate                                   | 950                        | 2,819     |   |
| Total non-performing assets                              | \$ 16,595                  | \$ 29,394 |   |
| Non-performing assets as a percentage of total loans     | .13                        | % .24     | % |
| Non-performing assets as a percentage of total assets    | .07                        | % .12     | % |
| Total loans past due 90 days and still accruing interest | \$ 16,916                  | \$ 16,467 |   |

Non-accrual loans, which are also classified as impaired, totaled \$15.6 million at September 30, 2016, and decreased \$10.9 million from balances at December 31, 2015. The decrease occurred mainly in business real estate loans, business loans, and construction real estate loans, which decreased \$5.9 million, \$2.1 million, and \$1.8 million, respectively. At September 30, 2016, non-accrual loans were comprised mainly of business (56.0%), personal real estate (23.2%), and business real estate (12.3%) loans. Foreclosed real estate totaled \$950 thousand at September 30, 2016, a decrease of \$1.9 million when compared to December 31, 2015. Total loans past due 90 days or more and still accruing interest were \$16.9 million as of September 30, 2016, an increase of \$449 thousand when compared to December 31, 2015. Balances by class for non-accrual loans and loans past due 90 days and still accruing interest are shown in the "Delinquent and non-accrual loans" section in Note 2 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 \$113.6 million at September 30, 2016 compared with \$113.1 million at December 31, 2015, resulting in an increase of \$445 thousand, or .4%.

| (In thousands)                      | September 30, December 31, |            |
|-------------------------------------|----------------------------|------------|
|                                     | 2016                       | 2015       |
| Potential problem loans:            |                            |            |
| Business                            | \$ 60,845                  | \$ 58,860  |
| Real estate – construction and land | 207                        | 1,159      |
| Real estate – business              | 51,000                     | 51,107     |
| Real estate – personal              | 1,536                      | 1,755      |
| Consumer                            | —                          | 262        |
| Total potential problem loans       | \$ 113,588                 | \$ 113,143 |

At September 30, 2016, the Company had \$59.0 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, and are further discussed in the

"Troubled debt restructurings" section in Note 2 to the consolidated financial statements. This balance includes certain commercial loans totaling \$33.2 million which are classified as substandard and included in the table above because of this classification.

#### 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 2 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 normally obtains an updated appraisal or valuation at the time a loan is renewed or modified, or if the loan becomes significantly delinquent or is in the process of being foreclosed upon.

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## Real Estate – Construction and Land Loans

The Company's portfolio of construction and land loans, as shown in the table below, amounted to 6.1% of total loans outstanding at September 30, 2016. The largest component of construction and land loans was commercial construction, which grew \$144.3 million during the nine months ended September 30, 2016. At September 30, 2016, multi-family residential construction loans totaled approximately \$194.2 million, or 38% of the commercial construction loan portfolio.

| (Dollars in thousands)                          | September 30,<br>2016 | % of<br>Total<br>Loans | % of<br>Total<br>Loans | December 31,<br>2015 | % of<br>Total<br>Loans | % of<br>Total<br>Loans |
|---|-----------------------|------------------------|------------------------|----------------------|------------------------|------------------------|
| Residential land and land development           | \$ 87,891             | 11.0                   | %.7                    | \$ 72,622            | 11.6                   | %.6                    |
| Residential construction                        | 146,419               | 18.2                   | 1.1                    | 131,943              | 21.2                   | 1.1                    |
| Commercial land and land development            | 56,587                | 7.1                    | .4                     | 54,176               | 8.7                    | .4                     |
| Commercial construction                         | 509,648               | 63.7                   | 3.9                    | 365,329              | 58.5                   | 2.9                    |
| Total real estate - construction and land loans | \$ 800,545            | 100.0                  | 6.1                    | \$ 624,070           | 100.0                  | 5.0                    |

## Real Estate – Business Loans

Total business real estate loans were \$2.5 billion at September 30, 2016 and comprised 19.1% 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 September 30, 2016, 40.3% of business real estate loans were for owner-occupied real estate properties, which present lower risk profiles.

| (Dollars in thousands)             | September 30,<br>2016 | % of<br>Total<br>Loans | % of<br>Total<br>Loans | December 31,<br>2015 | % of<br>Total<br>Loans | % of<br>Total<br>Loans |
|------------------------------------|-----------------------|------------------------|------------------------|----------------------|------------------------|------------------------|
| Owner-occupied                     | \$ 1,016,937          | 40.3                   | %.7                    | \$ 983,844           | 41.8                   | %.9                    |
| Retail                             | 327,646               | 13.0                   | 2.5                    | 322,644              | 13.7                   | 2.6                    |
| Multi-family                       | 247,352               | 9.8                    | 1.9                    | 196,212              | 8.3                    | 1.6                    |
| Office                             | 221,599               | 8.8                    | 1.7                    | 218,018              | 9.3                    | 1.8                    |
| Farm                               | 171,525               | 6.8                    | 1.3                    | 167,344              | 7.1                    | 1.3                    |
| Hotels                             | 168,985               | 6.7                    | 1.2                    | 157,317              | 6.7                    | 1.2                    |
| Industrial                         | 118,897               | 4.8                    | .9                     | 112,261              | 4.7                    | .9                     |
| Other                              | 247,587               | 9.8                    | 1.9                    | 197,904              | 8.4                    | 1.6                    |
| Total real estate - business loans | \$ 2,520,528          | 100.0                  | 19.1                   | \$ 2,355,544         | 100.0                  | 18.9                   |

## Real Estate – Personal Loans

The Company's \$2.0 billion personal real estate loan portfolio is composed mainly of residential first mortgage real estate loans. As shown on page 44, recent loss rates have remained low, and at September 30, 2016, loans past due over 30 days decreased \$716 thousand and non-accrual loans decreased \$791 thousand compared to December 31, 2015. Also, as shown in Note 2, only 4.4% of this portfolio has FICO scores of less than 660. Approximately \$20.1 million, or 1.0%, 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 at origination or have additional collateral pledged to secure the loan. Therefore, they are not perceived to represent above normal credit risk. Loans originated with interest only payments were not made to "qualify" the borrower for a lower payment amount. At September 30, 2016, loans with no mortgage insurance and an original LTV higher than 80% totaled \$158.2 million compared to \$146.8 million at December 31, 2015.

### Revolving Home Equity Loans

The Company had \$417.6 million in revolving home equity loans at September 30, 2016 that were generally collateralized by residential real estate. Most of these loans (93.0%) 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 September 30, 2016, the outstanding principal of loans with an original LTV higher than 80% was \$54.4 million, or 13.0% of the portfolio, compared to \$68.1 million as of December 31, 2015. Total revolving home equity loan balances over 30 days past due or on non-accrual status were \$3.3 million at September 30, 2016 compared to \$5.0 million at December 31, 2015. The weighted average FICO score for the total current portfolio balance is 775. 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 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 the remainder of 2016 through 2018, approximately 23% of the Company's current outstanding balances are expected to mature. Of these

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balances, approximately 83% have a FICO score of 700 or higher. 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.

**Other Consumer Loans**

Within the consumer loan portfolio are several direct and indirect product lines, which include loans for the purchase of automobiles, marine and RVs. Outstanding balances for auto loans were \$986.1 million and \$996.0 million at September 30, 2016 and December 31, 2015, respectively. The balances over 30 days past due amounted to \$10.4 million at September 30, 2016 compared to \$10.8 million at the end of 2015, and comprised 1.1% of the outstanding balances of these loans at both September 30, 2016 and December 31, 2015. For the nine months ended September 30, 2016, \$349.1 million of new auto loans were originated, compared to \$497.2 million during the full year of 2015. At September 30, 2016, the automobile loan portfolio had a weighted average FICO score of 732.

The Company's balance of marine and RV loans totaled \$110.8 million at September 30, 2016, compared to \$143.1 million at December 31, 2015, and the balances over 30 days past due amounted to \$2.7 million at September 30, 2016 compared to \$5.1 million at the end of 2015. The net charge-offs on marine and RV loans declined from \$1.6 million in the first nine months of 2015, to \$858 thousand in the first nine months of the current year.

Additionally, the Company offers low promotional rates on selected consumer credit card products. Out of a portfolio at September 30, 2016 of \$760.0 million in consumer credit card loans outstanding, approximately \$169.0 million, or 22.2%, carried a low promotional rate. Within the next six months, \$50.3 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.

**Energy Lending**

The Company's energy lending portfolio was comprised of lending to the petroleum and natural gas sectors and totaled \$145.4 million at September 30, 2016, as shown in the table below. As of September 30, 2016, there were \$22.8 million of energy loans, or 15.7% of the energy portfolio, with a "substandard" rating or on non-accrual status, compared to \$4.4 million, or 3.2% of the energy portfolio, at December 31, 2015. Of these amounts, non-accrual loans in the energy portfolio totaled \$1.0 million at September 30, 2016, compared to \$114.3 thousand at December 31, 2015. There were no energy loans 90 days past due and still accruing interest at both September 30, 2016 and December 31, 2015.

| (In thousands)                       | September 30, December 31, |            | Unfunded                                |
|--------------------------------------|----------------------------|------------|---|
|                                      | 2016                       | 2015       | commitments<br>at September<br>30, 2016 |
| Extraction                           | \$ 81,276                  | \$ 65,649  | \$ 33,097                               |
| Downstream distribution and refining | 21,602                     | 27,246     | 27,413                                  |
| Mid-stream shipping and storage      | 27,145                     | 28,678     | 45,774                                  |
| Support activities                   | 15,423                     | 14,946     | 8,205                                   |
| Total energy lending portfolio       | \$ 145,446                 | \$ 136,519 | \$ 114,489                              |

**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 \$880.7 million at September 30, 2016, compared to \$656.0 million at December 31, 2015. Additional unfunded commitments at September 30, 2016 totaled \$1.4 billion.

#### Income Taxes

Income tax expense was \$30.9 million in the third quarter of 2016, compared to \$31.5 million in the second quarter of 2016 and \$28.0 million in the third quarter of 2015. The Company's effective tax rate, including the effect of non-controlling interest, was 31.1% in both the second and third quarters of 2016, compared to 30.2% in the third quarter of 2015. Income tax expense for the first nine months of 2016 was \$91.9 million, compared to \$88.9 million for the same period during the previous year, resulting in effective tax rates of 31.1% and 30.8%, respectively. The increase in the effective tax rate for the three and nine months ended September 30, 2016 compared to the same periods in 2015 was primarily driven by higher state and local taxes.

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### Financial Condition

#### Balance Sheet

Total assets of the Company were \$24.7 billion at September 30, 2016 and \$24.6 billion at December 31, 2015. Earning assets (excluding the allowance for loan losses and fair value adjustments on investment securities) amounted to \$23.4 billion at September 30, 2016 and \$23.2 billion at December 31, 2015. The balance at September 30, 2016 was comprised of 57% in loans and 40% in investment securities.

At September 30, 2016, total loans, including those held for sale, increased \$795.5 million, or 6.4%, compared with balances at December 31, 2015. On an overall basis, the largest contributions to loan growth occurred in business loans, construction loans, and business real estate loans, which increased \$373.0 million, \$176.5 million, and \$165.0 million, respectively, over year end balances. The increase in business loans mainly resulted from growth in commercial and industrial loans and commercial credit card loans. Commercial construction projects contributed to the growth in construction loans. The increase in business real estate loans largely resulted from growth in owner-occupied and multi-family residential projects. Consumer loans, which includes automobile, marine and RV, fixed rate home equity, and other consumer loans, increased \$48.6 million during the first nine months of the year. Outstanding balances of automobile and other consumer loans grew by \$72.1 million, however, \$33.6 million of auto loans were sold in the second and third quarters of this year, in order to limit risk in the auto sector of the loan portfolio. Fixed rate home equity loans also grew by \$8.8 million. However, marine and RV loans continued to run off during the period by \$32.3 million. Personal real estate loans grew \$52.1 million during the first nine months of 2016; however, the Company originated and sold an additional \$107.9 million of longer-term fixed rate loans during this period. Declines in consumer credit card (down \$19.7 million) and revolving home equity loans (down \$15.4 million) partially offset growth throughout the year.

Available for sale investment securities, excluding fair value adjustments, decreased by \$479.3 million at September 30, 2016 compared to December 31, 2015. Purchases of securities during this period totaled \$1.2 billion, offset by maturities and pay downs of \$1.7 billion. The largest decreases in outstanding balances occurred in government-sponsored enterprise obligations, which decreased by \$349.3 million, and asset-backed securities, which decreased by \$257.2 million. At September 30, 2016, the duration of the investment portfolio was 2.7 years, and maturities and pay downs of approximately \$1.6 billion are expected to occur during the next 12 months.

Total deposits at September 30, 2016 amounted to \$20.2 billion and increased \$187.3 million compared to December 31, 2015. The growth of deposits was primarily driven by increases in money market and savings deposits, which grew by \$364.0 million (4.1%) and \$34.9 million (4.7%), respectively. Total C.D. and time deposit accounts increased \$14.5 million, or .7%. These increases were partially offset by decreases in interest checking balances of \$210.1 million, or 16.6%, and non-interest bearing deposits of \$16.0 million, or .2%. The decline in non-interest bearing deposits included reductions of \$363.4 million in business accounts, partially offset by an increase of \$360.2 million in government accounts.

Total borrowings were \$1.6 billion at September 30, 2016 compared to \$2.1 billion at December 31, 2015. Short-term borrowings of federal funds purchased and customer repurchase agreements totaled \$1.5 billion at September 30, 2016, a decrease of \$473.7 million from balances of \$2.0 billion at December 31, 2015. The overall decrease in these balances was due to decreases of \$263.3 million in federal funds purchased and \$210.3 million in customer 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 (resale agreements), and balances at the Federal Reserve Bank, as follows:

| (In thousands)  | September 30,<br>2016 | June 30,<br>2016 | December 31,<br>2015 |
|---|-----------------------|------------------|----------------------|
| Liquid assets:  |                       |                  |                      |
| Available for sale investment securities                  | \$ 9,438,871          | \$ 9,221,346     | \$ 9,777,004         |
| Federal funds sold  | 13,415                | 13,725           | 14,505               |
| Long-term securities purchased under agreements to resell | 725,000               | 825,000          | 875,000              |
| Balances at the Federal Reserve Bank                      | 56,767                | 183,223          | 23,803               |
| Total   | \$ 10,234,053         | \$ 10,243,294    | \$ 10,690,312        |

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Federal funds sold, which are funds lent to the Company's correspondent bank customers with overnight maturities, totaled \$13.4 million as of September 30, 2016. Long-term resale agreements, maturing in 2016 through 2018, totaled \$725.0 million at September 30, 2016. Under these agreements, the Company lends funds to upstream financial institutions and holds marketable securities, safe-kept by a third-party custodian, as collateral. This collateral totaled \$763.6 million in fair value at September 30, 2016. Interest earning balances at the Federal Reserve Bank, which have overnight maturities and are used for general liquidity purposes, totaled \$56.8 million at September 30, 2016. The fair value of the available for sale investment portfolio was \$9.4 billion at September 30, 2016 and included an unrealized net gain in fair value of \$226.8 million. The total net unrealized gain included net gains of \$94.0 million on mortgage and asset-backed securities, \$59.1 million on state and municipal obligations, and \$41.2 million on common and preferred stock held by the Parent.

Approximately \$1.6 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)   | September 30,<br>2016 | June 30,<br>2016 | December 31,<br>2015 |
|--|-----------------------|------------------|----------------------|
| Investment securities pledged for the purpose of securing: |                       |                  |                      |
| Federal Reserve Bank borrowings                            | \$ 128,595            | \$ 138,547       | \$ 166,153           |
| FHLB borrowings and letters of credit                      | 20,072                | 25,757           | 31,095               |
| Securities sold under agreements to repurchase             | 1,929,642             | 2,332,313        | 2,116,537            |
| Other deposits and swaps                                   | 1,934,892             | 2,055,453        | 1,827,195            |
| Total pledged securities                                   | 4,013,201             | 4,552,070        | 4,140,980            |
| Unpledged and available for pledging                       | 3,492,423             | 2,833,345        | 3,886,219            |
| Ineligible for pledging                                    | 1,933,247             | 1,835,931        | 1,749,805            |
| Total available for sale securities, at fair value         | \$ 9,438,871          | \$ 9,221,346     | \$ 9,777,004         |

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 September 30, 2016, such deposits totaled \$18.2 billion and represented 90.0% 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 \$1.3 billion at September 30, 2016. These accounts are normally considered more volatile and higher costing and comprised 6.3% of total deposits at September 30, 2016.

| (In thousands)           | September 30,<br>2016 | June 30,<br>2016 | December 31,<br>2015 |
|--------------------------|-----------------------|------------------|----------------------|
| Core deposit base:       |                       |                  |                      |
| Non-interest bearing     | \$ 7,130,415          | \$ 6,906,265     | \$ 7,146,398         |
| Interest checking        | 1,057,662             | 1,088,540        | 1,267,757            |
| Savings and money market | 9,965,864             | 9,890,194        | 9,566,989            |
| Total                    | \$ 18,153,941         | \$ 17,884,999    | \$ 17,981,144        |

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)

|  | September 30,<br>2016 | June 30,<br>2016 | December 31,<br>2015 |
|--|-----------------------|------------------|----------------------|
| Borrowings:                                    |                       |                  |                      |
| Federal funds purchased                        | \$ 293,640            | \$ 31,810        | \$ 556,970           |
| Securities sold under agreements to repurchase | 1,196,251             | 1,600,462        | 1,406,582            |
| FHLB advances                                  | 100,000               | 103,000          | 103,818              |
| Other debt                                     | 1,415                 | 878              | —                    |
| Total  | \$ 1,591,306          | \$ 1,736,150     | \$ 2,067,370         |

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 non-insured customer funds totaling \$1.2 billion, which generally mature

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overnight. The Company also borrows on a secured basis through advances from the FHLB, which totaled \$100.0 million at September 30, 2016. These advances have fixed interest rates and mature in 2017.

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 September 30, 2016.

| (In thousands)                | September 30, 2016 |                 |             |
|-------------------------------|--------------------|-----------------|-------------|
|                               | FHLB               | Federal Reserve | Total       |
| Collateral value pledged      | \$2,556,157        | \$1,295,944     | \$3,852,101 |
| Advances outstanding          | (100,000 )         | —               | (100,000 )  |
| Letters of credit issued      | (210,200 )         | —               | (210,200 )  |
| Available for future advances | \$2,245,957        | \$1,295,944     | \$3,541,901 |

In addition to those mentioned above, several other sources of liquidity are available. 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. The Company receives strong outside rankings from both Standard & Poor's and Moody's on both the consolidated company level and its subsidiary bank, Commerce Bank, which would support future financing efforts, should the need arise. These ratings are as follows:

## Standard &amp; Poor's Moody's

## Commerce Bancshares, Inc.

|                            |        |        |
|----------------------------|--------|--------|
| Issuer rating              | A-     |        |
| Preferred stock            | BBB-   | Baa1   |
| Rating outlook             | Stable | Stable |
| Commerce Bank              |        |        |
| Issuer rating              | A      | A2     |
| Baseline credit assessment |        | a1     |
| Short-term rating          | A-1    | P-1    |
| Rating outlook             | Stable | Stable |

The cash flows from the operating, investing and financing activities of the Company resulted in a net decrease in cash and cash equivalents of \$35.6 million during the first nine months of 2016, 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 \$346.2 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 \$92.8 million. These activities included \$1.7 billion in maturities and pay downs of investment securities, offset by purchases of \$1.1 billion, and a net increase in loans of \$817.9 million. Additionally, repayments of long-term securities purchased under agreements to resell provided cash of \$150.0 million. Financing activities used cash of \$289.0 million, resulting from a net decrease in borrowings of federal funds purchased and securities sold under agreements to repurchase of \$473.7 million. In addition, cash was used to fund dividends paid on common and preferred stock of \$72.0 million, and \$38.5 million was used to purchase treasury stock. These cash outlays were partially offset by a net increase of

\$295.0 million in deposits. 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.

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## Capital Management

The Company met all capital adequacy requirements and had regulatory capital ratios in excess of the levels established for well-capitalized institutions at September 30, 2016 and December 31, 2015, as shown in the following table.

| (Dollars in thousands)                 | September 30,<br>2016 | December 31,<br>2015 | Minimum<br>Ratios<br>under<br>Capital<br>Adequacy<br>Guidelines<br>* | Minimum Ratios<br>for<br>Well-Capitalized<br>Banks ** |   |
|--|-----------------------|----------------------|--|---|---|
| Risk-adjusted assets                   | \$18,492,932          | \$17,809,554         |  |   |   |
| Tier I common risk-based capital       | 2,156,611             | 2,051,474            |  |   |   |
| Tier I risk-based capital              | 2,301,395             | 2,196,258            |  |   |   |
| Total risk-based capital               | 2,475,579             | 2,364,761            |  |   |   |
| Tier I common risk-based capital ratio | 11.66                 | % 11.52              | % 7.00   | % 6.50  | % |
| Tier I risk-based capital ratio        | 12.44                 | % 12.33              | % 8.50   | % 8.00  | % |
| Total risk-based capital ratio         | 13.39                 | % 13.28              | % 10.50  | % 10.00   | % |
| Tier I leverage ratio                  | 9.58                  | % 9.23               | % 4.00   | % 5.00  | % |

\* as of the fully phased-in date of Jan. 1, 2019, including capital conservation buffer

\*\*under Prompt Corrective Action requirements

The Company maintains a treasury stock buyback program under authorizations by its Board of Directors and normally purchases stock in the open market. The Company purchased 943,428 shares at an average price of \$40.78 during the nine months ended September 30, 2016, including 20,730 shares at an average price of \$48.90 during the third quarter of 2016. Additionally, the Company purchased 6.7 million shares through accelerated share repurchase agreements during 2015 and 2014. At September 30, 2016, 3.8 million shares remained available for purchase under the current Board authorization.

The Company's common stock dividend policy reflects its earnings outlook, desired payout ratios, the need to maintain adequate capital and liquidity levels, and alternative investment options. The Company paid a \$.225 per share cash dividend on its common stock in each of the first three quarters of 2016, which was a 5% increase compared to its 2015 quarterly dividend.

## 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 September 30, 2016 totaled \$10.4 billion (including approximately \$5.0 billion in unused approved credit card lines). In addition, the Company enters into standby and commercial letters of credit. These contracts totaled \$352.1 million and \$2.9 million, respectively, at September 30, 2016. 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 consolidated balance sheet, amounted to \$2.4 million at September 30, 2016.

The Company regularly purchases various state tax credits arising from third-party property redevelopment. These credits are either resold to third parties at a profit or retained for use by the Company. During the first nine months of 2016, purchases and sales of tax credits amounted to \$27.3 million and \$19.1 million, respectively. Fees from sales of tax credits were \$2.4 million for the nine months ended September 30, 2016, compared to \$1.6 million in the same period last year. At September 30, 2016, the Company expected to fund outstanding purchase commitments of \$48.6 million during the remainder of 2016 and \$99.7 million in 2017.

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## Segment Results

The table below is a summary of segment pre-tax income results for the first nine months of 2016 and 2015.

| (Dollars in thousands)                             | Consumer   | Commercial | Wealth    | Segment<br>Totals | Other/<br>Elimination | Consolidated<br>Totals |
|--|------------|------------|-----------|-------------------|-----------------------|------------------------|
| Nine Months Ended September 30, 2016               |            |            |           |                   |                       |                        |
| Net interest income                                | \$201,166  | \$231,552  | \$32,604  | \$465,322         | \$41,525              | \$506,847              |
| Provision for loan losses                          | (26,533 )  | 3,919      | (120 )    | (22,734 )         | (3,184 )              | (25,918 )              |
| Non-interest income                                | 97,165     | 149,240    | 107,696   | 354,101           | 812                   | 354,913                |
| Investment securities losses, net                  | —          | —          | —         | —                 | (3,704 )              | (3,704 )               |
| Non-interest expense                               | (209,649 ) | (211,961 ) | (85,025 ) | (506,635 )        | (29,169 )             | (535,804 )             |
| Income before income taxes                         | \$62,149   | \$172,750  | \$55,155  | \$290,054         | \$6,280               | \$296,334              |
| Nine Months Ended September 30, 2015               |            |            |           |                   |                       |                        |
| Net interest income                                | \$199,265  | \$218,699  | \$31,921  | \$449,885         | \$21,948              | \$471,833              |
| Provision for loan losses                          | (25,500 )  | 842        | 114       | (24,544 )         | 5,003                 | (19,541 )              |
| Non-interest income                                | 87,462     | 144,685    | 102,517   | 334,664           | (2,567 )              | 332,097                |
| Investment securities gains, net                   | —          | —          | —         | —                 | 7,800                 | 7,800                  |
| Non-interest expense                               | (203,440 ) | (199,097 ) | (81,432 ) | (483,969 )        | (16,741 )             | (500,710 )             |
| Income before income taxes                         | \$57,787   | \$165,129  | \$53,120  | \$276,036         | \$15,443              | \$291,479              |
| Increase (decrease) in income before income taxes: |            |            |           |                   |                       |                        |
| Amount   | \$4,362    | \$7,621    | \$2,035   | \$14,018          | \$(9,163 )            | \$4,855                |
| Percent  | 7.5        | %4.6       | %3.8      | %5.1              | %(59.3 )              | %1.7                   |

## Consumer

For the nine months ended September 30, 2016, income before income taxes for the Consumer segment increased \$4.4 million, or 7.5%, compared to the first nine months of 2015. This increase was mainly due to growth in non-interest income of \$9.7 million, or 11.1%, and net interest income of \$1.9 million, or 1.0%. These increases were partly offset by higher non-interest expense of \$6.2 million, or 3.1%, and an increase in the provision for loan losses of \$1.0 million, or 4.1%. Net interest income increased due to a \$3.1 million increase in net allocated funding credits assigned to the Consumer segment's loan and deposit portfolios, partly offset by a decline of \$1.4 million in loan interest income. Non-interest income increased mainly due to growth in deposit fees (mainly deposit account service fees and overdraft and return item fees), mortgage banking revenue and bank card fees. Non-interest expense increased over the same period in the previous year due to higher bank card processing costs, bank card rewards expense, and supplies and communication expense. Supplies and communication expense increased over the prior year largely due to higher reissuance costs for new chip cards distributed to customers. In addition, higher costs were incurred for allocated support services, while bank card fraud losses declined from the prior year. The provision for loan losses totaled \$26.5 million, a \$1.0 million increase over the first nine months of 2015, which was mainly due to higher personal loan net charge-offs resulting from growth in the auto loan portfolio, partly offset by lower marine and RV loan net charge-offs.

## Commercial

For the nine months ended September 30, 2016, income before income taxes for the Commercial segment increased \$7.6 million, or 4.6%, compared to the same period in the previous year. This increase was mainly due to growth in net interest income and non-interest income, along with a decline in the provision for loan losses, and was partly offset by higher non-interest expense. Net interest income increased \$12.9 million, or 5.9%, due to an increase in loan



interest income, partly offset by a decline in net allocated funding credits and higher deposit interest expense. Non-interest income increased \$4.6 million, or 3.1%, over the previous year due to growth in bank card fees, corporate cash management fees, sweep commissions and tax credit sales fees. These increases were partly offset by a decline in leasing revenue. Non-interest expense increased \$12.9 million, or 6.5%, mainly due to increases in salaries expense, bank card processing costs, and allocated support and corporate costs. Also contributing to higher non-interest expense was a recovery of \$2.8 million in 2015 related to a letter of credit exposure which had been drawn upon and subsequently paid off. These increases were partly offset by declines in operating lease depreciation and allocated servicing costs. The provision for loan losses declined \$3.1 million from the same period last year, due to higher net recoveries on business real estate and construction loans.

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### Wealth

Wealth segment pre-tax profitability for the nine months ended September 30, 2016 increased \$2.0 million, or 3.8%, over the same period in the previous year. Net interest income increased \$683 thousand, mainly due to an increase in loan interest income, partly offset by lower net allocated funding credits. Non-interest income increased \$5.2 million, or 5.1%, over the prior year largely due to higher personal and institutional trust fees, cash sweep fees and a trust related settlement. Non-interest expense increased \$3.6 million, or 4.4%, mainly due to higher full-time salary costs and incentive compensation. The provision for loan losses increased \$234 thousand, mainly due to higher personal real estate and revolving home equity loan net charge-offs.

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 procedures, 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 \$9.2 million. This decrease was partly due to higher unallocated non-interest expense of \$12.4 million, offset by higher net interest income of \$19.6 million and non-interest income of \$3.4 million. Unallocated securities losses were \$3.7 million in the first nine months of 2016 compared to gains of \$7.8 million in 2015. Also, the unallocated loan loss provision increased \$8.2 million, as the provision was \$5.0 million less than charge-offs in the first nine months of 2015 compared to \$3.0 million in excess of charge-offs in the first nine months of 2016.

### Regulatory Changes Affecting the Banking Industry

In accordance with the Dodd-Frank Act, the Company began submitting its stress test results to the Federal Reserve in March 2014 and publicly disclosed the results of its stress testing for the first time in June 2015. In 2016, the Company submitted its stress test report to the Federal Reserve in July and publicly disclosed the results in October.

The Volcker Rule of the Dodd-Frank Act, effective on April 1, 2014, places trading restrictions on financial institutions and separates investment banking, private equity and proprietary trading (hedge fund) sections of financial institutions from their consumer lending arms. Key provisions restrict banks from simultaneously entering into advisory and creditor roles with their clients, such as with private equity firms. The Volcker Rule also restricts financial institutions from investing in and sponsoring certain types of investments, which must be divested by July 21, 2017. The Company withdrew from a private equity fund investment to comply with the Volcker Rule requirement in the previous quarter and realized a gain of \$1.8 million upon divestiture. The Company does not hold other significant investments requiring disposal.

### Impact of Recently Issued Accounting Standards

**Revenue from Contracts with Customers** The FASB issued ASU 2014-09, "Revenue from Contracts with Customers", in May 2014. The ASU supersedes revenue recognition requirements in Topic 605, Revenue Recognition, including most industry-specific revenue recognition guidance in the FASB Accounting Standards Codification. The core principle of the new guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance identifies specific steps that entities should apply in order to achieve this principle. The FASB continues to issue additional ASU's clarifying the revenue recognition guidance for certain implementation issues. Under the ASU and related amendments, the guidance is effective for interim and annual periods beginning January 1, 2018 and must be applied retrospectively. The Company formed a working group to address the new requirements and develop a project plan for evaluating the impact of the ASU's

adoption on the Company's consolidated financial statements, with a focus on the Company's accounting for brokerage commissions, trust fees, cash management fees, real-estate sales, and credit card revenue.

**Derivatives** The FASB issued ASU 2014-16, "Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or to Equity", in November 2014. The ASU provides guidance relating to certain hybrid financial instruments when determining whether the characteristics of the embedded derivative feature are clearly and closely related to the host contract. In making that evaluation, the characteristics of the entire hybrid instrument should be considered, including the embedded derivative feature that is being evaluated for separate accounting from the host contract. The amendments were effective January 1, 2016, and the adoption did not have a significant effect on the Company's consolidated financial statements.

In March 2016, the FASB issued ASU 2016-05, "Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships", which clarifies that a change in the counterparty to a derivative instruments that has been designated as the hedging instrument does not, in and of itself, require dedesignation of that hedging relationship provided that all other hedge accounting

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criteria continue to be met. The amendments are effective January 1, 2017 and are not expected to have a significant effect on the Company's consolidated financial statements.

The FASB issued ASU 2016-06, "Contingent Put and Call Options in Debt Instruments", in March 2016. The ASU clarifies the requirements for assessing whether contingent call (put) options that can accelerate the payment of principal on debt instruments are clearly and closely related to their debt hosts. Under the new guidance, the embedded options should be assessed solely in accordance with a four-step decision sequence, with no additional assessment of whether the triggering event is indexed to interest rates or credit risk. The amendments are effective January 1, 2017 and are not expected to have a significant effect on the Company's consolidated financial statements.

**Consolidation** The FASB issued ASU 2015-02, "Amendments to the Consolidation Analysis", in February 2015. The amendments require an evaluation of whether certain legal entities should be consolidated and modify the evaluation of whether limited partnerships and similar legal entities are variable interest entities or voting interest entities. The amendments were effective for interim and annual periods beginning January 1, 2016. The adoption did not have a significant effect on the Company's consolidated financial statements.

**Intangible Assets** The FASB issued ASU 2015-05, "Customer's Accounting for Fees Paid in a Cloud Computing Arrangement", in April 2015. The amendments provide guidance to customers about whether a cloud computing arrangement includes a software license. Arrangements containing a license should be recorded as consistent with the acquisition of software licenses, whereas arrangements that do not include a software license should be recorded as consistent with the accounting for service contracts. These amendments were effective for interim and annual periods beginning January 1, 2016. The adoption did not have a significant effect on the Company's consolidated financial statements.

**Financial Instruments** The FASB issued ASU 2016-01, "Recognition and Measurement of Financial Assets and Financial Liabilities", in January 2016. The amendments require all equity investments to be measured at fair value with changes in the fair value recognized through net income, other than those accounted for under the equity method of accounting or those that result in the consolidation of the investee. Additionally, these amendments require presentation in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk for those liabilities measured at fair value. The amendments also require use of the exit price notion when measuring the fair value of financial instruments for disclosure purposes. These amendments are effective for interim and annual periods beginning January 1, 2018. The Company is in the process of evaluating the impact of the ASU's adoption on the Company's consolidated financial statements, including potential changes to the Company's note disclosure of the fair value of its loan portfolio.

ASU 2016-13, "Measurement of Credit Losses on Financial Instruments", was issued in June 2016. Its implementation will result in a new loan loss accounting framework, also known as the current expected credit loss (CECL) model. CECL requires credit losses expected throughout the life of the asset portfolio on loans and held-to-maturity securities to be recorded at the time of origination. Under the current incurred loss model, losses are recorded when it is probable that a loss event has occurred. The new standard will require significant operational changes, especially in data collection and analysis. The ASU is effective for interim and annual periods beginning January 1, 2020, and is expected to increase the allowance upon adoption. The Company is in the process of reviewing the capability of its systems and processes to support the data collection and retention required to implement the new standard.

**Leases** In February 2016, the FASB issued ASU 2016-02, "Leases", in order to increase transparency and comparability by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The ASU primarily affects lessee accounting, which requires the lessee to recognize a right-of-use asset and a liability to make lease payments for those leases classified as operating leases under previous

GAAP. For leases with a term of 12 months or less, an election by class of underlying asset not to recognize lease assets and lease liabilities is permitted. The ASU also provides additional guidance as to the definition of a lease, identification of lease components, and sale and leaseback transactions. The amendments in the ASU are effective for interim and annual periods beginning January 1, 2019. The Company is in the process of evaluating the impact of the ASU's adoption on the Company's consolidated financial statements.

Liabilities The FASB issued ASU 2016-04, "Recognition of Breakage for Certain Prepaid Store-Value Products", in March 2016, in order to address current and potential future diversity in practice related to the derecognition of a prepaid store-value product liability. Such products include prepaid gift cards issued on a specific payment network and redeemable at network-accepting merchant locations, prepaid telecommunication cards, and traveler's checks. The amendments require that the portion of the dollar value of prepaid stored-value products that is ultimately unredeemed (that is, the breakage) be accounted for consistent with the breakage guidance for stored-value product transactions provided in ASC Topic 606 - Revenue from Contracts with Customers. These amendments are effective for interim and annual periods beginning January 1, 2018. The Company is in the process of evaluating the impact of the ASU's adoption on the Company's consolidated financial statements.

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**Investments** The FASB issued ASU 2016-07, "Equity Method and Joint Ventures", in March 2016, which eliminates the requirement that an entity retroactively adopt the equity method of accounting if an investment qualifies for use of the equity method as a result of an increase in ownership or influence. Instead, the cost of acquiring the additional interest should be added to the current basis of the previously held interest, and equity method accounting applied prospectively. The amendments are effective January 1, 2017 and are not expected to have a significant effect on the Company's consolidated financial statements.

**Stock Compensation** The FASB issued ASU 2016-09, "Improvements to Employee Share-Based Payment Accounting", in March 2016, in order to reduce complexity in this area and improve the usefulness of information provided to users. Amendments which will affect public companies include the recognition of excess tax benefits and deficiencies in income tax expense or benefit in the income statement, guidance as to the classification of excess tax benefits on the the statement of cash flows, an election to account for award forfeitures as they occur, and the ability to withhold taxes up to the maximum statutory rate in the applicable jurisdictions without triggering liability classification of the award. The amendments are effective January 1, 2017. At this time, the Company expects to elect to account for forfeitures as they occur. The effect of this election and other amendments are not expected to have a significant effect on the Company's consolidated financial statements.

**Statement of Cash Flows** The FASB issued ASU 2016-15, "Classification of Certain Cash Receipts and Cash Payments", in August 2016. The ASU addresses the presentation and classification in the Statement of Cash Flows of several specific cash flow issues. These include cash payments for debt prepayment or extinguishment costs, settlement of zero-coupon debt instruments, distributions received from equity method investees, and separately identifiable cash flows and application of the predominance principle. The amendments are effective January 1, 2018 and are 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 September 30, 2016 and 2015

| (Dollars in thousands)                                    | Third Quarter 2016 |                         |                        | Third Quarter 2015 |                         |                        |
|---|--------------------|-------------------------|------------------------|--------------------|-------------------------|------------------------|
|   | Average Balance    | Interest Income/Expense | Avg. Rates Earned/Paid | Average Balance    | Interest Income/Expense | Avg. Rates Earned/Paid |
| <b>ASSETS:</b>  |                    |                         |                        |                    |                         |                        |
| <b>Loans:</b>   |                    |                         |                        |                    |                         |                        |
| Business <sup>(A)</sup>                                   | \$4,694,340        | \$ 33,924               | 2.87 %                 | \$4,221,478        | \$ 29,101               | 2.73 %                 |
| Real estate — construction and land                       | 821,422            | 7,184                   | 3.48                   | 476,331            | 4,227                   | 3.52                   |
| Real estate — business                                    | 2,432,325          | 22,195                  | 3.63                   | 2,284,928          | 21,368                  | 3.71                   |
| Real estate — personal                                    | 1,943,951          | 18,249                  | 3.73                   | 1,911,469          | 17,961                  | 3.73                   |
| Consumer  | 1,947,956          | 19,122                  | 3.91                   | 1,861,636          | 18,786                  | 4.00                   |
| Revolving home equity                                     | 411,832            | 3,690                   | 3.56                   | 434,355            | 3,829                   | 3.50                   |
| Consumer credit card                                      | 750,412            | 21,804                  | 11.56                  | 746,066            | 21,797                  | 11.59                  |
| Overdrafts  | 4,652              | —                       | —                      | 5,233              | —                       | —                      |
| Total loans   | 13,006,890         | 126,168                 | 3.86                   | 11,941,496         | 117,069                 | 3.89                   |
| Loans held for sale                                       | 26,597             | 334                     | 5.00                   | 4,471              | 48                      | 4.26                   |
| <b>Investment securities:</b>                             |                    |                         |                        |                    |                         |                        |
| U.S. government and federal agency obligations            | 726,469            | 4,436                   | 2.43                   | 402,591            | 4,453                   | 4.39                   |
| Government-sponsored enterprise obligations               | 481,573            | 2,710                   | 2.24                   | 887,631            | 3,949                   | 1.77                   |
| State and municipal obligations <sup>(A)</sup>            | 1,747,794          | 15,821                  | 3.60                   | 1,805,931          | 15,676                  | 3.44                   |
| Mortgage-backed securities                                | 3,366,292          | 20,099                  | 2.38                   | 3,217,589          | 20,053                  | 2.47                   |
| Asset-backed securities                                   | 2,340,783          | 8,698                   | 1.48                   | 2,546,982          | 7,388                   | 1.15                   |
| Other marketable securities <sup>(A)</sup>                | 334,747            | 2,307                   | 2.74                   | 302,323            | 2,023                   | 2.65                   |
| Trading securities <sup>(A)</sup>                         | 18,433             | 112                     | 2.42                   | 22,283             | 153                     | 2.72                   |
| Non-marketable securities <sup>(A)</sup>                  | 113,954            | 2,932                   | 10.24                  | 114,062            | 2,380                   | 8.28                   |
| Total investment securities                               | 9,130,045          | 57,115                  | 2.49                   | 9,299,392          | 56,075                  | 2.39                   |
| <b>Federal funds sold and short-term securities</b>       |                    |                         |                        |                    |                         |                        |
| purchased under agreements to resell                      | 13,054             | 20                      | .61                    | 21,012             | 21                      | .40                    |
| Long-term securities purchased under agreements to resell | 766,302            | 3,328                   | 1.73                   | 1,007,606          | 3,273                   | 1.29                   |
| Interest earning deposits with banks                      | 207,944            | 268                     | .51                    | 160,687            | 103                     | .25                    |
| Total interest earning assets                             | 23,150,832         | 187,233                 | 3.22                   | 22,434,664         | 176,589                 | 3.12                   |
| Allowance for loan losses                                 | (153,517 )         |                         |                        | (150,890 )         |                         |                        |
| Unrealized gain on investment securities                  | 235,169            |                         |                        | 118,404            |                         |                        |
| Cash and due from banks                                   | 362,130            |                         |                        | 367,143            |                         |                        |
| Land, buildings and equipment, net                        | 347,621            |                         |                        | 359,481            |                         |                        |
| Other assets  | 441,798            |                         |                        | 380,115            |                         |                        |
| Total assets  | \$24,384,033       |                         |                        | \$23,508,917       |                         |                        |
| <b>LIABILITIES AND EQUITY:</b>                            |                    |                         |                        |                    |                         |                        |
| <b>Interest bearing deposits:</b>                         |                    |                         |                        |                    |                         |                        |
| Savings   | \$778,663          | 239                     | .12                    | \$739,172          | 237                     | .13                    |
| Interest checking and money market                        | 10,210,744         | 3,380                   | .13                    | 9,619,621          | 3,119                   | .13                    |

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|   |              |            |      |              |            |      |   |
|---|--------------|------------|------|--------------|------------|------|---|
| Time open & C.D.'s of less than \$100,000   | 740,729      | 683        | .37  | 820,792      | 786        | .38  |   |
| Time open & C.D.'s of \$100,000 and over    | 1,435,001    | 2,186      | .61  | 1,171,617    | 1,554      | .53  |   |
| Total interest bearing deposits             | 13,165,137   | 6,488      | .20  | 12,351,202   | 5,696      | .18  |   |
| Borrowings:                                 |              |            |      |              |            |      |   |
| Federal funds purchased and securities sold |              |            |      |              |            |      |   |
| under agreements to repurchase              | 1,163,728    | 724        | .25  | 1,677,322    | 483        | .11  |   |
| Other borrowings                            | 102,769      | 906        | 3.51 | 103,875      | 898        | 3.43 |   |
| Total borrowings                            | 1,266,497    | 1,630      | .51  | 1,781,197    | 1,381      | .31  |   |
| Total interest bearing liabilities          | 14,431,634   | 8,118      | .22  | % 14,132,399 | 7,077      | .20  | % |
| Non-interest bearing deposits               | 7,096,218    |            |      | 6,781,592    |            |      |   |
| Other liabilities                           | 306,306      |            |      | 250,626      |            |      |   |
| Equity                                      | 2,549,875    |            |      | 2,344,300    |            |      |   |
| Total liabilities and equity                | \$24,384,033 |            |      | \$23,508,917 |            |      |   |
| Net interest margin (T/E)                   |              | \$ 179,115 |      |              | \$ 169,512 |      |   |
| Net yield on interest earning assets        |              |            | 3.08 | %            |            | 3.00 | % |

(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

Nine Months Ended September 30, 2016 and 2015

| (Dollars in thousands)                                    | Nine Months 2016 |                         |                        | Nine Months 2015 |                         |                        |
|---|------------------|-------------------------|------------------------|------------------|-------------------------|------------------------|
|   | Average Balance  | Interest Income/Expense | Avg. Rates Earned/Paid | Average Balance  | Interest Income/Expense | Avg. Rates Earned/Paid |
| <b>ASSETS:</b>  |                  |                         |                        |                  |                         |                        |
| <b>Loans:</b>   |                  |                         |                        |                  |                         |                        |
| Business <sup>(A)</sup>                                   | \$4,626,041      | \$ 99,879               | 2.88 %                 | \$4,130,276      | \$ 85,964               | 2.78 %                 |
| Real estate — construction and land                       | 764,644          | 19,934                  | 3.48                   | 441,307          | 12,048                  | 3.65                   |
| Real estate — business                                    | 2,401,310        | 66,070                  | 3.68                   | 2,284,875        | 64,240                  | 3.76                   |
| Real estate — personal                                    | 1,919,905        | 53,977                  | 3.76                   | 1,893,510        | 53,493                  | 3.78                   |
| Consumer  | 1,936,860        | 55,931                  | 3.86                   | 1,803,305        | 53,815                  | 3.99                   |
| Revolving home equity                                     | 418,214          | 11,138                  | 3.56                   | 431,522          | 11,536                  | 3.57                   |
| Consumer credit card                                      | 746,893          | 64,343                  | 11.51                  | 743,052          | 64,747                  | 11.65                  |
| Overdrafts  | 4,447            | —                       | —                      | 5,117            | —                       | —                      |
| Total loans   | 12,818,314       | 371,272                 | 3.87                   | 11,732,964       | 345,843                 | 3.94                   |
| Loans held for sale                                       | 30,728           | 1,161                   | 5.05                   | 3,440            | 108                     | 4.20                   |
| <b>Investment securities:</b>                             |                  |                         |                        |                  |                         |                        |
| U.S. government and federal agency obligations            | 709,414          | 11,176                  | 2.10                   | 427,488          | 4,928                   | 1.54                   |
| Government-sponsored enterprise obligations               | 640,888          | 11,446                  | 2.39                   | 977,183          | 13,403                  | 1.83                   |
| State and municipal obligations <sup>(A)</sup>            | 1,743,426        | 47,267                  | 3.62                   | 1,788,436        | 46,735                  | 3.49                   |
| Mortgage-backed securities                                | 3,395,053        | 60,827                  | 2.39                   | 3,106,760        | 59,587                  | 2.56                   |
| Asset-backed securities                                   | 2,418,370        | 26,087                  | 1.44                   | 2,840,011        | 21,474                  | 1.01                   |
| Other marketable securities <sup>(A)</sup>                | 338,221          | 7,008                   | 2.77                   | 237,863          | 4,630                   | 2.60                   |
| Trading securities <sup>(A)</sup>                         | 19,052           | 358                     | 2.51                   | 19,607           | 407                     | 2.78                   |
| Non-marketable securities <sup>(A)</sup>                  | 119,256          | 7,328                   | 8.21                   | 110,389          | 7,180                   | 8.70                   |
| Total investment securities                               | 9,383,680        | 171,497                 | 2.44                   | 9,507,737        | 158,344                 | 2.23                   |
| <b>Federal funds sold and short-term securities</b>       |                  |                         |                        |                  |                         |                        |
| purchased under agreements to resell                      | 14,112           | 63                      | .60                    | 15,338           | 45                      | .39                    |
| Long-term securities purchased under agreements to resell | 813,685          | 10,157                  | 1.67                   | 1,035,712        | 9,994                   | 1.29                   |
| Interest earning deposits with banks                      | 184,288          | 689                     | .50                    | 215,426          | 404                     | .25                    |
| Total interest earning assets                             | 23,244,807       | 554,839                 | 3.19                   | 22,510,617       | 514,738                 | 3.06                   |
| Allowance for loan losses                                 | (152,154 )       |                         |                        | (153,308 )       |                         |                        |
| Unrealized gain on investment securities                  | 192,175          |                         |                        | 152,456          |                         |                        |
| Cash and due from banks                                   | 384,985          |                         |                        | 378,839          |                         |                        |
| Land, buildings and equipment, net                        | 351,886          |                         |                        | 360,537          |                         |                        |
| Other assets  | 409,043          |                         |                        | 383,948          |                         |                        |
| Total assets  | \$24,430,742     |                         |                        | \$23,633,089     |                         |                        |
| <b>LIABILITIES AND EQUITY:</b>                            |                  |                         |                        |                  |                         |                        |
| <b>Interest bearing deposits:</b>                         |                  |                         |                        |                  |                         |                        |
| Savings   | \$775,731        | 691                     | .12                    | \$726,779        | 648                     | .12                    |
| Interest checking and money market                        | 10,209,076       | 9,960                   | .13                    | 9,735,047        | 9,303                   | .13                    |

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|  |              |            |      |              |            |      |   |
|--|--------------|------------|------|--------------|------------|------|---|
| Time open & C.D.'s of less than \$100,000                                    | 758,154      | 2,134      | .38  | 844,375      | 2,484      | .39  |   |
| Time open & C.D.'s of \$100,000 and over                                     | 1,517,894    | 6,519      | .57  | 1,225,952    | 4,468      | .49  |   |
| Total interest bearing deposits  | 13,260,855   | 19,304     | .19  | 12,532,153   | 16,903     | .18  |   |
| Borrowings:  |              |            |      |              |            |      |   |
| Federal funds purchased and securities sold                                  |              |            |      |              |            |      |   |
| under agreements to repurchase   | 1,259,773    | 2,337      | .25  | 1,637,144    | 1,271      | .10  |   |
| Other borrowings   | 194,706      | 3,066      | 2.10 | 103,906      | 2,667      | 3.43 |   |
| Total borrowings   | 1,454,479    | 5,403      | .50  | 1,741,050    | 3,938      | .30  |   |
| Total interest bearing liabilities   | 14,715,334   | 24,707     | .22  | % 14,273,203 | 20,841     | .20  | % |
| Non-interest bearing deposits  | 6,963,081    |            |      | 6,716,334    |            |      |   |
| Other liabilities  | 273,760      |            |      | 275,012      |            |      |   |
| Equity   | 2,478,567    |            |      | 2,368,540    |            |      |   |
| Total liabilities and equity   | \$24,430,742 |            |      | \$23,633,089 |            |      |   |
| Net interest margin (T/E)  |              | \$ 530,132 |      |              | \$ 493,897 |      |   |
| Net yield on interest earning assets   |              |            | 3.05 | %            |            | 2.93 | % |
| (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 2015 Annual Report on Form 10-K.

The tables below compute the effects of gradual rising interest rates over a twelve month period on the Company's net interest income, assuming a static balance sheet with the exception of deposit attrition. The difference between the two simulations is the amount of deposit attrition incorporated, which is shown in the tables below. In both simulations, three rising rate scenarios were selected as shown in the tables, and net interest income was calculated and compared to a base scenario in which assets, liabilities and rates remained constant over a twelve month period. For each of the simulations, interest rates applicable to each interest earning asset or interest bearing liability were ratably increased during the year (by either 100, 200 or 300 basis points). The balances contained in the balance sheet were assumed not to change over the twelve month period, except that as presented in the tables below, it was assumed certain non-maturity type deposit attrition would occur, as a result of higher interest rates, and would be replaced with short-term federal funds borrowings.

The simulations reflect two different assumptions related to deposit attrition. The Company utilizes these simulations both for monitoring interest rate risk and for liquidity planning purposes. While the future effects of rising rates on deposit balances cannot be known, the Company maintains a practice of running multiple rate scenarios to better understand interest rate risk and its effect on the Company's performance. The Company believes that its approach to interest rate risk has appropriately considered its susceptibility to both rising rates and falling rates and has adopted strategies which minimize impacts to overall interest rate risk.

| Simulation A                    | September 30, 2016              |                                 |                                 | June 30, 2016                   |                                 |                                 |
|---------------------------------|---------------------------------|---------------------------------|---------------------------------|---------------------------------|---------------------------------|---------------------------------|
|                                 | \$                              | %                               |                                 | \$                              | %                               |                                 |
| (Dollars in millions)           | Change                          | Change                          | Assumed<br>Deposit<br>Attrition | Change                          | Change                          | Assumed<br>Deposit<br>Attrition |
|                                 | in<br>Net<br>Interest<br>Income | in<br>Net<br>Interest<br>Income |                                 | in<br>Net<br>Interest<br>Income | in<br>Net<br>Interest<br>Income |                                 |
| 300 basis points rising         | \$22.33                         | 3.32 %                          | \$(376.6)                       | \$27.14                         | 4.11 %                          | \$(387.2)                       |
| 200 basis points rising         | 19.6                            | 2.92                            | (265.1 )                        | 23.2                            | 3.52                            | (274.1 )                        |
| 100 basis points rising         | 12.8                            | 1.91                            | (141.1 )                        | 15.1                            | 2.30                            | (148.6 )                        |
| Simulation B                    | September 30, 2016              |                                 |                                 | June 30, 2016                   |                                 |                                 |
| (Dollars in millions)           | \$                              | %                               |                                 | \$                              | %                               |                                 |
|                                 | Change                          | Change                          | Assumed<br>Deposit<br>Attrition | Change                          | Change                          | Assumed<br>Deposit<br>Attrition |
| in<br>Net<br>Interest<br>Income | in<br>Net<br>Interest<br>Income | in<br>Net<br>Interest<br>Income |                                 | in<br>Net<br>Interest<br>Income |                                 |                                 |
| 300 basis points rising         | \$(1.9)                         | (.28) %                         | \$(1,589.0)                     | \$4.87                          | .72 %                           | \$(1,605.2)                     |
| 200 basis points rising         | .1                              | .01                             | (1,482.2 )                      | 5.5                             | .83                             | (1,497.3 )                      |
| 100 basis points rising         | (1.9 )                          | (.28 )                          | (1,364.7 )                      | 2.2                             | .34                             | (1,379.0 )                      |

The difference in these two simulations is the degree in which deposits are modeled to decline as noted in the above table. Both simulations assume that a decline in deposits would be offset by increased short-term borrowings, which are more rate sensitive and can result in higher interest costs in a rising rate environment. Under Simulation A, a gradual increase in interest rates of 100 basis points is expected to increase net interest income from the base calculation by \$12.8 million, while a gradual increase in rates of 200 basis points would increase net interest income by \$19.6 million. An increase in rates of 300 basis points would result an increase in net interest income of \$22.3 million. The change in net interest income from the base calculation at September 30, 2016 was lower than projections made at June 30, 2016 largely due to a decline in deposits, cash, and reverse repurchase agreements held during the third quarter of 2016, as well as an increase in short-term borrowings at higher rates. These factors lowering interest income were partially offset by growth in loans.

Under Simulation B, the same assumptions utilized in Simulation A were applied. However, in Simulation B, deposit attrition was accelerated to consider the effects that large deposit outflows might have on net interest income and liquidity planning purposes. The effect of higher deposit attrition was that greater reliance was placed on short-term borrowings at higher rates, which are more rate sensitive. As shown in the table, under these assumptions, net interest income in Simulation B was significantly lower than in Simulation A, reflecting higher costs for short-term borrowings.

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Projecting deposit activity in a historically low interest rate environment is difficult, and the Company cannot predict how deposits will react to rising rates. The comparison provided above provides insight into potential effects of changes in rates and deposit levels on net interest income.

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 September 30, 2016. 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 15, Legal and Regulatory 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 common stock registered pursuant to Section 12 of the Securities Exchange Act of 1934, as amended.

| Period                 | Total<br>Number of<br>Shares<br>Purchased | Average<br>Price<br>Paid per<br>Share | Total<br>Number of<br>Shares<br>Purchased<br>as part of<br>Publicly<br>Announced<br>Program | Maximum<br>Number<br>that May<br>Yet Be<br>Purchased<br>Under the<br>Program |
|------------------------|---|---------------------------------------|---|--|
| July 1 — 31, 2016      | 2,432                                     | \$ 48.03                              | 2,432   | 3,792,814  |
| August 1 — 31, 2016    | 16,175                                    | \$ 49.20                              | 16,175  | 3,776,639  |
| September 1 — 30, 2016 | 2,123                                     | \$ 48.98                              | 2,123   | 3,774,516  |
| Total                  | 20,730                                    | \$ 48.90                              | 20,730  | 3,774,516  |

The Company's stock purchases shown above were made under authorizations by the Board of Directors. Under the most recent authorization in October 2015 of 5,000,000 shares, 3,774,516 shares remained available for purchase at September 30, 2016.

## 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: November 7, 2016  
By /s/ JEFFERY D. ABERDEEN  
Jeffery D. Aberdeen  
Controller  
(Chief Accounting Officer)

Date: November 7, 2016

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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