COMMERCE BANCSHARES INC /MO/
Form 10-K
February 22, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549
FORM 10-K

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

For the Fiscal Year Ended December 31, 2012 — 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,	
Kansas City, MO	64106
	(Zip Code)
(Address of principal executive offices)	(Zip Code)

(816) 234-2000
(Registrant's telephone number, including area code)
Securities registered pursuant to Section 12(b) of the Act:

Title of class	Name of exchange on which registered
$5 Par Value Common Stock	NASDAQ Global Select Market

Securities registered pursuant to Section 12(g) of the Act:
NONE
Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes þ No o
Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes o No þ
Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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 Act. (Check one):

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

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

As of June 30, 2012, the aggregate market value of the voting stock held by non-affiliates of the Registrant was approximately $2,949,000,000.

As of February 8, 2013, there were 90,689,096 shares of Registrant's $5 Par Value Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive proxy statement for its 2013 annual meeting of shareholders, which will be filed within 120 days of December 31, 2012, are incorporated by reference into Part III of this Report.

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PART I

Item 1. BUSINESS

General

Commerce Bancshares, Inc., a bank holding company as defined in the Bank Holding Company Act of 1956, as amended, was incorporated under the laws of Missouri on August 4, 1966. Through a second tier wholly-owned bank holding company, it owns all of the outstanding capital stock of Commerce Bank (the “Bank”), which is headquartered in Missouri. The Bank engages in general banking business, providing a broad range of retail, corporate, investment, trust, and asset management products and services to individuals and businesses. Commerce Bancshares, Inc. also owns, directly or through the Bank, various non-banking subsidiaries. Their activities include underwriting credit life and credit accident and health insurance, selling property and casualty insurance (relating to consumer loans made by the Bank), private equity investment, securities brokerage, mortgage banking, and leasing activities. A list of Commerce Bancshares, Inc.'s subsidiaries is included as Exhibit 21.

Commerce Bancshares, Inc. and its subsidiaries, (collectively, the "Company") is one of the nation’s top 50 bank holding companies, based on asset size. At December 31, 2012, the Company had consolidated assets of $22.2 billion, loans of $9.8 billion, deposits of $18.3 billion, and equity of $2.2 billion. All of the Company’s operations conducted by its subsidiaries are consolidated for purposes of preparing the Company’s consolidated financial statements.

The Company’s goal is to be the preferred provider of targeted financial services in its communities, based on strong customer relationships. It believes in building long-term relationships based on top quality service, a strong risk management culture, and a strong balance sheet with industry-leading capital levels. The Company operates under a super-community banking format which incorporates large bank product offerings coupled with deep local market knowledge, augmented by experienced, centralized support in select critical areas. The Company’s focus on local markets is supported by an experienced team of managers assigned to each market and is also reflected in its financial centers and regional advisory boards, which are comprised of local business persons, professionals and other community representatives, who assist the Company in responding to local banking needs. In addition to this local market, community-based focus, the Company offers sophisticated financial products available at much larger financial institutions.

The Company's banking facilities are located throughout Missouri, Kansas, and central Illinois, as well as Tulsa, Oklahoma and Denver, Colorado. Its two largest markets include St. Louis and Kansas City, which serve as the central hubs for the entire Company.

The markets the Bank serves, being located in the lower Midwest, provide natural sites for production and distribution facilities and also serve as transportation hubs. The economy has been well-diversified in these markets with many major industries represented, including telecommunications, automobile, aircraft and general manufacturing, health care, numerous service industries, food production, and agricultural production and related industries. In addition, several of the Illinois markets are located in areas with some of the most productive farmland in the world. The real estate lending operations of the Bank are centered in its lower Midwestern markets. Historically, these markets have generally tended to be less volatile than in other parts of the country. While the decline in the national real estate market resulted in significantly higher real estate loan losses during recent years for the banking industry, management believes the diversity and nature of the Bank’s markets has resulted in lower real estate loan losses in these markets and is a key factor in the Bank’s relatively lower loan loss levels during this period.

From time to time, the Company evaluates the potential acquisition of various financial institutions. In addition, the Company regularly considers the potential disposition of certain of its assets and branches. The Company seeks merger or acquisition partners that are culturally similar, have experienced management and possess either significant market presence or have potential for improved profitability through financial management, economies of scale and expanded services. The Company has not transacted any significant acquisitions or sales during the past several years.

The Company employed 4,270 persons on a full-time basis and 608 persons on a part-time basis at December 31, 2012. The Company provides a variety of benefit programs including a 401(k) plan as well as group life, health, accident, and other insurance. The Company also maintains training and educational programs designed to address the significant and changing regulations facing the financial services industry and prepare employees for positions of increasing responsibility.

Competition

The Company faces intense competition from hundreds of financial service providers. It competes with national and state banks for deposits, loans and trust accounts, and with savings and loan associations and credit unions for deposits and consumer lending products. In addition, the Company competes with other financial intermediaries such as securities brokers and dealers, personal loan companies, insurance companies, finance companies, and certain governmental agencies. With the passage of the

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Gramm-Leach-Bliley Financial Modernization Act of 1999, competition has increased over time from institutions not subject to the same regulatory restrictions as domestic banks and bank holding companies. The Company generally competes on the basis of customer service and responsiveness to customer needs, reputation, interest rates on loans and deposits, lending limits, and customer convenience, such as location of offices. The Company has approximately 13% of the deposit market share in Kansas City and approximately 9% of the deposit market share in St. Louis.

Operating Segments

The Company is managed in three operating segments. The Consumer segment includes the retail branch network, consumer installment lending, personal mortgage banking, consumer debit and credit bank card activities. It provides services through a network of 204 full-service branches, a widespread ATM network of 403 machines, and the use of alternative delivery channels such as extensive online banking and telephone banking services. In 2012, this retail segment contributed 23% of total segment pre-tax income. The Commercial segment provides a full array of corporate lending, merchant and commercial bank card products, leasing, and international services, as well as business and government deposit and cash management services. Fixed income investments are sold to individuals and institutional investors through the Capital Markets Group, which is also included in this segment. In 2012, the Commercial segment contributed 63% of total segment pre-tax income. The Wealth segment provides traditional trust and estate tax planning services, brokerage services, and advisory and discretionary investment portfolio management services to both personal and institutional corporate customers. This segment also manages the Company’s family of proprietary mutual funds, which are available for sale to both trust and general retail customers. At December 31, 2012, the Wealth segment managed investments with a market value of $17.0 billion and administered an additional $13.3 billion in non-managed assets. Additional information relating to operating segments can be found on pages 45 and 88.

Government Policies

The Company's operations are affected by federal and state legislative changes, by the United States government, and by policies of various regulatory authorities, including those of the numerous states in which they operate. These include, for example, the statutory minimum legal lending rates, domestic monetary policies of the Board of Governors of the Federal Reserve System, United States fiscal policy, international currency regulations and monetary policies, the U.S. Patriot Act, and capital adequacy and liquidity constraints imposed by federal and state bank regulatory agencies.

Supervision and Regulation

The following information summarizes existing laws and regulations that materially affect the Company's operations. It does not discuss all provisions of these laws and regulations and it does not include all laws and regulations that affect the Company presently or may affect the Company in the future.

General

The Company, as a bank holding company, is primarily regulated by the Board of Governors of the Federal Reserve System under the Bank Holding Company Act of 1956 (BHC Act). Under the BHC Act, the Federal Reserve Board’s prior approval is required in any case in which the Company proposes to acquire all or substantially all of the assets of any bank, acquire direct or indirect ownership or control of more than 5% of the voting shares of any bank, or merge or consolidate with any other bank holding company. With certain exceptions, the BHC Act also prohibits the Company from acquiring direct or indirect ownership or control of more than 5% of any class of voting shares of any non-banking company. Under the BHC Act, the Company may not engage in any business other than managing and controlling banks or furnishing certain specified services to subsidiaries and may not acquire voting control of non-banking companies unless the Federal Reserve Board determines such businesses and services to be closely related to banking. When reviewing bank acquisition applications for approval, the Federal Reserve Board considers, among other things, the Bank’s record in meeting the credit needs of the communities it serves in accordance with the Community Reinvestment Act of 1977, as amended (CRA). Under the terms of the CRA, banks have a continuing obligation, consistent with safe and sound operation, to help meet the credit needs of their communities, including

providing credit to individuals residing in low- and moderate-income areas. The Bank has a current CRA rating of "outstanding".

The Company is required to file with the Federal Reserve Board various reports and additional information the Federal Reserve Board may require. The Federal Reserve Board also makes regular examinations of the Company and its subsidiaries. The Company's banking subsidiary is a state chartered Federal Reserve member bank and is subject to regulation, supervision and examination by the Federal Reserve Bank of Kansas City and the State of Missouri Division of Finance. The Bank is also subject to regulation by the Federal Deposit Insurance Corporation (FDIC). In addition, there are numerous other federal and state laws and regulations which control the activities of the Company and the Bank, including requirements and limitations relating to capital and reserve requirements, permissible investments and lines of business, transactions with affiliates, loan limits, mergers and acquisitions, issuance of securities, dividend payments, and extensions of credit. If the Company fails to comply with these or other applicable laws and regulations, it may be subject to civil monetary penalties, imposition of cease and desist orders or other

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written directives, removal of management and, in certain circumstances, criminal penalties. This regulatory framework is intended primarily for the protection of depositors and the preservation of the federal deposit insurance funds, not for the protection of security holders. Statutory and regulatory controls increase a bank holding company's cost of doing business and limit the options of its management to employ assets and maximize income.

In addition to its regulatory powers, the Federal Reserve Bank affects the conditions under which the Company operates by its influence over the national supply of bank credit. The Federal Reserve Board employs open market operations in U.S. government securities and oversees changes in the discount rate on bank borrowings, changes in the federal funds rate on overnight inter-bank borrowings, and changes in reserve requirements on bank deposits in implementing its monetary policy objectives. These methods are used in varying combinations to influence the overall level of the interest rates charged on loans and paid for deposits, the price of the dollar in foreign exchange markets, and the level of inflation. The monetary policies of the Federal Reserve have a significant effect on the operating results of financial institutions, most notably on the interest rate environment. In view of changing conditions in the national economy and in the money markets, as well as the effect of credit policies of monetary and fiscal authorities, no prediction can be made as to possible future changes in interest rates, deposit levels or loan demand, or their effect on the financial statements of the Company.

The financial industry operates under laws and regulations that are under constant review by various agencies and legislatures and are subject to sweeping change. The Company currently operates as a bank holding company, as defined by the Gramm-Leach-Bliley Financial Modernization Act of 1999 (GLB Act), and the Bank qualifies as a financial subsidiary under the Act, which allows it to engage in investment banking, insurance agency, brokerage, and underwriting activities that were not available to banks prior to the GLB Act. The GLB Act also included privacy provisions that limit banks' abilities to disclose non-public information about customers to non-affiliated entities.

The Company must also comply with the requirements of the Bank Secrecy Act (BSA). The BSA is designed to help fight drug trafficking, money laundering, and other crimes. Compliance is monitored by the Federal Reserve. The BSA was enacted to prevent banks and other financial service providers from being used as intermediaries for, or to hide the transfer or deposit of money derived from, criminal activity. Since its passage, the BSA has been amended several times. These amendments include the Money Laundering Control Act of 1986. which made money laundering a criminal act, as well as the Money Laundering Suppression Act of 1994 which required regulators to develop enhanced examination procedures and increased examiner training to improve the identification of money laundering schemes in financial institutions.

The USA PATRIOT Act, established in 2001. substantially broadened the scope of U.S. anti-money laundering laws and regulations by imposing significant new compliance and due diligence obligations, creating new crimes and penalties and expanding the extra-territorial jurisdiction of the United States. The regulations impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing, and the regulations include significant penalties for non-compliance.

Subsidiary Bank

Under Federal Reserve policy, the bank holding company, Commerce Bancshares, Inc. (the "Parent"), is expected to act as a source of financial strength to its bank subsidiary and to commit resources to support it in circumstances when it might not otherwise do so. In addition, loans by a bank holding company to any of its subsidiary banks are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary banks. In the event of a bank holding company's bankruptcy, any commitment by the bank holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank will be assumed by the bankruptcy trustee and entitled to a priority of payment.

Deposit Insurance

Substantially all of the deposits of the Bank are insured up to the applicable limits by the Bank Insurance Fund of the FDIC, generally up to $250,000 per depositor, for each account ownership category. The Bank pays deposit insurance premiums to the FDIC based on an assessment rate established by the FDIC for Bank Insurance Fund member institutions. The FDIC established a risk-based assessment system under which institutions are classified and pay premiums according to their perceived risk to the federal deposit insurance funds. In February 2011, under the provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the FDIC issued a final rule changing its assessment base from total domestic deposits to average total assets minus average tangible equity. The rule altered other adjustments in the current assessment system for heavy use of unsecured liabilities, secured liabilities and brokered deposits, and added an adjustment for holdings of unsecured bank debt. For banks with more than $10 billion in assets, the FDIC 's new rule changed the assessment rate, abandoning the previous method for determining premiums, and instead relying on a scorecard designed to measure financial performance and ability to withstand stress, in addition to measuring the FDIC’s exposure should the bank fail. The new rule was effective for quarters beginning April 1, 2011. Because the Company has maintained a strong balance sheet with solid amounts of capital and has not offered many of the complex financial

products that were prevalent in the marketplace, the risk-based FDIC insurance assessments under the new methods were less than amounts calculated under the old assessment methods. Accordingly, the Company's FDIC insurance expense in 2012 was $10.4 million, a decrease of $2.7 million as compared to FDIC expense in 2011. In late 2009, member institutions were required to prepay their quarterly FDIC premiums. The Bank made a prepayment of $68.7 million in 2009, and the current unused balance at December 31, 2012 was $25.4 million. A refund of the unused balance is expected to be received in the second quarter of 2013.

Payment of Dividends

The Federal Reserve Board may prohibit the payment of cash dividends to shareholders by bank holding companies if their actions constitute unsafe or unsound practices. The principal source of the Parent's cash revenues is cash dividends paid by the Bank. The amount of dividends paid by the Bank in any calendar year is limited to the net profit of the current year combined with the retained net profits of the preceding two years, and permission must be obtained from the Federal Reserve Board for dividends exceeding these amounts. The payment of dividends by the Bank may also be affected by factors such as the maintenance of adequate capital.

Capital Adequacy

The Company is required to comply with the capital adequacy standards established by the Federal Reserve. These capital adequacy guidelines generally require bank holding companies to maintain minimum total capital equal to 8% of total risk-adjusted assets and off-balance sheet items (the “Total Risk-Based Capital Ratio”), with at least one-half of that amount consisting of Tier I, or core capital, and the remaining amount consisting of Tier II, or supplementary capital. Tier I capital for bank holding companies generally consists of the sum of common shareholders’ equity, qualifying non-cumulative perpetual preferred stock, a limited amount of qualifying cumulative perpetual preferred stock and minority interests in the equity accounts of consolidated subsidiaries, less goodwill and other non-qualifying intangible assets. Tier II capital generally consists of hybrid capital instruments, term subordinated debt and, subject to limitations, general allowances for loan losses. Assets are adjusted under the risk-based guidelines to take into account different risk characteristics.

In addition, the Federal Reserve also requires bank holding companies to comply with minimum leverage ratio requirements. The leverage ratio is the ratio of a banking organization’s Tier I capital to its total consolidated quarterly average assets (as defined for regulatory purposes), net of the allowance for loan losses, goodwill and certain other intangible assets. The minimum leverage ratio for bank holding companies is 4%. At December 31, 2012, the Bank was “well-capitalized” under regulatory capital adequacy standards, as further discussed on page 91.

In June 2012, the Federal Reserve released for comment a proposal to enact in the United States the international agreement referred to as Basel III. Capital and liquidity standards consistent with Basel III will be formally implemented in the United States through a series of rules. The proposed rules include higher capital requirements and would raise minimum capital levels, redefine the significant inputs to the capital ratio calculation, and be phased in over a period of years from 2013 through 2019. The initial comment period for the proposed rules ended in October 2012, and in November 2012, the effective date for initial Basel III implementation was delayed. A new implementation date has yet to be announced. The Company believes its current capital ratios would be higher than those required in the Basel III proposal issued by the Federal Reserve.

Recent Significant Legislation Affecting the Company

In July 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) was signed into law. The Dodd-Frank Act is sweeping legislation intended to overhaul regulation of the financial services industry and requires rulemaking and reports over the next several years. Among its many provisions, the Dodd-Frank Act established a new council of “systemic risk” regulators, created a new consumer protection division within the Federal Reserve, empowers the Federal Reserve to supervise the largest, most complex financial companies, allows the government to seize and liquidate failing financial companies, and gives regulators new powers to oversee the

derivatives market.

In June 2011, the Federal Reserve, under the provisions of the Dodd-Frank Act, approved a final debit card interchange rule that significantly limits the amount of debit card interchange fees charged by banks. The rule caps an issuer's base fee at 21 cents per transaction and allows additional fees to help cover fraud losses. The new pricing is a reduction of approximately 45% when compared to previous market rates. The rule also limits network exclusivity, requiring issuers to ensure that a debit card transaction can be carried on two unaffiliated networks: one signature-based and one PIN-based. The rules apply to bank issuers with more than $10 billion in assets and took effect in phases, with the base fee cap effective October 1, 2011 and the network exclusivity rule effective on April 1, 2012.

The Dodd-Frank Act also established the Consumer Financial Protection Bureau (CFPB) and authorizes it to supervise certain consumer financial services companies and large depository institutions and their affiliates for consumer protection purposes.

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Subject to the provisions of the Act, the CFPB has responsibility to implement, examine for compliance with, and enforce "Federal consumer financial law." As a depository institution, the Company will be subject to examinations by the CFPB, which will focus on the Company's ability to detect, prevent, and correct practices that present a significant risk of violating the law and causing consumer harm.

In October 2012, the Federal Reserve, as required by the Dodd-Frank Act, approved new stress testing regulations applicable to certain financial companies with total consolidated assets of more than $10 billion but less than $50 billion. The rule requires that these financial companies, including Commerce Bancshares, conduct stress tests on an annual basis. The stress tests will have an as-of date of September 30, 2013 using scenarios provided by the Federal Reserve in November of the same year, and the Company is required to submit regulatory reports to the Federal Reserve on its stress tests by March 31, 2014. During June 2015, the Company will be required to make public disclosures of the results of tests performed as of September 30, 2014.

Available Information

The Company's principal offices are located at 1000 Walnut, Kansas City, Missouri (telephone number 816-234-2000). The Company makes available free of charge, through its Web site at www.commercebank.com, reports filed with the Securities and Exchange Commission as soon as reasonably practicable after the electronic filing. These filings include the annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports.

Statistical Disclosure

The information required by Securities Act Guide 3 — "Statistical Disclosure by Bank Holding Companies" is located on the pages noted below.

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Item 1a. RISK FACTORS

Making or continuing an investment in securities issued by Commerce Bancshares, Inc., including its common stock, involves certain risks that you should carefully consider. If any of the following risks actually occur, its business, financial condition or results of operations could be negatively affected, the market price for your securities could decline, and you could lose all or a part of your investment. Further, to the extent that any of the information contained in this Annual Report on Form 10-K constitutes forward-looking statements, the risk factors set forth below also are cautionary statements identifying important factors that could cause the Company's actual results to differ materially from those expressed in any forward-looking statements made by or on behalf of Commerce Bancshares, Inc.

Difficult market conditions have adversely affected the Company's industry and may continue to do so.

Given the concentration of the Company's banking business in the United States, it is particularly exposed to downturns in the U.S. economy. The economic trends which began in 2008, such as declines in the housing market

(e.g., falling home prices and increasing foreclosures), unemployment and under-employment, negatively impacted the credit performance of mortgage loans and resulted in significant write-downs of asset values by financial institutions. The weak U.S. economy and tightening of credit during recent years led to a lack of consumer confidence, increased market volatility and widespread reduction of business activity generally. More recently, the economy has begun to stabilize. The housing market has improved over recent years, and asset write-downs have slowed. However, there remain risks that could undermine the more recent improvements in the economy's stabilization.

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In particular, the Company may face the following risks in connection with these market conditions:

- Unemployment has improved over recent years but remains at historically high levels. Continued high unemployment levels and weak economic activity may affect consumer confidence levels and may cause declines in consumer credit usage, adverse changes in payment patterns, and higher loan delinquencies and default rates. These could impact the Company's future loan losses and provision for loan losses, as a significant part of the Company's business includes consumer and credit card lending.
- Reduced levels of economic activity may also cause declines in financial service transactions, including bank card, corporate cash management and other fee businesses, as well as the fees earned by the Company on such transactions.
- The Company's ability to assess the creditworthiness of its customers may be impaired if the models and approaches it uses to select, manage, and underwrite its customers become less predictive of future behaviors, causing higher future credit losses.
- The process used to estimate losses inherent in the Company's loan portfolio requires difficult, subjective, and complex judgments, including forecasts of economic conditions and how these economic predictions might impair the ability of its borrowers to repay their loans. If an instance occurs that renders these predictions no longer capable of accurate estimation, this may in turn impact the reliability of the process.
- Competition in the industry could intensify as a result of the increasing consolidation of financial services companies in connection with current market conditions, thereby reducing market prices for various products and services which could in turn reduce Company revenues.
- Though bank failures slowed during 2011 and 2012 as compared to 2009 and 2010, failures during this period remained higher than historical levels. Due to higher bank failures in recent years and continued uncertainty about the future, the Company may be required to pay high levels of FDIC premiums for extended periods of time.
- The U.S. economy is also affected by foreign economic events, such as the European debt crisis that developed during the past year. Although the Company does not hold foreign debt, global conditions affecting interest rates, business export activity, capital expenditures by businesses, and investor confidence may negatively affect the Company by means of reduced loan demand or reduced transaction volume with the Company.
- The United States is faced with large debts outstanding and a significant debate by Congress on how to address this situation. Automatic spending cuts scheduled by law to go into effect in March 2013, or revisions to this law by Congress, could result in lower government spending and thus slow economic growth in the short-term. Should this occur, unemployment could increase, demand for business and consumer loans and other financial products could decline, and credit losses could increase, thus reducing the Company's profitability.

Significant changes in banking laws and regulations could materially affect the Company's business.

As a result of the recent banking crisis, a significant increase in bank regulation has occurred. A number of new laws and regulations have already been implemented, including those which reduce overdraft fees, credit card revenues, and revenues from student lending activities. These recently adopted regulations have resulted in lower revenues and higher operating costs. As discussed in Item 1, the Dodd-Frank Act passed in July 2010 contains significant complex regulations for all financial institutions. Among its many provisions are rules which established a new council of "systemic risk" regulators, created a new consumer protection division within the Federal Reserve, empower the Federal Reserve to supervise the largest, most complex financial companies, allow the government to seize and liquidate failing financial companies, and give regulators new powers to oversee the derivatives market.

Because the Company has maintained a strong balance sheet and has not offered many of the complex financial products that were prevalent in the marketplace, there are a number of provisions within the Dodd-Frank Act, including higher capital standards, improved lending transparency and risk-based FDIC insurance assessments, that management does not expect to negatively affect the Company's future financial results. However, the Company has already been significantly affected by enacted regulation on debit cards, and a number of provisions within the law include the potential for higher costs due to increased regulatory and compliance burdens, which will result in lower revenues or increasing costs for the Company. In addition to these and other new regulations which are already in place and are discussed above, the Company will likely face increased regulation of the industry. Increased regulation,

along with possible changes in tax laws and accounting rules, may have a significant impact on the way the Company conducts business, implements strategic initiatives, engages in tax planning and makes financial disclosures. Compliance with such regulation may divert resources from other areas of the business and limit the ability to pursue other opportunities.

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The performance of the Company is dependent on the economic conditions of the markets in which the Company operates.
The Company’s success is heavily influenced by the general economic conditions of the specific markets in which it operates. Unlike larger national or other regional banks that are more geographically diversified, the Company provides financial services primarily throughout the states of Missouri, Kansas, and central Illinois, and has recently expanded into Oklahoma, Colorado and other surrounding states. As the Company does not have a significant presence in other parts of the country, a prolonged economic downtown in these markets could have a material adverse effect on the Company’s financial condition and results of operations.

Significant changes in federal monetary policy could materially affect the Company’s business.
The Federal Reserve System regulates the supply of money and credit in the United States. Its polices determine in large part the cost of funds for lending and investing by influencing the interest rate earned on loans and paid on borrowings and interest bearing deposits. Credit conditions are influenced by its open market operations in U.S. government securities, changes in the member bank discount rate, and bank reserve requirements. Changes in Federal Reserve Board policies are beyond the Company’s control and difficult to predict, and such changes may result in lower interest margins and a continued lack of demand for credit products.

The soundness of other financial institutions could adversely affect the Company.
The Company’s ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institution counterparties. Financial services institutions are interrelated as a result of trading, clearing, counterparty or other relationships. The Company has exposure to many different industries and counterparties and routinely executes transactions with counterparties in the financial industry, including brokers and dealers, commercial banks, investment banks, mutual funds, and other institutional clients. Transactions with these institutions include overnight and term borrowings, interest rate swap agreements, securities purchased and sold, short-term investments, and other such transactions. As a result of this exposure, defaults by, or rumors or questions about, one or more financial services institutions or the financial services industry generally, could lead to market-wide liquidity problems and defaults by other institutions. Many of these transactions expose the Company to credit risk in the event of default of its counterparty or client, while other transactions expose the Company to liquidity risks should funding sources quickly disappear. In addition, the Company’s credit risk may be exacerbated when the collateral held cannot be realized or is liquidated at prices not sufficient to recover the full amount of the exposure due to the Company. Any such losses could materially and adversely affect results of operations.

The Company’s asset valuation may include methodologies, estimations and assumptions which are subject to differing interpretations and could result in changes to asset valuations that may materially adversely affect its results of operations or financial condition.
The Company uses estimates, assumptions, and judgments when certain financial assets and liabilities are measured and reported at fair value. Assets and liabilities carried at fair value inherently result in a higher degree of financial statement volatility. Fair values and the information used to record valuation adjustments for certain assets and liabilities are based on quoted market prices and/or other observable inputs provided by independent third-party sources, when available. When such third-party information is not available, fair value is estimated primarily by using cash flow and other financial modeling techniques utilizing assumptions such as credit quality, liquidity, interest rates and other relevant inputs. Changes in underlying factors, assumptions, or estimates in any of these areas could materially impact the Company’s future financial condition and results of operations.
During periods of market disruption, including periods of significantly rising or high interest rates, rapidly widening credit spreads or illiquidity, it may be difficult to value certain assets if trading becomes less frequent and/or market data becomes less observable. There may be certain asset classes in active markets with significant observable data that become illiquid due to the current financial environment. In such cases, certain asset valuations may require more subjectivity and management judgment. As such, valuations may include inputs and assumptions that are less observable or require greater estimation. Further, rapidly changing and unprecedented credit and equity market

conditions could materially impact the valuation of assets as reported within the Company’s consolidated financial statements, and the period-to-period changes in value could vary significantly. Decreases in value may have a material adverse effect on results of operations or financial condition.

The Company’s investment portfolio values may be adversely impacted by deterioration in the credit quality of underlying collateral within the various categories of investment securities it owns.
The Company generally invests in securities issued by municipal entities, government-backed agencies or privately issued securities that are highly rated and evaluated at the time of purchase, however, these securities are subject to changes in market value due to changing interest rates and implied credit spreads. Over the past several years, budget deficits and other financial problems in a number of states and political subdivisions have been reported in the media. While the Company maintains rigorous risk management practices over bonds issued by municipalities, further credit deterioration in these bonds could occur and result in losses. Certain mortgage and asset-backed securities represent beneficial interests which are collateralized by residential

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mortgages, credit cards, automobiles, mobile homes or other assets. While these investment securities are highly rated at the time of initial investment, the value of these securities may decline significantly due to actual or expected deterioration in the underlying collateral, especially residential mortgage collateral. Market conditions have resulted in a deterioration in fair values for non-guaranteed mortgage-backed and other asset-backed securities. Under accounting rules, when the impairment is due to declining expected cash flows, some portion of the impairment, depending on the Company’s intent to sell and the likelihood of being required to sell before recovery, must be recognized in current earnings. This could result in significant non-cash losses.

Future loan losses could increase.
The Company maintains an allowance for loan losses that represents management’s best estimate of probable losses that have been incurred at the balance sheet date within the existing portfolio of loans. The level of the allowance reflects management’s continuing evaluation of industry concentrations, specific credit risks, loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions and unidentified losses inherent in the current loan portfolio. Although the loan losses have declined significantly in 2012, they had been at elevated levels during the period 2007 through 2011 when compared to historical experience, particularly in residential construction, consumer, and credit card loans, due to the past deterioration in the housing industry and general economic conditions in recent years. While the housing sector and overall economy have begun to slowly recover, business activities across a range of industries continue to face difficulties due to the lack of consumer spending and the lack of liquidity in the global credit markets. A continuation or worsening of current financial market conditions could result in further loan losses, which may negatively affect the Company's results of operations and could further increase levels of its allowance. In addition, the Company’s allowance level is subject to review by regulatory agencies, and that review could result in adjustments to the allowance. See the section captioned “Allowance for Loan Losses” in Item 7, Management’s Discussion and Analysis of Financial Condition and Results of Operations, of this report for further discussion related to the Company’s process for determining the appropriate level of the allowance for possible loan loss.

The Company is subject to both interest rate and liquidity risk.
With oversight from its Asset-Liability Management Committee, the Company devotes substantial resources to monitoring its liquidity and interest rate risk on a monthly basis. The Company's net interest income is the largest source of overall revenue to the Company, representing 62% of total revenue. The interest rate environment in which the Company operates fluctuates in response to general economic conditions and policies of various governmental and regulatory agencies, particularly the Federal Reserve Board. Changes in monetary policy, including changes in interest rates, will influence loan originations, deposit generation, demand for investments and revenues and costs for earning assets and liabilities.
Additionally the Company manages its balance sheet in order to maximize its net interest income from its net earning assets while insuring that there is ample liquidity to meet fluctuating cash flows coming from either funding sources or its earning assets.
Since the end of 2008, a weakened U.S. economy has resulted in significant growth in deposits from both consumers and businesses. From 2008 through 2012, total deposits grew by $5.5 billion. During the same period, the Federal Reserve reduced interest rates to unprecedented low levels. Loan demand remained weak through this period, and the Company invested these new deposits in its investment securities portfolio, which grew by $5.9 billion from 2008 through 2012. At December 31, 2012 the Company's loan to deposit rate was 56%, a sign of strong liquidity. Investment securities generally carry lower rates than loans, and as these securities have grown, interest margins have been pressured. Furthermore the Company attempts to diversify its investment portfolio while keeping duration short, in order to ensure it is always able to meet liquidity needs for future changes in loans or deposit balances.
While loans grew in 2012 by 7% as the economy strengthened somewhat, the low interest rate environment in which all banks operate will continue to pressure the Company's interest margins. Should the demand for loans increase in the future while deposit balances decline significantly, the Company's liquidity risk could change, as it is dependent on the Company's ability to manage maturities within its investment portfolio to fund these changing cash flows.

The Company operates in a highly competitive industry and market area.
The Company operates in the financial services industry, which is facing a rapidly changing environment having numerous competitors including other banks and insurance companies, securities dealers, brokers, trust and investment companies and mortgage bankers. Consolidation among financial service providers is likely to occur, and there are many new changes in technology, product offerings and regulation. As consolidation occurs, larger regional banks may acquire smaller banks in our market and add to existing competition. These new banks may lower fees in an effort to grow market share, which could result in a loss of customers and lower fee revenue for the Company. The Company must continue to make investments in its products and delivery systems to stay competitive with the industry as a whole, or its financial performance may suffer.

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The Company’s reputation and future growth prospects could be impaired if events occur which breach its customers’ privacy.
The Company relies heavily on communications and information systems to conduct its business, and as part of its business, the Company maintains significant amounts of data about its customers and the products they use. Additionally, customers rely on online bank products. While the Company has policies and procedures and safeguards designed to prevent or limit the effect of failure, interruption or security breach of its information systems, there can be no assurances that any such failures, interruptions or security breaches will not occur; or if they do occur, that they will be adequately addressed. In addition to unauthorized access, denial-of-service attacks could overwhelm Company Web sites and prevent the Company from adequately serving customers. Should any of the Company's systems become compromised, the reputation of the Company could be damaged, relationships with existing customers may be impaired, the compromise could result in lost business, and as a result, the Company could incur significant expenses trying to remedy the incident.

The Company may not attract and retain skilled employees.
The Company’s success depends, in large part, on its ability to attract and retain key people. Competition for the best people can be intense, and the Company spends considerable time and resources attracting and hiring qualified people for its various business lines and support units. The unexpected loss of the services of one or more of the Company’s key personnel could have a material adverse impact on the Company’s business because of their skills, knowledge of the Company’s market, and years of industry experience, as well as the difficulty of promptly finding qualified replacement personnel.

Item 1b. UNRESOLVED STAFF COMMENTS
None

Item 2. PROPERTIES
The main offices of the Bank are located in the larger metropolitan areas of its markets in various multi-story office buildings. The Bank owns its main offices and leases unoccupied premises to the public. The larger offices include:

Building	Net rentable square footage	% occupied in total	% occupied by bank
922 Walnut Kansas City, MO	256,000	95 %	93 %
1000 Walnut Kansas City, MO	403,000	85	38
811 Main Kansas City, MO	237,000	100	100
8000 Forsyth Clayton, MO	178,000	97	97
1551 N. Waterfront Pkwy Wichita, KS	120,000	97	32

Various installment loan, credit card, trust and safe deposit functions operate out of leased offices in downtown Kansas City, Missouri. The Company has an additional 199 branch locations in Missouri, Illinois, Kansas, Oklahoma and Colorado which are owned or leased, and 158 off-site ATM locations.

Item 3. LEGAL PROCEEDINGS
The information required by this item is set forth in Item 8 under Note 18, Commitments, Contingencies and Guarantees on page 104.

Item 4. MINE SAFETY DISCLOSURES

Not applicable

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Executive Officers of the Registrant

The following are the executive officers of the Company as of February 22, 2013, each of whom is designated annually. There are no arrangements or understandings between any of the persons so named and any other person pursuant to which such person was designated an executive officer.

Name and Age	Positions with Registrant
Jeffery D. Aberdeen, 59	Controller of the Company since December 1995. He is also Controller of the Company's subsidiary bank, Commerce Bank.
Kevin G. Barth, 52	Executive Vice President of the Company since April 2005 and Executive Vice President of Commerce Bank since October 1998. Senior Vice President of the Company and Officer of Commerce Bank prior thereto.
Jeffrey M. Burik, 54	Senior Vice President of the Company since February 2013. Executive Vice President of Commerce Bank since November 2007.
Daniel D. Callahan, 56	Executive Vice President and Chief Credit Officer of the Company since December 2010 and Senior Vice President of the Company prior thereto. Executive Vice President of Commerce Bank since May 2003.
Sara E. Foster, 52	Executive Vice President of the Company since February 2012 and Senior Vice President of the Company since February 1998.
David W. Kemper, 62	Chairman of the Board of Directors of the Company since November 1991, Chief Executive Officer of the Company since June 1986. He was President of the Company from April 1982 until February 2013. He is Chairman of the Board, President and Chief Executive Officer of Commerce Bank. He is the son of James M. Kemper, Jr. (a former Director and former Chairman of the Board of the Company), the brother of Jonathan M. Kemper, Vice Chairman of the Company, and father of John W. Kemper, President and Chief Operating Officer of the Company.
John W. Kemper, 35	President and Chief Operating Officer of the Company since February 2013, and Executive Vice President and Chief Administrative Officer of the Company prior thereto. Senior Vice President of Commerce Bank since January 2009. Prior to his employment with Commerce Bank in August 2007, he was employed as an engagement manager with a global management consulting firm, managing strategy and operations projects primarily focused in the financial service industry. He is the son of David W. Kemper, Chairman and Chief Executive Officer of the Company and nephew of Jonathan M. Kemper, Vice Chairman of the Company.
Jonathan M. Kemper, 59	Vice Chairman of the Company since November 1991 and Vice Chairman of Commerce Bank since December 1997. Prior thereto, he was Chairman of the Board, Chief Executive Officer, and President of Commerce Bank. He is the son of James M. Kemper, Jr. (a former Director and former Chairman of the Board of the Company), the brother of David W. Kemper, Chairman and Chief Executive Officer of the Company, and uncle of John W. Kemper, President and Chief Operating Officer of the Company.
Charles G. Kim, 52	Chief Financial Officer of the Company since July 2009. Executive Vice President of the Company since April 1995 and Executive Vice President of Commerce Bank

	since January 2004. Prior thereto, he was Senior Vice President of Commerce Bank.
Seth M. Leadbeater, 62	Vice Chairman of the Company since January 2004. Prior thereto he was Executive Vice President of the Company. Vice Chairman of Commerce Bank since September 2004. Prior thereto he was Executive Vice President of Commerce Bank.
Michael J. Petrie, 56	Senior Vice President of the Company since April 1995. Prior thereto, he was Vice President of the Company.
Robert J. Rauscher, 55	Senior Vice President of the Company since October 1997. Senior Vice President of Commerce Bank prior thereto.
V. Raymond Stranghoener, 61	Executive Vice President of the Company since July 2005 and Senior Vice President of the Company prior thereto.

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PART II

Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Commerce Bancshares, Inc.
Common Stock Data
The following table sets forth the high and low prices of actual transactions in the Company's common stock and cash dividends paid for the periods indicated (restated for the 5% stock dividend distributed in December 2012).

	Quarter	High	Low	Cash Dividends	
2012	First	$39.31	$35.78	$.219	
	Second	39.05	34.45	.219	
	Third	40.70	35.91	.219	
	Fourth	38.70	34.69	1.648	*
2011	First	$38.70	$34.96	$.209	
	Second	39.82	36.33	.209	
	Third	39.91	30.14	.209	
	Fourth	36.83	29.99	.209	
2010	First	$36.16	$32.44	$.203	
	Second	37.34	30.68	.203	
	Third	34.85	30.32	.203	
	Fourth	36.82	31.16	.203	

* Includes a special dividend of $1.429 per share

Commerce Bancshares, Inc. common shares are listed on the Nasdaq Global Select Market (NASDAQ) under the symbol CBSH. The Company had 4,135 shareholders of record as of December 31, 2012.

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Performance Graph

The following graph presents a comparison of Company (CBSH) performance to the indices named below. It assumes $100 invested on December 31, 2007 with dividends invested on a cumulative total shareholder return basis.

	2007	2008	2009	2010	2011	2012
Commerce (CBSH)	100.00	105.31	100.00	110.34	113.81	116.78
NASDAQ Bank	100.00	72.91	60.66	72.13	64.51	77.18
S&P 500	100.00	63.00	79.67	91.67	93.61	108.59

The following table sets forth information about the Company’s purchases of its $5 par value common stock, its only class of stock registered pursuant to Section 12 of the Exchange Act, during the fourth quarter of 2012.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Program	Maximum Number that May Yet Be Purchased Under the Program
October 1—31, 2012	329,095	$37.83	329,095	2,572,965
November 1—30, 2012	444,277	$38.01	444,277	2,128,688
December 1—31, 2012	1,070	$35.06	1,070	2,127,618
Total	774,442	$37.93	774,442	2,127,618

The Company’s stock purchases shown above were made under authorizations by the Board of Directors. Under the most recent authorization in July 2012 of 3,000,000 shares, 2,127,618 shares remained available for purchase at December 31, 2012.

Item 6. SELECTED FINANCIAL DATA

The required information is set forth below in Item 7.

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Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

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 which 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 the risk factors identified in Item 1a Risk Factors and the following: 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; and competition with other entities that offer financial services.

Overview

Commerce Bancshares, Inc. and its subsidiaries (the "Company") operates as a super-community bank offering an array of sophisticated financial products delivered with high-quality, personal customer service. It is the largest bank holding company headquartered in Missouri, with its principal offices in Kansas City and St. Louis, Missouri. Customers are served from approximately 360 locations in Missouri, Kansas, Illinois, Oklahoma and Colorado using delivery platforms which include an extensive network of branches and ATM machines, full-featured online banking, and a central contact center.

The core of the Company's competitive advantage is its focus on the local markets it services and its concentration on relationship banking and high touch service. In order to enhance shareholder value, the Company grows its core revenue by expanding new and existing customer relationships, utilizing improved technology, and enhancing customer satisfaction.

Various indicators are used by management in evaluating the Company's financial condition and operating performance. Among these indicators are the following:

- Net income and growth in earnings per share — Net income attributable to Commerce Bancshares, Inc. was $269.3 million, an increase of 5.1% compared to the previous year. The return on average assets was 1.30%. Diluted earnings per share increased 7.8% in 2012 compared to 2011.
- Growth in total revenue — Total revenue is comprised of net interest income and non-interest income. Total revenue in 2012 increased slightly over 2011, as non-interest income grew $6.7 million and net interest income fell $6.2 million. Non-interest income saw increases in trust and capital market fees, partly offset by declines in bank card transaction fees, deposit fees, and loan fees and sales. However, past regulatory actions which have reduced fees from overdraft, debit card, and student lending activities have been somewhat mitigated by growth in corporate card revenue, which increased $13.0 million in 2012, and growth in other types of deposit fees. The net interest margin declined to 3.41% in 2012, a 24 basis point decline from 2011, as average rates continued to fall and the lending environment remained challenging.
- Expense control — Total non-interest expense increased less than 1% this year compared to 2011. Salaries and employee benefits, the largest component, increased by $15.6 million, or 4.5% due to higher salaries, incentives, medical and retirement costs. In addition, other operating expenses included a $5.7 million increase in data processing

costs and the accrual of $5.2 million in potential losses arising from the preliminary settlement of Visa, Inc. (Visa) credit card interchange litigation.

- Asset quality — Net loan charge-offs in 2012 decreased $25.2 million from those recorded in 2011 and averaged .42% of loans compared to .70% in the previous year. Total non-performing assets, which include non-accrual loans and foreclosed real estate, amounted to $64.9 million at December 31, 2012, a decrease of $28.9 million from balances at the previous year end, and represented .66% of loans outstanding.
- Shareholder return — Total shareholder return, including the change in stock price and dividend reinvestment, was 2.6% over the past year and 6.5% over the past 10 years. Record earnings over the last two years have strengthened capital

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and liquidity and allowed the Company to pay a special fourth quarter cash dividend of $1.43* per share in advance of higher tax rates now in effect.
* Restated for the 5% stock dividend distributed in December 2012.

The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes. The historical trends reflected in the financial information presented below are not necessarily reflective of anticipated future results.

Key Ratios

(Based on average balances)	2012	2011	2010	2009	2008
Return on total assets	1.30%	1.32%	1.22%	.96%	1.15%
Return on total equity	12.00	12.15	11.15	9.76	11.81
Equity to total assets	10.84	10.87	10.91	9.83	9.71
Loans to deposits (1)	55.80	59.15	70.02	79.79	92.11
Non-interest bearing deposits to total deposits	32.82	30.26	28.65	26.48	24.05
Net yield on interest earning assets (tax equivalent basis)	3.41	3.65	3.89	3.93	3.96
(Based on end of period data)					
Non-interest income to revenue (2)	38.44	37.82	38.54	38.41	38.80
Efficiency ratio (3)	59.26	59.10	59.71	59.88	63.08
Tier I risk-based capital ratio	13.60	14.71	14.38	13.04	10.92
Total risk-based capital ratio	14.93	16.04	15.75	14.39	12.31
Tier I leverage ratio	9.14	9.55	10.17	9.58	9.06
Tangible common equity to assets ratio (4)	9.25	9.91	10.27	9.71	8.25
Cash dividend payout ratio	79.48	31.06	35.52	44.15	38.54

(1) Includes loans held for sale.
(2) Revenue includes net interest income and non-interest income.
(3) The efficiency ratio is calculated as non-interest expense (excluding intangibles amortization) as a percent of revenue.
(4) The tangible common equity ratio is calculated as stockholders' equity reduced by goodwill and other intangible assets (excluding mortgage servicing rights) divided by total assets reduced by goodwill and other intangible assets (excluding mortgage servicing rights).

Selected Financial Data

(In thousands, except per share data)	2012	2011	2010	2009	2008
Net interest income	$639,906	$646,070	$645,932	$635,502	$592,739
Provision for loan losses	27,287	51,515	100,000	160,697	108,900
Non-interest income	399,630	392,917	405,111	396,259	375,712
Investment securities gains (losses), net	4,828	10,812	(1,785)	(7,195)	30,294
Non-interest expense	618,469	617,249	631,134	621,737	615,380
Net income attributable to Commerce Bancshares, Inc.	269,329	256,343	221,710	169,075	188,655
Net income per common share-basic*	2.91	2.70	2.30	1.79	2.05
Net income per common share-diluted*	2.90	2.69	2.29	1.78	2.04
Cash dividends	211,608	79,140	78,231	74,720	72,055
Cash dividends per share*	2.305	.834	.812	.790	.784
Market price per share*	35.06	36.30	36.04	33.45	36.16
Book value per share*	23.76	23.24	21.19	19.63	17.14
Common shares outstanding*	91,414	93,400	95,503	96,093	92,124

Total assets	22,159,589	20,649,367	18,502,339	18,120,189	17,532,447
Loans, including held for sale	9,840,211	9,208,554	9,474,733	10,490,327	11,644,544
Investment securities	9,669,735	9,358,387	7,409,534	6,473,388	3,780,116
Deposits	18,348,653	16,799,883	15,085,021	14,210,451	12,894,733
Long-term debt	503,710	511,817	512,273	1,236,062	1,447,781
Equity	2,171,574	2,170,361	2,023,464	1,885,905	1,579,467
Non-performing assets	64,863	93,803	97,320	116,670	79,077

*Restated for the 5% stock dividend distributed in December 2012.

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Results of Operations

				$ Change		% Change	
(Dollars in thousands)	2012	2011	2010	'12-'11	'11-'10	'12-'11	'11-'10
Net interest income	$639,906	$646,070	$645,932	$(6,164)	$138	(1.0)%	—%
Provision for loan losses	(27,287)	(51,515)	(100,000)	(24,228)	(48,485)	(47.0)	(48.5)
Non-interest income	399,630	392,917	405,111	6,713	(12,194)	1.7	(3.0)
Investment securities gains (losses), net	4,828	10,812	(1,785)	(5,984)	12,597	(55.3)	NM
Non-interest expense	(618,469)	(617,249)	(631,134)	1,220	(13,885)	.2	(2.2)
Income taxes	(127,169)	(121,412)	(96,249)	5,757	25,163	4.7	26.1
Non-controlling interest expense	(2,110)	(3,280)	(165)	(1,170)	3,115	(35.7)	NM
Net income attributable to Commerce Bancshares, Inc.	$269,329	$256,343	$221,710	$12,986	$34,633	5.1%	15.6%

Net income attributable to Commerce Bancshares, Inc. for 2012 was $269.3 million, an increase of $13.0 million, or 5.1%, compared to $256.3 million in 2011. Diluted income per share was $2.90 in 2012 compared to $2.69 in 2011. The increase in net income largely resulted from a $24.2 million decrease in the provision for loan losses coupled with an increase of $6.7 million in non-interest income. These increases to net income were partly offset by a decline of $6.2 million in net interest income, $6.0 million in lower net securities gains, and a $5.8 million increase in income tax expense. The return on average assets was 1.30% in 2012 compared to 1.32% in 2011, and the return on average equity was 12.00% compared to 12.15% in 2011. At December 31, 2012, the ratio of tangible common equity to assets was 9.25% compared to 9.91% at year end 2011.

During 2012, net interest income decreased $6.2 million to $639.9 million, as compared to $646.1 million in 2011. This decline was due to lower rates earned on investment securities and loans, partly offset by higher balances in these assets and lower rates paid on deposits. The provision for loan losses totaled $27.3 million in 2012, a decrease of $24.2 million from the prior year. Net loan charge-offs declined by $25.2 million in 2012 compared to 2011, mainly in business, construction, consumer, and consumer credit card loans.

Non-interest income for 2012 was $399.6 million, an increase of $6.7 million, or 1.7%, compared to $392.9 million in 2011. This increase resulted mainly from higher trust fees and capital market fees, and a $13.0 million increase in corporate card revenue. Corporate card revenue has shown strong growth over the past several years, resulting from both new customer transactions and increased volumes from existing customers as the Company continues to expand this product on a national basis. Debit card interchange income, which was limited by rules adopted in Dodd-Frank legislation effective in the fourth quarter of 2011, declined $19.3 million. Deposit fees decreased $3.2 million, as declines in overdraft and return items fees were partly offset by increases in other types of deposit fees. Loan fees and sales declined $1.5 million, as sales of home mortgages in the secondary market were discontinued in late 2011.

Investment securities gains amounted to $4.8 million, a decrease of $6.0 million from $10.8 million in investment securities gains during 2011. The 2012 gains resulted mainly from fair value adjustments and sales of private equity investments.

Non-interest expense for 2012 was $618.5 million, an increase of $1.2 million over $617.2 million in 2011. This slight overall increase included a $15.6 million increase in salaries and benefits expense, as well as a $5.7 million increase in data processing and software expense. During 2012, non-interest expense included a $5.2 million loss contingency related to Visa interchange litigation, which is discussed further in Note 18 to the consolidated financial statements. Offsetting these increases in non-interest expense during 2012 was $18.3 million expensed during 2011 related to debit card overdraft litigation, also discussed further in Note 18. Income tax expense was $127.2 million in 2012 compared to $121.4 million in 2011, resulting in an effective tax rate of 32.1% in both years.

Net income attributable to Commerce Bancshares, Inc. for 2011 was $256.3 million, an increase of $34.6 million, or 15.6%, compared to $221.7 million in 2010. Diluted income per share was $2.69 in 2011 compared to $2.29 in 2010. The increase in net income resulted from a $48.5 million decrease in the provision for loan losses coupled with a decline of $13.9 million in non-interest expense and $12.6 million in higher net securities gains. These effects were partly offset by a $12.2 million decline in non-interest income and a $25.2 million increase in income tax expense. Non-interest expense included the accrual of $18.3 million for a lawsuit settlement regarding debit card overdrafts, as mentioned above. In addition, an indemnification obligation liability related to Visa, also discussed in Note 18, was reduced by $4.4 million, decreasing expense. The return on average assets was 1.32% in 2011 compared to 1.22% in 2010, and the return on average equity was 12.15% compared to 11.15% in 2010. At December 31, 2011, the ratio of tangible common equity to assets was 9.91% compared to 10.27% at year end 2010.

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During 2011, net interest income increased $138 thousand to $646.1 million, as compared to $645.9 million in 2010. This slight growth was due to lower rates incurred on deposits, higher average balances in investment securities, and lower average borrowing levels. These effects were partly offset by lower rates earned on both investment securities and loans, in addition to lower loan balances. The provision for loan losses totaled $51.5 million in 2011, a decrease of $48.5 million from the prior year. Net loan charge-offs declined by $32.4 million in 2011 compared to 2010, mainly in construction, consumer, and consumer credit card loans.

Non-interest income for 2011 was $392.9 million, a decrease of $12.2 million, or 3.0%, compared to $405.1 million in 2010. This decrease was the result of a decline in overdraft fees of $10.2 million in 2011, due to the Company's implementation on July 1, 2010 of new overdraft regulations on debit card transactions, as well as a decline of $3.1 million in debit card interchange income resulting from the Dodd-Frank legislation mentioned above. Also contributing to the decline in non-interest income in 2011 was a $14.6 million decrease in gains on sales of student loans. This occurred as new federal regulations over guaranteed student loans caused the Company to exit the guaranteed student loan business and the Company sold most of its student loans in 2010. Partially offsetting these decreases in non-interest income was a $9.5 million increase in corporate card revenue. In addition, trust fees rose $7.4 million on strong new account sales.

Investment securities gains amounted to $10.8 million, an increase of $12.6 million over $1.8 million in investment securities losses during 2010. As in 2012, the 2011 gains also resulted mainly from fair value adjustments and sales of private equity investments.

Non-interest expense for 2011 was $617.2 million, a decrease of $13.9 million, or 2.2%, compared to $631.1 million in 2010. This decline was partly due to slight decreases in salaries and benefits expense, as well as marketing and equipment expenses, but was mainly driven by reductions of $4.7 million in supplies and communication expense and $6.1 million in FDIC insurance expense. During 2010, non-interest expense included an $11.8 million debt pre-payment penalty on Federal Home Loan Bank (FHLB) advances. These effects on non-interest expense were partly offset by an $18.3 million loss recorded in 2011 related to debit card overdraft litigation, as mentioned above. Income tax expense was $121.4 million in 2011 compared to $96.2 million in 2010, resulting in effective tax rates of 32.1% and 30.3%, respectively.

The Company paid a special cash dividend of $1.43 per share, in addition to its regular quarterly cash dividend of $.22 per share, on December 17, 2012. In addition, it distributed a 5% stock dividend for the nineteenth consecutive year. All per share and average share data in this report has been restated to reflect the 2012 stock dividend.

Critical Accounting Policies

The Company's consolidated financial statements are prepared based on the application of certain accounting policies, the most significant of which are described in Note 1 to the consolidated financial statements. Certain of these policies require numerous estimates and strategic or economic assumptions that may prove inaccurate or be subject to variations which may significantly affect the Company's reported results and financial position for the current period or future periods. The use of estimates, assumptions, and judgments are necessary when financial assets and liabilities are required to be recorded at, or adjusted to reflect, fair value. Current economic conditions may require the use of additional estimates, and some estimates may be subject to a greater degree of uncertainty due to the current instability of the economy. 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.

Allowance for Loan Losses

The Company performs periodic and systematic detailed reviews of its loan portfolio to assess overall collectability. The level of the allowance for loan losses reflects the Company's estimate of the losses inherent in the loan portfolio at any point in time. While these estimates are based on substantive methods for determining allowance requirements, actual outcomes may differ significantly from estimated results, especially when determining allowances for business, construction and business real estate loans. These loans are normally larger and more complex, and their collection rates are harder to predict. Personal banking loans, including personal real estate, credit card and consumer loans, are individually smaller and perform in a more homogenous manner, making loss estimates more predictable. Further discussion of the methodology used in establishing the allowance is provided in the Allowance for Loan Losses section of Item 7 and in Note 1 to the consolidated financial statements.

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Valuation of Investment Securities
The Company carries its investment securities at fair value and employs valuation techniques which utilize observable inputs when those inputs are available. These observable inputs reflect assumptions market participants would use in pricing the security and are developed based on market data obtained from sources independent of the Company. When such information is not available, the Company employs valuation techniques which utilize unobservable inputs, or those which reflect the Company’s own assumptions about market participants, based on the best information available in the circumstances. These valuation methods typically involve cash flow and other financial modeling techniques. Changes in underlying factors, assumptions, estimates, or other inputs to the valuation techniques could have a material impact on the Company's future financial condition and results of operations. Assets and liabilities carried at fair value inherently result in more financial statement volatility. Under the fair value measurement hierarchy, fair value measurements are classified as Level 1 (quoted prices), Level 2 (based on observable inputs) or Level 3 (based on unobservable, internally-derived inputs), as discussed in more detail in Note 15 on Fair Value Measurements. Most of the available for sale investment portfolio is priced utilizing industry-standard models that consider various assumptions observable in the marketplace or which can be derived from observable data. Such securities totaled approximately $8.9 billion, or 93.9% of the available for sale portfolio at December 31, 2012, and were classified as Level 2 measurements. The Company also holds $126.4 million in auction rate securities. These were classified as Level 3 measurements, as no liquid market currently exists for these securities, and fair values were derived from internally generated cash flow valuation models which used unobservable inputs significant to the overall measurement.

Changes in the fair value of available for sale securities, excluding credit losses relating to other-than-temporary impairment, are reported in other comprehensive income. The Company periodically evaluates the available for sale portfolio for other-than-temporary impairment. Evaluation for other-than-temporary impairment is based on the Company’s intent to sell the security and whether it is likely that it will be required to sell the security before the anticipated recovery of its amortized cost basis. If either of these conditions is met, the entire loss (the amount by which the amortized cost exceeds the fair value) must be recognized in current earnings. If neither condition is met, but the Company does not expect to recover the amortized cost basis, the Company must determine whether a credit loss has occurred. This credit loss is the amount by which the amortized cost basis exceeds the present value of cash flows expected to be collected from the security. The credit loss, if any, must be recognized in current earnings, while the remainder of the loss, related to all other factors, is recognized in other comprehensive income.

The estimation of whether a credit loss exists and the period over which the security is expected to recover requires significant judgment. The Company must consider available information about the collectability of the security, including information about past events, current conditions, and reasonable forecasts, which includes payment structure, prepayment speeds, expected defaults, and collateral values. Changes in these factors could result in additional impairment, recorded in current earnings, in future periods.

At December 31, 2012, certain non-agency guaranteed mortgage-backed securities with a fair value of $101.7 million were identified as other-than-temporarily impaired. The cumulative credit-related impairment loss initially recorded on these securities amounted to $11.6 million, which was recorded in the consolidated statements of income.

The Company, through its direct holdings and its private equity subsidiaries, has numerous private equity investments, categorized as non-marketable securities in the accompanying consolidated balance sheets. These investments are reported at fair value and totaled $73.2 million at December 31, 2012. Changes in fair value are reflected in current earnings and reported in investment securities gains (losses), net, in the consolidated statements of income. Because there is no observable market data for these securities, fair values are internally developed using available information and management’s judgment, and the securities are classified as Level 3 measurements. Although management believes its estimates of fair value reasonably reflect the fair value of these securities, key assumptions regarding the projected financial performance of these companies, the evaluation of the investee company’s management team, and

other economic and market factors may affect the amounts that will ultimately be realized from these investments.

Accounting for Income Taxes

Accrued income taxes represent the net amount of current income taxes which are expected to be paid attributable to operations as of the balance sheet date. Deferred income taxes represent the expected future tax consequences of events that have been recognized in the financial statements or income tax returns. Current and deferred income taxes are reported as either a component of other assets or other liabilities in the consolidated balance sheets, depending on whether the balances are assets or liabilities. Judgment is required in applying generally accepted accounting principles in accounting for income taxes. The Company regularly monitors taxing authorities for changes in laws and regulations and their interpretations by the judicial systems. The aforementioned changes, as well as any changes that may result from the resolution of income tax examinations by federal and state taxing authorities, may impact the estimate of accrued income taxes and could materially impact the Company's financial position and results of operations.

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Net Interest Income

Net interest income, the largest source of revenue, results from the Company's lending, investing, borrowing, and deposit gathering activities. It is affected by both changes in the level of interest rates and changes in the amounts and mix of interest earning assets and interest bearing liabilities. 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.

(In thousands)	2012 Change due to Average Volume	2012 Average Rate	2012 Total	2011 Change due to Average Volume	2011 Average Rate	2011 Total
Interest income, fully taxable equivalent basis						
Loans	$7,898	$(24,813)	$(16,915)	$(18,171)	$(25,066)	$(43,237)
Loans held for sale	(882)	128	(754)	(5,292)	316	(4,976)
Investment securities:						
U.S. government and federal agency obligations	(1,231)	(3,777)	(5,008)	(1,787)	9,382	7,595
Government-sponsored enterprise obligations	1,223	(1,351)	(128)	1,112	78	1,190
State and municipal obligations	8,945	(6,877)	2,068	9,786	(3,267)	6,519
Mortgage-backed securities	9,548	(16,426)	(6,878)	29,458	(28,275)	1,183
Asset-backed securities	6,017	(4,600)	1,417	9,168	(17,204)	(8,036)
Other securities	(555)	3,016	2,461	(1,007)	1,521	514
Short-term federal funds sold and securities purchased under agreements to resell	30	(3)	27	31	(24)	7
Long-term securities purchased under agreements to resell	2,165	3,554	5,719	10,495	411	10,906
Interest earning deposits with banks	(147)	(1)	(148)	56	4	60
Total interest income	33,011	(51,150)	(18,139)	33,849	(62,124)	(28,275)
Interest expense						
Interest bearing deposits:						
Savings	78	(128)	(50)	61	169	230
Interest checking and money market	2,273	(9,397)	(7,124)	4,059	(7,731)	(3,672)
Time open and C.D.'s of less than $100,000	(1,445)	(1,989)	(3,434)	(4,722)	(6,797)	(11,519)
Time open and C.D.'s of $100,000 and over	(766)	(1,332)	(2,098)	763	(5,338)	(4,575)
Federal funds purchased and securities sold under agreements to repurchase	219	(1,152)	(933)	(90)	(753)	(843)
Other borrowings	7	(206)	(199)	(11,258)	(10)	(11,268)
Total interest expense	366	(14,204)	(13,838)	(11,187)	(20,460)	(31,647)
Net interest income, fully taxable equivalent basis	$32,645	$(36,946)	$(4,301)	$45,036	$(41,664)	$3,372

Net interest income totaled $639.9 million in 2012 compared to $646.1 million in 2011. On a tax equivalent basis, net interest income totaled $665.2 million and decreased $4.3 million from the previous year. This slight decrease was mainly the result of higher average investment securities balances and loan balances earning at a lower average rate than the previous year, partially offset by lower rates paid on deposits and borrowings. The net yield on earning assets (tax equivalent) was 3.41% in 2012 compared with 3.65% in the previous year.

During 2012, interest income on loans (tax equivalent, including loans held for sale) declined $17.7 million from 2011 due to a 25 basis point decrease in average rates earned, slightly offset by a $119.2 million increase in average loan balances. The average tax equivalent rate earned on the loan portfolio, including held for sale loans, was 4.82% compared to 5.07% in the previous year, reflecting the overall lower rate environment affecting the industry. Interest earned on business loans decreased $2.6 million as a result of a decline in rates of 15 basis points and was partially offset by a 1.8% increase in average balances. Interest on construction loans decreased $3.7 million due to a $63.5 million decline in average balances coupled with a 23 basis point decrease in average rates. Business real estate average loan balances increased $76.2 million, or 3.6%, while average rates earned decreased by 32 basis points, which together resulted in a net $3.3 million decrease in interest income. Interest income on personal real estate loans and consumer loans declined $3.4 million and $3.7 million, respectively, due to lower rates partially offset by higher average loan balances. Average consumer loan balances increased $61.8 million, which was mainly the result of increases of $123.8 million in auto loans and $33.7 million in fixed rate home equity loans. These increases were partially offset by a $103.9

million decrease in marine and recreational vehicle (RV) loans as that portfolio continues to pay down, as a result of the Company's exit from the marine/RV origination business in 2008. Interest earned on consumer credit card loans increased by $1.2 million due to a 41 basis point increase in the average rate earned, partly offset by the impact of a $16.0 million decrease in average balances.

Tax equivalent interest income on investment securities decreased by $6.1 million in 2012 due to a 38 basis point decrease in average rates earned on these investments, partially offset by a $992.7 million, or 12.3%, increase in average balances outstanding. The average rate earned on the total investment securities portfolio declined from 2.93% in 2011 to 2.55% in 2012. Interest income on mortgage-backed securities decreased $6.9 million in 2012 due to a 43 basis point decrease in rates earned on these securities, offset by an increase of 8.3%, or $296.5 million, in average balances. Interest on asset-backed securities increased slightly due to an increase in average balances of $481.3 million partially offset by a decline in rates of 16 basis points. Interest (tax exempt) on municipal securities increased $2.1 million due to higher average balances, which increased $202.1 million in 2012, partially offset by the impact of a 50 basis point decrease in average rates earned. Interest on U.S. government and federal agency securities decreased by $5.0 million in 2012, which was mostly due to a decrease in inflation income on inflation-protected securities. Interest on long-term resell agreements increased $5.7 million in 2012 compared to the prior year due to a $123.7 million increase in the average balances of these instruments, coupled with an increase in the average rate earned from 1.75% in the previous year to 2.15% in 2012.

During 2012, interest expense on deposits decreased $12.7 million compared to 2011. This was the result of lower rates on all deposit products coupled with a $402.2 million decline in average certificate of deposit balances, but partly offset by the effects of higher average balances of money market and interest checking accounts, which grew by $727.7 million. Average rates paid on deposit balances declined 13 basis points in 2012 to .30%. Interest expense on borrowings declined $1.1 million, mainly the result of average rates declining by 14 basis points to .33%, but partly offset by an increase of $151.0 million, or 14.6% in the average balances of federal funds purchased and securities sold under agreements to repurchase. The average rate paid on total interest bearing liabilities decreased to .30% compared to .43% in 2011.

During 2011, interest income on loans (tax equivalent, including loans held for sale) declined $48.2 million from 2010 due to a $787.4 million decrease in average loan balances, coupled with an 8 basis point decrease in average rates earned. The decrease in average loans compared to the previous year included a decrease of $554.0 million in average student loans, as a result of regulations, effective in mid 2010, which prohibit banks from originating federally guaranteed student loans. The average tax equivalent rate earned on the loan portfolio, including held for sale loans, was 5.07% compared to 5.15% in the previous year. Interest earned on business loans decreased $6.2 million as a result of a decline in rates of 25 basis points, which was offset by a slight increase in average balances. Interest on construction loans decreased $3.6 million due to a decline in average balances, but was offset by higher rates, while interest on personal real estate loans declined $7.5 million due to lower rates and balances. Interest on consumer loans decreased $14.1 million from the previous year due to a decline of $131.4 million in average consumer loans coupled with a 47 basis point decrease in rates earned. Interest earned on consumer credit card loans decreased by $4.7 million due to a combination of lower balances and rates earned on these loans.

Tax equivalent interest income on investment securities increased by $9.0 million in 2011 compared to 2010 due to a $1.4 billion increase in average balances outstanding, but was offset by lower rates earned on these investments. The average rate earned on the investment securities portfolio declined from 3.40% in 2010 to 2.93% in 2011. Interest income on mortgage-backed securities increased $1.2 million in 2011 due to growth in average balances of $734.6 million but was offset by a decline in rates earned on these securities. Interest on asset-backed securities declined $8.0 million due to a decline in rates of 70 basis points but was offset by higher average balances of $470.2 million. Interest (tax exempt) on municipal securities increased $6.5 million mainly due to higher average balances, which increased $208.1 million in 2011. Interest on U.S. government, agency and government-sponsored enterprise securities grew by $8.8 million in 2011, which was mostly due to an increase of $7.0 million in inflation income on inflation-protected securities. Interest on long-term resell agreements also increased $10.9 million in 2011 compared to the prior year, due to a $618.7 million increase in the average balances of these instruments in 2011.

Interest expense on deposits decreased $19.5 million in 2011 compared to 2010. This was mainly the result of lower rates on most deposit products coupled with a $283.5 million decline in average certificate of deposit balances, and partly offset by the effects of higher average balances of money market and interest checking accounts, which grew by $917.6 million. Average rates paid on deposit balances declined 21 basis points to .43% in 2011 from .64% in 2010. Interest expense on borrowings declined $12.1 million, mainly the result of lower average FHLB advances, which decreased $339.8 million, or 76.5%, due to scheduled maturities of advances and the early pay off of $125.0 million in the fourth quarter of 2010. The average rate paid on total interest bearing liabilities decreased to .43% compared to .71% in 2010.

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Provision for Loan Losses

The provision for loan losses totaled $27.3 million in 2012, which represented a decrease of $24.2 million from the 2011 provision of $51.5 million. Net loan charge-offs for the year totaled $39.3 million compared with $64.5 million in 2011, or a decrease of $25.2 million. The decrease in net loan charge-offs from the previous year was mainly the result of lower business, construction, consumer credit card and consumer losses, which declined $7.5 million, $7.2 million, $7.1 million and $4.0 million, respectively. The allowance for loan losses totaled $172.5 million at December 31, 2012, a decrease of $12.0 million compared to the prior year, and represented 1.75% of outstanding loans. The provision for loan losses is recorded to bring the allowance for loan losses to a level deemed adequate by management based on the factors mentioned in the following “Allowance for Loan Losses” section of this discussion.

Non-Interest Income

(Dollars in thousands)	2012	2011	2010	% Change '12-'11	'11-'10
Bank card transaction fees	$154,197	$157,077	$148,888	(1.8)%	5.5%
Trust fees	94,679	88,313	80,963	7.2	9.1
Deposit account charges and other fees	79,485	82,651	92,637	(3.8)	(10.8)
Capital market fees	21,066	19,846	21,098	6.1	(5.9)
Consumer brokerage services	10,162	10,018	9,190	1.4	9.0
Loan fees and sales	6,037	7,580	23,116	(20.4)	(67.2)
Other	34,004	27,432	29,219	24.0	(6.1)
Total non-interest income	$399,630	$392,917	$405,111	1.7%	(3.0)%
Non-interest income as a % of total revenue*	38.4%	37.8%	38.5%		
Total revenue per full-time equivalent employee	$220.8	$219.0	$211.1		

*Total revenue is calculated as net interest income plus non-interest income.

Non-interest income totaled $399.6 million, an increase of $6.7 million, or 1.7%, compared to $392.9 million in 2011. Bank card fees declined $2.9 million, or 1.8%, from last year, as a result of a decline in debit card interchange fees of $19.3 million, or 35.7% (mainly the effect of new pricing regulations effective in the fourth quarter of 2011), which was partly offset by continued growth in corporate card fees of $13.0 million, or 22.4%. Corporate card and debit card fees for 2012 totaled $70.8 million and $34.6 million, respectively. Merchant fees grew by 8.9% due to higher transaction volumes and totaled $26.2 million for the year, while credit card fees grew 5.9% and totaled $22.6 million. Trust fee income increased $6.4 million, or 7.2%, resulting mainly from growth in personal and institutional trust fees. The market value of total customer trust assets (on which fees are charged) totaled $30.2 billion at year end 2012 and grew 10.7% over year end 2011. Deposit account fees decreased $3.2 million, or 3.8%, primarily due to a decline in overdraft and return item fees of $6.5 million, while various other deposit fees increased $3.4 million. Overdraft fees comprised 43.3% of total deposit account fees in 2012, down from 49.5% in 2011. Corporate cash management fees comprised 40.3% of total deposit account fees in 2012 and were flat compared to 2011. Capital market fees increased $1.2 million, or 6.1%, resulting from growth in sales of mainly fixed income securities to correspondent banks and other commercial customers. Consumer brokerage services revenue increased $144 thousand, or 1.4%, due to growth in advisory fees, mostly offset by lower life insurance revenue. Loan fees and sales revenue was down $1.5 million, or 20.4%, due to a decline in mortgage banking revenue (mainly because the Company retained all first mortgage loan originations in 2012). Other non-interest income increased by $6.6 million, or 24.0%, mainly due to higher tax credit sales income, leasing revenue and net gains related to banking properties in 2012.

During 2011, non-interest income decreased $12.2 million, or 3.0%, from 2010 to $392.9 million. Bank card fees increased $8.2 million, or 5.5%, over 2010, primarily due to growth in transaction fees earned on corporate card and

merchant activity, which grew by 19.7% and 5.4%, respectively. Debit card fees declined $3.1 million, or 5.4%, as a result of new regulations for pricing debit card transactions, which were effective October 1, 2011. Debit card fees totaled $53.9 million in 2011 and comprised 34.3% of total bank card fees, while corporate card fees totaled $57.8 million and comprised 36.8% of total fees. Trust fee income increased $7.4 million, or 9.1%, as a result of growth in personal and institutional trust fees. The market value of total customer trust assets totaled $27.3 billion at year end 2011 and grew 8.9% over year end 2010. Deposit account fees decreased $10.0 million, or 10.8%, due mainly to lower overdraft fees resulting in part from new regulations in 2010. Overdraft fees comprised 49.5% of total deposit account fee income in 2011, down from 55.2% in 2010. Capital market fees decreased $1.3 million, or 5.9%, due to lower securities sales to correspondent banks and other commercial customers, while consumer brokerage services revenue increased by $828 thousand, or 9.0%, due to growth in advisory fees. Compared with 2010, loan fees and sales declined $15.5 million in 2011 due to a decline in gains on student loan sales, as the Company exited from the student loan origination business in 2010. Other income decreased $1.8 million largely due to higher write-downs in 2011 on various banking properties held for sale.

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Investment Securities Gains (Losses), Net

Net gains and losses on investment securities during 2012, 2011 and 2010 are shown in the table below. Included in these amounts are gains and losses arising from sales of bonds from the Company's available for sale portfolio, including credit-related losses on debt securities identified as other-than-temporarily impaired. Also shown below are gains and losses relating to non-marketable private equity investments, which are primarily held by the Parent's majority-owned private equity subsidiaries. These include fair value adjustments, in addition to gains and losses realized upon disposition. Portions of the fair value adjustments attributable to minority interests are reported as non-controlling interest in the consolidated statements of income and resulted in expense of $1.3 million and $2.6 million in 2012 and 2011, respectively, and income of $108 thousand in 2010.

Net securities gains of $4.8 million were recorded in 2012, which include $6.0 million in gains resulting from sales and fair value adjustments related to private equity investments. Partly offsetting these gains were credit-related impairment losses of $1.5 million 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 $101.7 million at December 31, 2012. The cumulative credit-related impairment losses initially recorded on these securities totaled $11.6 million.

Net securities gains of $10.8 million were recorded in 2011, compared to net losses of $1.8 million in 2010. Gains of $13.2 million in 2011 resulted from sales and fair value adjustments related to private equity investments. Partly offsetting these gains were credit-related other-than-temporary impairment (OTTI) losses of $2.5 million. Losses in 2010 were comprised of $5.1 million in OTTI losses, partly offset by $3.5 million of net gains resulting from sales from the available for sale portfolio, mainly in municipal and mortgage-backed bonds.

(In thousands)	2012	2011	2010
Available for sale:			
Municipal bonds	$16	$177	$1,172
Corporate bonds	—	—	498
Agency mortgage-backed bonds	342	—	1,434
Non-agency mortgage-backed bonds	—	—	384
OTTI losses on non-agency mortgage-backed bonds	(1,490)	(2,537)	(5,069)
Non-marketable:			
Private equity investments	5,960	13,172	(204)
Total investment securities gains (losses), net	$4,828	$10,812	$(1,785)

Non-Interest Expense

(Dollars in thousands)	2012	2011	2010	% Change '12-'11	% Change '11-'10
Salaries	$302,675	$293,318	$292,675	3.2 %	.2 %
Employee benefits	58,224	52,007	53,875	12.0	(3.5)
Net occupancy	45,534	46,434	46,987	(1.9)	(1.2)
Equipment	20,147	22,252	23,324	(9.5)	(4.6)
Supplies and communication	22,321	22,448	27,113	(.6)	(17.2)
Data processing and software	73,798	68,103	67,935	8.4	.2
Marketing	15,106	16,767	18,161	(9.9)	(7.7)
Deposit insurance	10,438	13,123	19,246	(20.5)	(31.8)
Debit overdraft litigation	—	18,300	—	(100.0)	100.0
Debt extinguishment	—	—	11,784	—	(100.0)
Other	70,226	64,497	70,034	8.9	(7.9)
Total non-interest expense	$618,469	$617,249	$631,134	.2 %	(2.2)%
Efficiency ratio	59.3 %	59.1 %	59.7 %		
	58.4 %	55.9 %	54.9 %		

Salaries and benefits as a % of total non-interest expense			
Number of full-time equivalent employees	4,708	4,745	4,979

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Non-interest expense was $618.5 million in 2012, an increase of $1.2 million, or .2%, over the previous year. Salaries and benefits expense increased by $15.6 million, or 4.5%, largely due to higher salaries, incentive compensation, medical and retirement expense. Full-time equivalent employees totaled 4,708 at December 31, 2012, a decline of .8% from the prior year. Occupancy expense declined $900 thousand, or 1.9%, primarily resulting from lower depreciation and outside services expense, partly offset by a decline in rent income. Equipment expense decreased $2.1 million, or 9.5%, also due to lower depreciation expense. Supplies and communication expense decreased slightly, while marketing expense was lower by $1.7 million, or 9.9%. Data processing and software expense increased $5.7 million, or 8.4%, mainly due to higher bank card processing expense. Deposit insurance expense declined $2.7 million, or 20.5%, as a result of new FDIC assessment rules which became effective in the second quarter of 2011. Other non-interest expense increased $5.7 million, or 8.9%, mainly due to the accrual in 2012 of $5.2 million for anticipated costs resulting from the proposed settlement of certain Visa-related interchange litigation. Also, during 2011 the Company's indemnification obligation related to Visa litigation was reduced by $4.4 million, and a similar decrease to expense did not occur in 2012. Partly offsetting these increases to other non-interest expense in 2012 were reductions of $853 thousand in regulatory examination fees and $788 thousand in intangible asset amortization, in addition to an increase of $1.7 million in deferred loan origination costs.

In 2011, non-interest expense was $617.2 million, a decrease of $13.9 million, or 2.2%, from the previous year. In December 2011, the Company reached a class-wide settlement on a debit card overdraft lawsuit. The settlement provided for a payment of $18.3 million, which was recorded as expense in 2011. Salaries and benefits expense decreased by $1.2 million, or .4%, due to lower salary expense, medical insurance costs and pension plan expense, partly offset by higher incentive compensation. Total salaries expense was up $643 thousand, or .2%, over 2010, while the number of full-time equivalent employees declined 4.7% to 4,745 at December 31, 2011. Occupancy costs decreased $553 thousand, or 1.2%, primarily resulting from lower depreciation expense and outside services expense. Equipment expense decreased $1.1 million, or 4.6%, due to lower equipment rental and service contract expense. Supplies and communication expense declined $4.7 million, or 17.2%, due to lower costs for customer checks, postage, paper supplies and telephone and network costs. Data processing and software costs increased slightly due to higher bank card processing costs, which were partly offset by lower student loan servicing costs. Marketing expense declined $1.4 million, or 7.7%, while deposit insurance was lower by $6.1 million, or 31.8%, mainly because of the FDIC rule change mentioned above. Other non-interest expense decreased $5.5 million, or 7.9%, largely due to a decline in foreclosed property costs of $6.7 million, which was due to lower write-downs to fair value, sale losses and other holding costs in 2011. Additionally, the Company's indemnification obligation related to Visa litigation was reduced by $4.4 million in both 2011 and 2010 due to funding actions by Visa.

Income Taxes

Income tax expense was $127.2 million in 2012, compared to $121.4 million in 2011 and $96.2 million in 2010. The increase in income tax expense over 2011 was proportional to the increase in pre-tax income. The effective tax rate, including the effect of non-controlling interest, in 2012 and 2011 was 32.1% compared to 30.3% in 2010. The Company's effective tax rate in 2012 and 2011 was higher than 2010 primarily due to increased state and local taxes. The Company’s effective tax rates in the years noted above were lower than the federal statutory rate of 35% mainly due to tax-exempt interest on state and local municipal obligations.

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Financial Condition

Loan Portfolio Analysis

Classifications of consolidated loans by major category at December 31 for each of the past five years are shown in the table below. This portfolio consists of loans which were acquired or originated with the intent of holding to their maturity. Loans held for sale are separately discussed in a following section. A schedule of average balances invested in each loan category below appears on page 50.

	Balance at December 31				
(In thousands)	2012	2011	2010	2009	2008
Commercial:					
Business	$3,134,801	$2,808,265	$2,957,043	$2,877,936	$3,404,371
Real estate — construction and land	355,996	386,598	460,853	665,110	837,369
Real estate — business	2,214,975	2,180,100	2,065,837	2,104,030	2,137,822
Personal banking:					
Real estate — personal	1,584,859	1,428,777	1,440,386	1,537,687	1,638,553
Consumer	1,289,650	1,114,889	1,164,327	1,333,763	1,615,455
Revolving home equity	437,567	463,587	477,518	489,517	504,069
Student	—	—	—	331,698	358,049
Consumer credit card	804,245	788,701	831,035	799,503	779,709
Overdrafts	9,291	6,561	13,983	6,080	7,849
Total loans	$9,831,384	$9,177,478	$9,410,982	$10,145,324	$11,283,246

The contractual maturities of loan categories at December 31, 2012, and a breakdown of those loans between fixed rate and floating rate loans are as follows:

	Principal Payments Due			
(In thousands)	In One Year or Less	After One Year Through Five Years	After Five Years	Total
Business	$1,730,827	$1,127,318	$276,656	$3,134,801
Real estate — construction and land	221,623	129,882	4,491	355,996
Real estate — business	575,510	1,414,276	225,189	2,214,975
Real estate — personal	150,142	432,700	1,002,017	1,584,859
Total business and real estate loans	$2,678,102	$3,104,176	$1,508,353	7,290,631
Consumer (1)				1,289,650
Revolving home equity (2)				437,567
Consumer credit card (3)				804,245
Overdrafts				9,291
Total loans				$9,831,384
Loans with fixed rates	$625,216	$1,810,282	$684,576	$3,120,074
Loans with floating rates	2,052,886	1,293,894	823,777	4,170,557
Total business and real estate loans	$2,678,102	$3,104,176	$1,508,353	$7,290,631

(1) Consumer loans with floating rates totaled $129.8 million.
(2) Revolving home equity loans with floating rates totaled $431.4 million.
(3) Consumer credit card loans with floating rates totaled $621.7 million.

Total loans at December 31, 2012 were $9.8 billion, an increase of $653.9 million, or 7.1%, over balances at December 31, 2011. The growth in loans during 2012 occurred in business, consumer, business and personal real estate and credit card loans, partly offset by declines in construction and revolving home equity loans. Business loans increased $326.5 million, or 11.6%, reflecting growth in lease, tax-free and wholesale auto floor plan loans. Business

real estate loans increased 1.6% as demand for new loans remained soft. Construction loans decreased $30.6 million, or 7.9%, and continued to be affected by low demand during most of the year; however, modest growth occurred in the fourth quarter of the year as the housing industry saw some improvement. Personal real estate loans increased $156.1 million, or 10.9%, as the Company retained all first mortgage loan originations in 2012. Consumer loans were higher by $174.8 million, or 15.7%, primarily due to strong demand for consumer automobile lending, while marine and recreational vehicle lending, which the Company ceased in 2008, continued to run off. Revolving home equity

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loans decreased $26.0 million, or 5.6%, due to fewer new account activations. Consumer credit card loans increased by $15.5 million, or 2.0%, mainly due to greater usage by existing customers.

The Company currently generates approximately 33% of its loan portfolio in the St. Louis market, 28% in the Kansas City market, and 39% in other regional markets. The portfolio is diversified from a business and retail standpoint, with 58% in loans to businesses and 42% in loans to consumers. A balanced approach to loan portfolio management and an historical aversion toward credit concentrations, from an industry, geographic and product perspective, have contributed to low levels of problem loans and loan losses.

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 approximately $483.1 million and $538.0 million at December 31, 2012 and 2011, respectively, with an additional $1.1 billion in unfunded commitments at each period end.

Commercial Loans

Business

Total business loans amounted to $3.1 billion at December 31, 2012 and include loans used mainly to fund customer accounts receivable, inventories, and capital expenditures. The business loan portfolio includes tax advantaged financings which carry tax free interest rates. These loans totaled $435.2 million at December 31, 2012 and increased 8.5% over December 31, 2011. The portfolio also includes direct financing and sales type leases totaling $311.6 million, which are used by commercial customers to finance capital purchases ranging from computer equipment to office and transportation equipment. These leases increased $69.8 million, or 28.9%, over 2011 and comprise 3.2% of the Company's total loan portfolio. Also included in this portfolio are corporate card loans, which totaled $209.3 million at December 31, 2012. These loans, which increased by 25.4% in 2012, are made in conjunction with the Company's corporate card business, which assists the increasing number of businesses that are shifting from paper checks to a credit card payment system in order to automate payment processes. These loans are generally short-term, with outstanding balances averaging between 7 to 13 days in duration, which helps to limit risk in these loans.

Business loans, excluding corporate card loans, are made primarily to customers in the regional trade area of the Company, generally the central Midwest, encompassing the states of Missouri, Kansas, Illinois, and nearby Midwestern markets, including Iowa, Oklahoma, Colorado and Ohio. This portfolio is diversified from an industry standpoint and includes businesses engaged in manufacturing, wholesaling, retailing, agribusiness, insurance, financial services, public utilities, healthcare, and other service businesses. Emphasis is upon middle-market and community businesses with known local management and financial stability. Consistent with management's strategy and emphasis upon relationship banking, most borrowing customers also maintain deposit accounts and utilize other banking services. Net loan recoveries in this category totaled $2.5 million in 2012, while net loan charge-offs of $5.0 million were recorded in 2011. Net loan recoveries mainly resulted from the receipt of $3.6 million on two non-accrual business loans during the second quarter of 2012. Non-accrual business loans were $13.1 million (.4% of business loans) at December 31, 2012 compared to $25.7 million at December 31, 2011. The decrease was largely due to the payoff of one non-accrual loan of $8.0 million.

Real Estate-Construction and Land

The portfolio of loans in this category amounted to $356.0 million at December 31, 2012 and comprised 3.6% of the Company's total loan portfolio. These loans are predominantly made to businesses in the local markets of the Company's banking subsidiary. Commercial construction and land development loans totaled $225.6 million, or 63.4% of total construction loans at December 31, 2012. Commercial construction loans are made during the construction phase for small and medium-sized office and medical buildings, manufacturing and warehouse facilities, apartment

complexes, shopping centers, hotels and motels, and other commercial properties. Exposure to larger, speculative commercial properties remains low. Commercial land development loans relate to land owned or developed for use in conjunction with business properties. Residential construction and land development loans at December 31, 2012 totaled $130.4 million, or 36.6% of total construction loans. The largest percentage of residential construction and land development loans are for projects located in the Kansas City and St. Louis metropolitan areas. Credit risk in this sector has been high over the last few years, especially in residential land development lending, as a result of the weak housing industry. However, in 2012, net loan recoveries of $283 thousand were recorded, compared to net charge-offs of $7.0 million in 2011, reflecting an improved housing environment. Construction and land development loans on non-accrual status declined to $13.7 million at year end 2012 compared to $22.8 million at year end 2011 with approximately 50% of the non-accrual balance at year end 2012 comprised of loans to three individual borrowers. The Company’s watch list, which includes special

mention and substandard categories, included $13.8 million of residential land and construction loans which are being closely monitored.

Real Estate-Business

Total business real estate loans were $2.2 billion at December 31, 2012 and comprised 22.5% of the Company's total loan portfolio. This category includes mortgage loans for small and medium-sized office and medical buildings, manufacturing and warehouse facilities, shopping centers, hotels and motels, churches, and other commercial properties. Emphasis is placed on owner-occupied (46.7% of this portfolio) and income producing commercial real estate properties, which present lower risk levels. The borrowers and/or the properties are generally located in local and regional markets. Additional information about loans by category is presented on page 32. At December 31, 2012, non-accrual balances amounted to $17.3 million, or .8%, of the loans in this category, down from $19.4 million at year end 2011. The Company experienced net charge-offs of $5.1 million in 2012 (.2% of average business real estate loans), compared to net charge-offs of $3.6 million in 2011. The increase in charge-offs over the prior year was mainly due to a $1.5 million charge-off on a loan to one specific borrower.

Personal Banking Loans

Real Estate-Personal

At December 31, 2012, there were $1.6 billion in outstanding personal real estate loans, which comprised 16.1% of the Company's total loan portfolio. The mortgage loans in this category are mainly for owner-occupied residential properties. The Company originates both adjustable rate and fixed rate mortgage loans. The Company retains adjustable rate mortgage loans, and in 2012 retained all fixed rate loans as directed by its Asset/Liability Management Committee, given historically low concentrations of these loans. The Company originates its loans and does not purchase any from outside parties or brokers. Further, it has never maintained or promoted subprime or reduced document products. At December 31, 2012, 40% of the portfolio was comprised of adjustable rate loans while 60% was comprised of fixed rate loans. Levels of mortgage loan origination activity increased in 2012 compared to 2011, with originations of $414 million in 2012 compared with $223 million in 2011. Growth in mortgage loan originations was the result of improved demand for housing, in addition to low interest rates, which also generated greater loan demand. The Company has experienced lower loan losses in this category than many others in the industry and believes this is partly because of its conservative underwriting culture, stable markets, and the fact that it does not offer subprime lending products or purchase loans from brokers. Net loan charge-offs for 2012 amounted to $1.4 million, compared to $2.8 million in the previous year. The non-accrual balances of loans in this category decreased to $6.9 million at December 31, 2012, compared to $7.6 million at year end 2011.

Consumer

Consumer loans consist of auto, marine, tractor/trailer, recreational vehicle (RV), fixed rate home equity, and other consumer installment loans. These loans totaled $1.3 billion at year end 2012. Approximately 62% of consumer loans outstanding were originated indirectly from auto and other dealers, while the remaining 38% were direct loans made to consumers. Approximately 44% of the consumer portfolio consists of automobile loans, 25% in marine and RV loans and 16% in fixed rate home equity lending. As mentioned above, total consumer loans increased by $174.8 million in 2012 as a result of growth in auto lending of $212.0 million, or 59%, partly offset by the run-off of $92.3 million in marine and RV loans. Net charge-offs on consumer loans were $8.1 million in 2012 compared to $12.2 million in 2011. Net charge-offs decreased to .7% of average consumer loans in 2012 compared to 1.1% in 2011. Consumer loan net charge-offs included marine and RV loan net charge-offs of $6.6 million, which were 1.8% of average marine and RV loans in 2012, compared to 2.1% in 2011.

Revolving Home Equity

Revolving home equity loans, of which 99% are adjustable rate loans, totaled $437.6 million at year end 2012. An additional $651.3 million was available in unused lines of credit, which can be drawn at the discretion of the borrower. Home equity loans are secured mainly by second mortgages (and less frequently, first mortgages) on

residential property of the borrower. The underwriting terms for the home equity line product permit borrowing availability, in the aggregate, generally up to 80% or 90% of the appraised value of the collateral property at the time of origination. Net charge-offs totaled $1.8 million, or .4% of average revolving home equity loans, compared to $1.7 million in 2011.

Consumer Credit Card

Total consumer credit card loans amounted to $804.2 million at December 31, 2012 and comprised 8.2% of the Company’s total loan portfolio. The credit card portfolio is concentrated within regional markets served by the Company. The Company offers a variety of credit card products, including affinity cards, rewards cards, and standard and premium credit cards, and emphasizes its credit card relationship product, Special Connections. Approximately 61% of the households in Missouri that own a Commerce credit card product also maintain a deposit relationship with the subsidiary bank. At December 31, 2012, approximately 77% of

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the outstanding credit card loan balances had a floating interest rate, compared to 69% in the prior year. Net charge-offs amounted to $24.5 million in 2012, a decline of $7.1 million from $31.6 million in 2011. The ratio of credit card loan net charge-offs to total average credit card loans totaled 3.4% in 2012 compared to 4.2% in 2011. These ratios remain below national loss averages in those years.

Loans Held for Sale

Total loans held for sale at December 31, 2012 were $8.8 million, a decrease of $22.2 million from $31.1 million at year end 2011. These have historically consisted of federally guaranteed student loans, which the Company no longer originates, and fixed-rate personal real estate loans, which the Company no longer actively sells to third parties. The balance at December 31, 2012 was comprised solely of student loans.

Allowance for Loan Losses

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 reserves needed for pools of loans.

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

Loans which are not individually evaluated are segregated by loan type and sub-type and are collectively evaluated. These loans include commercial loans (business, construction and business real estate) which have been graded pass, special mention or substandard and all personal banking loans, except personal real estate loans on non-accrual status. Collectively-evaluated loans include certain troubled debt restructurings with similar risk characteristics. Allowances determined for personal banking loans, which are generally smaller balance homogeneous type loans, use consistent methodologies which consider historical and current loss trends, delinquencies and current economic conditions. Allowances for commercial type loans, which are generally larger and more complex in structure with more unpredictable loss characteristics, use methods which consider historical and current loss trends, current loan grades, delinquencies, industry concentrations, economic conditions throughout the Company's markets as monitored by Company credit officers, and general economic conditions.

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

At December 31, 2012, the allowance for loan losses was $172.5 million compared to a balance at year end 2011 of $184.5 million. Total loans delinquent 90 days or more and still accruing were $15.3 million at December 31, 2012, a

small increase of $389 thousand compared to year end 2011. Non-accrual loans at December 31, 2012 were $51.4 million, a decrease of $24.1 million from the prior year and were mainly comprised of $17.3 million of business real estate loans, $13.7 million of construction loans and $13.1 million of business loans. As the result of improving credit trends noted in the Company's analysis of the allowance, the provision for loan losses was $12.0 million less than net charge-offs for the year, thereby reducing the allowance for loan losses to $172.5 million. The percentage of allowance to loans, excluding loans held for sale, decreased to 1.75% at December 31, 2012 compared to 2.01% at year end 2011 as a result of the decrease in the allowance balance. The percentage of allowance to non-accrual loans was 336% at December 31, 2012.

Net loan charge-offs totaled $39.3 million in 2012, representing a $25.2 million decrease compared to net charge-offs of $64.5 million in 2011. Net recoveries on business loans were $2.5 million in 2012, compared to net charge-offs of $5.0 million in 2011. Net recoveries on construction and land loans were $283 thousand compared to net charge-offs of $7.0 million in 2011. Net

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charge-offs related to consumer loans decreased $4.0 million to $8.1 million in 2012, which included net charge-offs of $6.6 million related to marine and RV loans. Additionally, net charge-offs related to consumer credit cards were $24.5 million in 2012 compared to $31.6 million in 2011. Approximately 62.3% of total net loan charge-offs during 2012 were related to consumer credit card loans compared to 49.0% during 2011. Net consumer credit card charge-offs decreased to 3.4% of average consumer credit card loans in 2012 compared to 4.2% in 2011, as a result of an improving economy and lower delinquencies.

The ratio of net charge-offs to total average loans outstanding in 2012 was .42% compared to .70% in 2011 and 1.00% in 2010. The provision for loan losses in 2012 was $27.3 million, compared to provisions of $51.5 million in 2011 and $100.0 million in 2010.

The Company considers the allowance for loan losses of $172.5 million adequate to cover losses inherent in the loan portfolio at December 31, 2012.

The schedules which follow summarize the relationship between loan balances and activity in the allowance for loan losses:

	Years Ended December 31				
(Dollars in thousands)	2012	2011	2010	2009	2008
Loans outstanding at end of year[(A)]	$9,831,384	$9,177,478	$9,410,982	$10,145,324	$11,283,246
Average loans outstanding[(A)]	$9,379,316	$9,222,568	$9,698,670	$10,629,867	$10,935,858
Allowance for loan losses:					
Balance at beginning of year	$184,532	$197,538	$194,480	$172,619	$133,586
Additions to allowance through charges to expense	27,287	51,515	100,000	160,697	108,900
Loans charged off:					
Business	2,809	6,749	8,550	15,762	7,820
Real estate — construction and land	1,244	7,893	15,199	34,812	6,215
Real estate — business	7,041	4,176	4,780	5,957	2,293
Real estate — personal	2,416	3,217	2,484	3,150	1,765
Consumer	12,288	16,052	24,587	35,979	26,229
Revolving home equity	2,044	1,802	2,014	1,197	447
Consumer credit card	33,098	39,242	54,287	54,060	35,825
Overdrafts	2,221	2,254	2,672	3,493	4,499
Total loans charged off	63,161	81,385	114,573	154,410	85,093
Recoveries of loans previously charged off:					
Business	5,306	1,761	3,964	2,925	3,406
Real estate — construction and land	1,527	943	193	720	—
Real estate — business	1,933	613	722	709	117
Real estate — personal	990	445	428	363	51
Consumer	4,161	3,896	4,108	3,772	4,782
Revolving home equity	240	135	39	7	18
Consumer credit card	8,623	7,625	6,556	4,785	4,309
Overdrafts	1,094	1,446	1,621	2,293	2,543
Total recoveries	23,874	16,864	17,631	15,574	15,226
Net loans charged off	39,287	64,521	96,942	138,836	69,867
Balance at end of year	$172,532	$184,532	$197,538	$194,480	$172,619
Ratio of allowance to loans at end of year	1.75 %	2.01 %	2.10 %	1.92 %	1.53 %

Ratio of provision to average loans outstanding	.29 %	.56 %	1.03 %	1.51 %	1.00 %

(A) Net of unearned income, before deducting allowance for loan losses, excluding loans held for sale.

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	Years Ended December 31				
	2012	2011	2010	2009	2008
Ratio of net charge-offs (recoveries) to average loans outstanding, by loan category:					
Business	(.08)%	.17%	.16%	.41%	.13%
Real estate — construction and land	(.08)	1.66	2.69	4.61	.89
Real estate — business	.23	.17	.20	.24	.10
Real estate — personal	.09	.19	.14	.18	.11
Consumer	.69	1.09	1.64	2.20	1.28
Revolving home equity	.40	.36	.41	.24	.09
Consumer credit card	3.35	4.23	6.28	6.77	4.06
Overdrafts	18.40	11.62	14.42	12.27	16.40
Ratio of total net charge-offs to total average loans outstanding	.42%	.70%	1.00%	1.31%	.64%

The following schedule provides a breakdown of the allowance for loan losses by loan category and the percentage of each loan category to total loans outstanding at year end:

(Dollars in thousands)	2012		2011		2010		2009		2008	
	Loan Loss Allowance Allocation	% of Loans to Total Loans	Loan Loss Allowance Allocation	% of Loans to Total Loans	Loan Loss Allowance Allocation	% of Loans to Total Loans	Loan Loss Allowance Allocation	% of Loans to Total Loans	Loan Loss Allowance Allocation	% of Loans to Total Loans
Business	$47,729	31.9%	$49,217	30.5%	$47,534	31.4%	$40,455	28.4%	$35,185	30.2%
RE — construction and land	20,555	3.6	28,280	4.2	21,316	4.9	33,659	6.6	24,714	7.4
RE — business	37,441	22.5	45,000	23.8	51,096	22.0	31,515	20.7	26,081	19.0
RE — personal	3,937	16.1	3,701	15.6	4,016	15.3	5,435	15.2	4,985	14.5
Consumer	15,165	13.1	15,369	12.1	19,449	12.4	30,257	13.1	30,503	14.3
Revolving home equity	4,861	4.5	2,220	5.1	2,502	5.1	1,737	4.8	1,445	4.4
Student	—	—	—	—	—	—	229	3.3	—	3.2
Consumer credit card	41,926	8.2	39,703	8.6	50,532	8.8	49,923	7.9	47,993	6.9
Overdrafts	918	.1	1,042	.1	1,093	.1	1,270	—	1,713	.1
Total	$172,532	100.0%	$184,532	100.0%	$197,538	100.0%	$194,480	100.0%	$172,619	100.0%

Risk Elements of Loan Portfolio

Management reviews the loan portfolio continuously for evidence of problem loans. During the ordinary course of business, management becomes aware of borrowers that may not be able to meet the contractual requirements of loan agreements. Such loans are placed under close supervision with consideration given to placing the loan on non-accrual status, the need for an additional allowance for loan loss, and (if appropriate) partial or full loan charge-off. Loans are placed on non-accrual status when management does not expect to collect payments consistent with acceptable and agreed upon terms of repayment. After a loan is placed on non-accrual status, any interest previously accrued but not yet collected is reversed against current income. Interest is included in income only as received and only after all previous loan charge-offs have been recovered, so long as management is satisfied there is no impairment of collateral values. The loan is returned to accrual status only when the borrower has brought all past due principal and interest payments current, and, in the opinion of management, the borrower has demonstrated the ability to make future payments of principal and interest as scheduled. 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 comprised of those personal banking loans that are exempt under regulatory rules from being classified as non-accrual. Consumer installment loans and related accrued interest are normally charged down to the fair value of related collateral (or are charged off in full if no collateral) once the loans are more than 120 days delinquent. Credit card loans and the related accrued interest are charged off when the receivable is more than 180 days past due.

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The following schedule shows non-performing assets and loans past due 90 days and still accruing interest.

	December 31				
(Dollars in thousands)	2012	2011	2010	2009	2008
Total non-accrual loans	$51,410	$75,482	$85,275	$106,613	$72,896
Real estate acquired in foreclosure	13,453	18,321	12,045	10,057	6,181
Total non-performing assets	$64,863	$93,803	$97,320	$116,670	$79,077
Non-performing assets as a percentage of total loans	.66 %	1.02 %	1.03 %	1.15 %	.70 %
Non-performing assets as a percentage of total assets	.29 %	.45 %	.53 %	.64 %	.45 %
Total past due 90 days and still accruing interest	$15,347	$14,958	$20,466	$42,632	$39,964

The table below shows the effect on interest income in 2012 of loans on non-accrual status at year end.

(In thousands)	
Gross amount of interest that would have been recorded at original rate	$4,606
Interest that was reflected in income	561
Interest income not recognized	$4,045

Non-accrual loans, which are also classified as impaired, totaled $51.4 million at year end 2012, a decrease of $24.1 million from the balance at year end 2011. The decrease in non-accrual loans occurred mainly in the business and real estate construction and land loan categories, which decreased $12.7 million and $9.1 million, respectively. The decline in non-accrual loans was largely attributable to improved credit quality in the loan portfolio. At December 31, 2012, non-accrual loans were comprised primarily of business real estate loans (33.7%), construction and land real estate loans (26.6%), and business loans (25.4%). Foreclosed real estate decreased $4.9 million to a total of $13.5 million at year end 2012. The decline was mainly due to a partial sale of a construction project. Total non-performing assets remain low compared to the overall banking industry in 2012, with the non-performing loans to total loans ratio at .52% at December 31, 2012. Loans past due 90 days and still accruing interest increased $389 thousand at year end 2012 compared to 2011. 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 of 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 $141.9 million at December 31, 2012 compared with $250.7 million at December 31, 2011, resulting in a decrease of $108.8 million, or 43.4%. The change in potential problem loans was largely due to decreases of $58.3 million in business real estate loans, $30.3 million in business loans, and $20.9 million in construction and land real estate loans.

	December 31	
(In thousands)	2012	2011
Potential problem loans:		
Business	$44,881	$75,213
Real estate – construction and land	33,762	54,696
Real estate – business	55,362	113,652
Real estate – personal	7,891	6,900
Consumer	—	208
Total potential problem loans	$141,896	$250,669

At December 31, 2012, the Company had approximately $94.0 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. Of this balance,

$28.5 million have been placed on non-accrual status. Of the remaining $65.5 million, approximately $40.3 million were commercial loans (business, construction and business real estate) classified as substandard, which were renewed at interest rates that were not judged to be market rates for new debt with similar risk. These loans are performing under their modified terms, and the Company believes it probable that all amounts due under the modified terms of the agreements will be collected. However, because of their substandard classification, they are included as potential problem loans in the table above. An additional $14.7 million in troubled debt restructurings were

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composed of certain credit card loans under various debt management and assistance programs. Other restructured loans include $10.4 million of personal banking loans which were not reaffirmed in bankruptcy, on which the borrowers are continuing to make payments.

Loans with Special Risk Characteristics

Management relies primarily on an internal risk rating system, in addition to delinquency status, to assess risk in the loan portfolio, and these statistics are presented in Note 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. Construction and land loans and business real estate loans are subject to higher risk as a result of the current weak economic climate and issues in the housing industry. Certain personal real estate products (residential first mortgages and home equity loans) have contractual features that could increase credit exposure in a market of declining real estate prices, when interest rates are steadily increasing, or when a geographic area experiences an economic downturn. For these personal real estate loans, higher risks could exist when 1) loan terms require a minimum monthly payment that covers only interest, or 2) loan-to-collateral value (LTV) ratios at origination are above 80%, with no private mortgage insurance. Information presented below for personal real estate and home equity loans is based on LTV ratios which were calculated with valuations at loan origination date. The Company does not attempt to obtain updated appraisals or valuations unless the loans become significantly delinquent or are in the process of being foreclosed upon. For credit monitoring purposes, the Company relies on delinquency monitoring along with obtaining refreshed FICO scores, and in the case of home equity loans, reviewing line utilization and credit bureau information annually. This has remained an effective means of evaluating credit trends and identifying problem loans, partly because the Company offers standard, conservative lending products.

Real Estate - Construction and Land Loans

The Company’s portfolio of construction loans, as shown in the table below, amounted to 3.6% of total loans outstanding at December 31, 2012.

(Dollars in thousands)	December 31, 2012	% of Total	% of Total Loans	December 31, 2011	% of Total	% of Total Loans
Residential land and land development	$61,794	17.4 %	.6 %	$70,708	18.3 %	.8 %
Residential construction	68,590	19.2	.7	70,009	18.1	.7
Commercial land and land development	83,491	23.5	.9	97,379	25.2	1.1
Commercial construction	142,121	39.9	1.4	148,502	38.4	1.6
Total real estate – construction and land loans	$355,996	100.0 %	3.6 %	$386,598	100.0 %	4.2 %

Real Estate – Business Loans

Total business real estate loans were $2.2 billion at December 31, 2012 and comprised 22.5% 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. Approximately 47% of these loans were for owner-occupied real estate properties, which present lower risk profiles.

(Dollars in thousands)	December 31, 2012	% of Total	% of Total Loans	December 31, 2011	% of Total	% of Total Loans
Owner-occupied	$1,035,407	46.7 %	10.5 %	$1,057,652	48.5 %	11.5 %
Office	269,756	12.2	2.7	270,200	12.3	3.0
Retail	245,021	11.1	2.5	226,447	10.4	2.5

Multi-family	184,208	8.3	1.9	174,285	8.0	1.9
Hotels	155,392	7.0	1.6	119,039	5.5	1.3
Farm	123,613	5.6	1.3	121,966	5.6	1.3
Industrial	110,645	5.0	1.1	98,092	4.5	1.1
Other	90,933	4.1	.9	112,419	5.2	1.2
Total real estate - business loans	$2,214,975	100.0 %	22.5 %	$2,180,100	100.0 %	23.8 %

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Real Estate - Personal Loans

The Company’s $1.6 billion personal real estate loan portfolio is composed of first mortgages on residential real estate. The majority of this portfolio is comprised of approximately $1.4 billion of loans made to the retail customer base and includes both adjustable rate and fixed rate mortgage loans. As shown in Note 2 to the consolidated financial statements, 5.5% of the retail-based portfolio has FICO scores of less than 660, and delinquency levels have been low. Loans of approximately $12.7 million in this portfolio were structured with interest only payments. Interest only loans are typically made to high net-worth borrowers and generally have low LTV ratios or have additional collateral pledged to secure the loan, and, therefore, they are not perceived to represent above normal credit risk. Loans originated with interest only payments were not made to "qualify" the borrower for a lower payment amount. A small portion of the total portfolio is composed of personal real estate loans made to commercial customers, which totaled $224.5 million at December 31, 2012.

The following table presents information about the retail-based personal real estate loan portfolio for 2012 and 2011.

(Dollars in thousands)	2012 Principal Outstanding at December 31	% of Loan Portfolio		2011 Principal Outstanding at December 31	% of Loan Portfolio	
Loans with interest only payments	$12,730	.9	%	$15,186	1.3	%
Loans with no insurance and LTV:						
Between 80% and 90%	76,023	5.6		78,446	6.5	
Between 90% and 95%	26,871	2.0		25,131	2.1	
Over 95%	33,290	2.4		38,995	3.2	
Over 80% LTV with no insurance	136,184	10.0		142,572	11.8	
Total loan portfolio from which above loans were identified	1,360,194			1,205,462		

Revolving Home Equity Loans

The Company also has revolving home equity loans that are generally collateralized by residential real estate. Most of these loans (93.6%) 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 shown in the tables below, the percentage of loans with LTV ratios greater than 80% has remained a small segment of this portfolio, and delinquencies have been low and stable. Over the next three years, as much as 40% of the Company's revolving home equity loans are expected to mature, which were originated in 2003 through 2007. At maturity, the accounts are re-underwritten and if they qualify under the Company's credit, collateral and capacity policies, the borrower is given the option to renew the line of credit, or to convert the outstanding balance to an amortizing loan. If criteria are not met, amortization is required, or the borrower may pay off the loan.

(Dollars in thousands)	Principal Outstanding at December 31, 2012	*		New Lines Originated During 2012	*		Unused Portion of Available Lines at December 31, 2012	*		Balances Over 30 Days Past Due	*	
Loans with interest only payments	$409,593	93.6	%	$60,673	13.9	%	$637,677	145.7	%	$4,011	.9	%
Loans with LTV:												
Between 80% and 90%	45,698	10.4		9,747	2.2		36,568	8.4		462	.1	
Over 90%	15,310	3.5		1,528	.4		11,320	2.5		358	.1	
Over 80% LTV	61,008	13.9		11,275	2.6		47,888	10.9		820	.2	
	437,567			135,657			649,963					

Total loan portfolio from which
above loans were identified

* Percentage of total principal outstanding of $437.6 million at December 31, 2012.

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(Dollars in thousands)	Principal Outstanding at December 31, 2011	*		New Lines Originated During 2011	*		Unused Portion of Available Lines at December 31, 2011	*		Balances Over 30 Days Past Due	*	
Loans with interest only payments	$438,123	94.5	%	$19,607	4.2	%	$631,719	136.3	%	$1,301	.3	%
Loans with LTV:												
Between 80% and 90%	51,520	11.1		7,802	1.7		39,212	8.4		350	.1	
Over 90%	18,653	4.0		150	—		10,961	2.4		255	—	
Over 80% LTV	70,173	15.1		7,952	1.7		50,173	10.8		605	.1	
Total loan portfolio from which above loans were identified	463,587			121,149			651,108					

* Percentage of total principal outstanding of $463.6 million at December 31, 2011.

Fixed Rate Home Equity Loans

In addition to the residential real estate mortgage loans and the revolving floating rate line product discussed above, the Company offers a third choice to those consumers desiring a fixed rate loan and a fixed maturity date. This fixed rate home equity loan, typically for home repair or remodeling, is an alternative for individuals who want to finance a specific project or purchase and decide to lock in a specific monthly payment over a defined period. Outstanding balances for these loans were $210.1 million and $142.0 million at December 31, 2012 and 2011, respectively. At times, these loans are written with interest only monthly payments and a balloon payoff at maturity; however, less than 5% of the outstanding balance had interest only payments at December 31, 2012 and 2011. The delinquency history on this product has been low, as balances over 30 days past due totaled only $2.0 million, or .9% of the portfolio, and $1.6 million, or 1.2% of the portfolio, at year end 2012 and 2011, respectively.

(Dollars in thousands)	2012 Principal Outstanding at December 31	*		New Loans Originated	*		2011 Principal Outstanding at December 31	*		New Loans Originated	*	
Loans with interest only payments	$4,128	2.0	%	$5,464	2.6	%	$5,965	4.2	%	$8,669	6.1	%
Loans with LTV:												
Between 80% and 90%	36,427	17.3		26,438	12.6		19,346	13.6		8,520	6.0	
Over 90%	17,561	8.4		6,628	3.1		18,599	13.1		4,098	2.9	
Over 80% LTV	53,988	25.7		33,066	15.7		37,945	26.7		12,618	8.9	
Total loan portfolio from which above loans were identified	210,064						141,977					

* Percentage of total principal outstanding of $210.1 million and $142.0 million at December 31, 2012 and 2011, respectively.

Management does not believe these loans collateralized by real estate (revolving home equity, personal real estate, and fixed rate home equity) represent any unusual concentrations of risk, as evidenced by net charge-offs in 2012 of $1.8 million, $1.4 million and $466 thousand, respectively. The amount of any increased potential loss on high LTV agreements relates mainly to amounts advanced that are in excess of the 80% collateral calculation, not the entire approved line. The Company currently offers no subprime first mortgage or home equity loans. These are characterized as new loans to customers with FICO scores below 650 for home equity loans, 660 for

government-insured first mortgages, and 680 for all other conventional first mortgages. The Company does not purchase brokered loans.

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Other Consumer Loans

Within the consumer loan portfolio are several direct and indirect product lines comprised mainly of loans secured by automobiles and other passenger vehicles, marine, and RVs. During 2012, $440.2 million of new automobile loans were originated, compared to $222.3 million during 2011. However, marine and RV loan production has been curtailed since 2008. The loss ratios experienced for marine and RV loans have been higher than for other consumer loan products in recent years, at 1.8% and 2.1% in 2012 and 2011, respectively, but year end balances over 30 days past due have decreased $3.0 million from 2011. The table below provides the total outstanding principal and other data for this group of direct and indirect lending products at December 31, 2012 and 2011.

	2012			2011		
(In thousands)	Principal Outstanding at December 31	New Loans Originated	Balances Over 30 Days Past Due	Principal Outstanding at December 31	New Loans Originated	Balances Over 30 Days Past Due
Passenger vehicles	$569,616	$440,206	$4,454	$357,575	$222,268	$2,606
Marine	88,858	1,450	2,948	113,770	1,488	3,703
RV	238,991	—	4,443	306,383	—	6,702
Total	$897,465	$441,656	$11,845	$777,728	$223,756	$13,011

Additionally, the Company offers low introductory rates on selected consumer credit card products. Out of a portfolio at December 31, 2012 of $804.2 million in consumer credit card loans outstanding, approximately $129.5 million, or 16.1%, carried a low introductory rate. Within the next six months, $29.0 million of these loans are scheduled to convert to the ongoing higher contractual rate. To mitigate some of the risk involved with this credit card product, the Company performs credit checks and detailed analysis of the customer borrowing profile before approving the loan application. Management believes that the risks in the consumer loan portfolio are reasonable and the anticipated loss ratios are within acceptable parameters.

Investment Securities Analysis

Investment securities are comprised of securities which are classified as available for sale, non-marketable, or trading. During 2012, total investment securities increased $260.2 million, or 2.8%, to $9.4 billion (excluding unrealized gains/losses) compared to $9.1 billion at the previous year end. During 2012, securities of $3.4 billion were purchased, which included $1.8 billion in asset-backed securities. Total sales, maturities and pay downs were $3.1 billion during 2012. During 2013, maturities and pay downs of approximately $2.2 billion are expected to occur. The average tax equivalent yield earned on total investment securities was 2.55% in 2012 and 2.93% in 2011.

At December 31, 2012, the fair value of available for sale securities was $9.5 billion, including a net unrealized gain in fair value of $263.7 million, compared to a net unrealized gain of $212.6 million at December 31, 2011. The overall unrealized gain in fair value at December 31, 2012 included gains of $132.9 million in agency mortgage-backed securities, $38.8 million in U.S. government and federal agency obligations, $29.8 million in state and municipal obligations, and $27.4 million in equity securities held by the Parent.

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Available for sale investment securities at year end for the past two years are shown below:

	December 31	
(In thousands)	2012	2011
Amortized Cost		
U.S. government and federal agency obligations	$399,971	$328,530
Government-sponsored enterprise obligations	467,063	311,529
State and municipal obligations	1,585,926	1,220,840
Agency mortgage-backed securities	3,248,007	3,989,464
Non-agency mortgage-backed securities	224,223	315,752
Asset-backed securities	3,152,913	2,692,436
Other debt securities	174,727	135,190
Equity securities	5,695	18,354
Total available for sale investment securities	$9,258,525	$9,012,095
Fair Value		
U.S. government and federal agency obligations	$438,759	$364,665
Government-sponsored enterprise obligations	471,574	315,698
State and municipal obligations	1,615,707	1,245,284
Agency mortgage-backed securities	3,380,955	4,106,059
Non-agency mortgage-backed securities	237,011	316,902
Asset-backed securities	3,167,394	2,693,143
Other debt securities	177,752	141,260
Equity securities	33,096	41,691
Total available for sale investment securities	$9,522,248	$9,224,702

The largest component of the available for sale portfolio consists of agency mortgage-backed securities, which are collateralized bonds issued by agencies, including FNMA, GNMA, FHLMC, FHLB, Federal Farm Credit Banks and FDIC. Non-agency mortgage-backed securities totaled $237.0 million, at fair value, at December 31, 2012, and included Alt-A type mortgage-backed securities of $108.8 million and prime/jumbo loan type securities of $128.2 million. Certain of the non-agency mortgage-backed securities are other-than-temporarily impaired, and the processes for determining impairment and the related losses are discussed in Note 3 to the consolidated financial statements. The portfolio does not have exposure to subprime originated mortgage-backed or collateralized debt obligation instruments.

At December 31, 2012, U.S. government obligations included $438.6 million in U.S. Treasury inflation-protected securities, and state and municipal obligations included $126.4 million in auction rate securities, at fair value. Other debt securities include corporate bonds, notes and commercial paper. Available for sale equity securities are mainly comprised of common stock held by the Parent which totaled $30.7 million at December 31, 2012.

The types of debt securities in the available for sale security portfolio are presented in the table below. Additional detail by maturity category is provided in Note 3 to the consolidated financial statements.

	December 31, 2012					
	Percent of Total Debt Securities		Weighted Average Yield		Estimated Average Maturity*	
Available for sale debt securities:						
U.S. government and federal agency obligations	4.6	%	1.23	%	5.9	years
Government-sponsored enterprise obligations	5.0		1.75		9.0	
State and municipal obligations	17.0		2.47		7.0	

Agency mortgage-backed securities	35.6	2.82	3.1
Non-agency mortgage-backed securities	2.5	6.08	4.1
Asset-backed securities	33.4	.94	2.1
Other debt securities	1.9	3.47	5.2

*Based on call provisions and estimated prepayment speeds.

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Non-marketable securities, which totaled $118.7 million at December 31, 2012, included $30.7 million in Federal Reserve Bank stock and $14.6 million in Federal Home Loan Bank (Des Moines) stock held by the bank subsidiary in accordance with debt and regulatory requirements. These are restricted securities which, lacking a market, are carried at cost. Other non-marketable securities also include private equity securities which are carried at estimated fair value.

The Company engages in private equity activities primarily through several private equity subsidiaries. These subsidiaries hold investments in various business entities, which are carried at fair value and totaled $68.2 million at December 31, 2012. In addition to investments held by its private equity subsidiaries, the Parent directly holds investments in several private equity concerns, which totaled $4.3 million at year end 2012. Most of the private equity investments are not readily marketable. While the nature of these investments carries a higher degree of risk than the normal lending portfolio, this risk is mitigated by the overall size of the investments and oversight provided by management, and management believes the potential for long-term gains in these investments outweighs the potential risks.

Non-marketable securities at year end for the past two years are shown below:

	December 31	
(In thousands)	2012	2011
Debt securities	$32,068	$31,683
Equity securities	86,582	84,149
Total non-marketable investment securities	$118,650	$115,832

In addition to its holdings in the investment securities portfolio, the Company holds long-term securities purchased under agreements to resell, which totaled $1.2 billion and $850.0 million at December 31, 2012 and 2011, respectively. These investments mature in 2013 through 2016, and most have rates that fluctuate with published indices within a fixed range. The counterparties to these agreements are other financial institutions from whom the Company has accepted collateral of $1.3 billion in marketable investment securities at December 31, 2012. The average rate earned on these agreements during 2012 was 2.15%.

The Company also holds $300.0 million in offsetting repurchase and resell agreements at December 31, 2012, which are further discussed in Note 3 to the consolidated financial statements. These agreements involve the exchange of collateral under simultaneous repurchase and resell agreements with the same financial institution counterparty. These repurchase and resell agreements have been offset against each other in the balance sheet, as permitted under current accounting guidance.

Deposits and Borrowings

Deposits are the primary funding source for the Bank and are acquired from a broad base of local markets, including both individual and corporate customers. Total deposits were $18.3 billion at December 31, 2012, compared to $16.8 billion last year, reflecting an increase of $1.5 billion, or 9.2%. This increase follows 11.4% growth in 2011 over 2010, and reflects a continuing sense of uncertainty about future economic stability by borrowers and investors.

Average deposits grew by $1.2 billion, or 7.4%, in 2012 compared to 2011 with most of this growth occurring in business demand deposits, which grew $714.7 million, or 21.3%, and in interest checking and money market deposits, which increased $727.7 million, or 9.4%. Certificates of deposit with balances under $100,000 fell on average by $173.9 million, or 13.5%, and certificates of deposit over $100,000 decreased by $228.3 million, or 16.2%.

The following table shows year end deposits by type as a percentage of total deposits.

	December 31			
	2012		2011	
Non-interest bearing	34.3	%	32.0	%

Savings, interest checking and money market	53.5	53.2
Time open and C.D.'s of less than $100,000	5.9	6.9
Time open and C.D.'s of $100,000 and over	6.3	7.9
Total deposits	100.0 %	100.0 %

Core deposits, which include non-interest bearing, interest checking, savings, and money market deposits, supported 74% of average earning assets in 2012 and 71% in 2011. Average balances by major deposit category for the last six years appear on page 50. A maturity schedule of time deposits outstanding at December 31, 2012 is included in Note 6 on Deposits in the consolidated financial statements.

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The Company’s primary sources of overnight borrowings are federal funds purchased and securities sold under agreements to repurchase (repurchase agreements). Balances in these accounts can fluctuate significantly on a day-to-day basis and generally have one day maturities. These short-term balances totaled $683.6 million at December 31, 2012. The Company also holds $400.0 million in long-term structured repurchase agreements that will mature throughout 2013 and 2014. Total balances of federal funds purchased and repurchase agreements outstanding at year end 2012 were $1.1 billion, a $172.5 million decrease from the $1.3 billion balance outstanding at year end 2011. On an average basis, these borrowings increased $151.0 million, or 14.6%, during 2012, with increases of $77.1 million in federal funds purchased and $73.9 million in repurchase agreements. The average rate paid on total federal funds purchased and repurchase agreements was .07% during 2012 and .17% during 2011.

Most of the Company’s long-term debt is comprised of fixed rate advances from the FHLB. These borrowings declined from $104.3 million at December 31, 2011, to $103.7 million outstanding at December 31, 2012. The average rate paid on FHLB advances was 3.60% during both 2012 and 2011. Most of the remaining balance outstanding at December 31, 2012 is due in 2017.

Liquidity and Capital Resources

Liquidity Management

Liquidity is managed within the Company in order to satisfy cash flow requirements of deposit and borrowing customers while at the same time meeting its own cash flow needs. The Company maintains its liquidity position through a variety of sources including:

- A portfolio of liquid assets including marketable investment securities and overnight investments,
- A large customer deposit base and limited exposure to large, volatile certificates of deposit,
- Lower long-term borrowings that might place demands on Company cash flow,
- Relatively low loan to deposit ratio promoting strong liquidity,
- Excellent debt ratings from both Standard & Poor’s and Moody’s national rating services, and
- Available borrowing capacity from outside sources.

Since 2008, when some of the major banking institutions experienced severe capital erosion, liquidity risk has been a concern affecting the general banking industry. The Company has taken numerous steps to address liquidity risk and over the past few years has developed a variety of liquidity sources which it believes will provide the necessary funds for future growth. Over the past several years, overall liquidity improved significantly throughout the banking industry and within the Company as a result of growth in deposits, a decline in loans outstanding and growth in marketable securities. As a result, the Company’s average loans to deposits ratio, one measure of liquidity, decreased from 59.2% in 2011 to 55.8% in 2012.

The Company’s most liquid assets include available for sale marketable investment securities, federal funds sold, balances at the Federal Reserve Bank, and securities purchased under agreements to resell (resell agreements). At December 31, 2012 and 2011, such assets were as follows:

(In thousands)	2012	2011
Available for sale investment securities	$9,522,248	$9,224,702
Federal funds sold	27,595	11,870
Long-term securities purchased under agreements to resell	1,200,000	850,000
Balances at the Federal Reserve Bank	179,164	39,853
Total	$10,929,007	$10,126,425

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Federal funds sold, which are sold to the Company's correspondent bank customers and have overnight maturities, totaled $27.6 million at December 31, 2012. At December 31, 2012, the Company held $1.2 billion in long-term resell agreements, maturing in 2013 through 2016, from other large financial institutions. Under these agreements, the Company holds marketable securities as collateral, which totaled $1.3 billion in fair value at December 31, 2012. Interest earning balances at the Federal Reserve Bank, which have overnight maturities and are used for general liquidity purposes, totaled $179.2 million at December 31, 2012. The Company's available for sale investment portfolio includes scheduled maturities and expected pay downs of approximately $2.2 billion during 2013, and offers substantial resources to meet either new loan demand or reductions in the Company's deposit funding base. The Company pledges portions of its investment securities portfolio to secure public fund deposits, repurchase agreements, trust funds, letters of credit issued by the FHLB, and borrowing capacity at the Federal Reserve Bank. At December 31, 2012 and 2011, total investment securities pledged for these purposes were as follows:

(In thousands)	2012	2011
Investment securities pledged for the purpose of securing:		
Federal Reserve Bank borrowings	$604,121	$642,306
FHLB borrowings and letters of credit	46,732	111,860
Repurchase agreements	2,105,867	2,048,074
Other deposits	1,550,114	1,564,105
Total pledged securities	4,306,834	4,366,345
Unpledged and available for pledging	3,428,781	3,260,695
Ineligible for pledging	1,786,633	1,597,662
Total available for sale securities, at fair value	$9,522,248	$9,224,702

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 December 31, 2012, such deposits totaled $16.1 billion and represented 87.8% of the Company's total deposits. These core deposits are normally less volatile, often with customer relationships tied to other products offered by the Company promoting long lasting relationships and stable funding sources. During 2012, total core deposits increased $1.8 billion, with consumer core deposits growing $1.1 billion and corporate core deposits up $657.5 million. Much of this growth occurred in the fourth quarter of 2012, and reflected not only seasonal patterns but also an increased need for liquidity. Also, extremely low interest rates provide customers with fewer investment alternatives. Additionally in 2011, total core deposits increased $2.0 billion, reflecting similar trends as in the current year. While the Company considers core consumer deposits less volatile, corporate deposits could decline if interest rates increase significantly or if corporate customers increase investing activities and reduce deposit balances. In order to address funding needs if these corporate deposits decline, the Company maintains adequate levels of earning assets totaling $2.2 billion which mature in 2013 as noted above. In addition, as shown on page 40, the Company has borrowing capacity of $3.2 billion through advances from the FHLB and the Federal Reserve.

(In thousands)	2012	2011
Core deposit base:		
Non-interest bearing	$6,299,903	$5,377,549
Interest checking	976,144	968,430
Savings and money market	8,841,799	7,965,511
Total	$16,117,846	$14,311,490

Time open and certificates of deposit of $100,000 or greater totaled $1.2 billion at December 31, 2012. These deposits are normally considered more volatile and higher costing and comprised 6.3% of total deposits at December 31, 2012.

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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, repurchase agreements, and advances from the FHLB, as follows:

(In thousands)	2012	2011
Borrowings:		
Federal funds purchased	$24,510	$153,330
Repurchase agreements	1,059,040	1,102,751
FHLB advances	103,710	104,302
Other long-term debt	—	7,515
Total	$1,187,260	$1,367,898

Federal funds purchased, which totaled $24.5 million at December 31, 2012, are unsecured overnight borrowings obtained mainly from upstream correspondent banks with which the Company maintains approved lines of credit. Repurchase agreements are secured by a portion of the Company's investment portfolio and are comprised of both non-insured customer funds, totaling $659.0 million at December 31, 2012, and structured repurchase agreements of $400.0 million. Customer repurchase agreements are offered to customers wishing to earn interest in highly liquid balances and are used by the Company as a funding source considered to be stable, but short-term in nature. The structured repurchase agreements were borrowed from an upstream financial institution and are due in 2013 and 2014. The Company also borrows on a secured basis through advances from the FHLB, which totaled $103.7 million at December 31, 2012. All of these advances have fixed interest rates, with the majority maturing in 2017. The overall long-term debt position of the Company is small relative to the Company's overall liability position.

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 and permits 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 December 31, 2012.

	December 31, 2012		
(In thousands)	FHLB	Federal Reserve	Total
Total collateral value pledged	$2,039,676	$1,474,583	$3,514,259
Advances outstanding	(103,710)	—	(103,710)
Letters of credit issued	(260,050)	—	(260,050)
Available for future advances	$1,675,916	$1,474,583	$3,150,499

The Company's average loans to deposits ratio was 55.8% at December 31, 2012, which is considered in the banking industry to be a measure of strong liquidity. Also, the Company receives outside ratings from both Standard & Poor's and Moody's on both the consolidated company and its subsidiary bank, Commerce Bank. These ratings are as follows:

	Standard & Poor's	Moody's
Commerce Bancshares, Inc.		
Issuer rating	A-	
Commercial paper rating		P-1
Rating outlook	Stable	Stable

Commerce Bank		
Issuer rating	A	Aa3
Bank financial strength rating		B
Rating outlook	Stable	Stable

The Company considers these ratings to be indications of a sound capital base and strong liquidity and believes that these ratings would help ensure the ready marketability of its commercial paper, should the need arise. No commercial paper has been outstanding during the past ten years. The Company has no subordinated or hybrid debt instruments which would affect future

borrowing capacity. Because of its lack of significant long-term debt, the Company believes that, through its Capital Markets Group or in other public debt markets, it could generate additional liquidity from sources such as jumbo certificates of deposit, privately-placed corporate notes or other forms of debt. Future financing could also include the issuance of common or preferred stock.

The cash flows from the operating, investing and financing activities of the Company resulted in a net increase in cash and cash equivalents of $262.3 million in 2012, as reported in the consolidated statements of cash flows on page 59 of this report. Operating activities, consisting mainly of net income adjusted for certain non-cash items, provided cash flow of $383.1 million and has historically been a stable source of funds. Investing activities used total cash of $1.2 billion in 2012 and consisted mainly of purchases and maturities of available for sale investment securities, changes in long-term securities purchased under agreements to resell, and changes in the level of the Company's loan portfolio. Growth in the loan portfolio used cash of $693.2 million. Net purchases of long-term resell agreements used cash of $350.0 million, and growth in the investment securities portfolio used cash of $85.3 million. Investing activities are somewhat unique to financial institutions in that, while large sums of cash flow are normally used to fund growth in investment securities, loans, or other bank assets, they are normally dependent on the financing activities described below.

Financing activities provided total cash of $1.0 billion, primarily resulting from a $1.5 billion increase in deposits. This increase to cash was partly offset by net decrease of $172.5 million in borrowings of federal funds purchased and repurchase agreements, purchases of treasury stock of $104.9 million, and cash dividend payments of $211.6 million. Future short-term liquidity needs for daily operations are not expected to vary significantly, and the Company maintains adequate liquidity to meet these cash flows. The Company's sound equity base, along with its low debt level, common and preferred stock availability, and excellent debt ratings, provide several alternatives for future financing. Future acquisitions may utilize partial funding through one or more of these options.

Cash flows resulting from the Company's transactions in its common stock were as follows:

(In millions)	2012	2011	2010
Exercise of stock-based awards and sales to affiliate non-employee directors	$15.6	$15.3	$11.3
Purchases of treasury stock	(104.9)	(101.2)	(41.0)
Cash dividends paid	(211.6)	(79.1)	(78.2)
Cash used	$(300.9)	$(165.0)	$(107.9)

The Parent faces unique liquidity constraints due to legal limitations on its ability to borrow funds from its bank subsidiary. The Parent obtains funding to meet its obligations from two main sources: dividends received from bank and non-bank subsidiaries (within regulatory limitations) and management fees charged to subsidiaries as reimbursement for services provided by the Parent, as presented below:

(In millions)	2012	2011	2010
Dividends received from subsidiaries	$235.0	$180.1	$105.1
Management fees	23.7	19.3	22.6
Total	$258.7	$199.4	$127.7

These sources of funds are used mainly to pay cash dividends on outstanding common stock, pay general operating expenses, and purchase treasury stock. At December 31, 2012, the Parent's available for sale investment securities totaled $65.2 million at fair value, consisting of common stock and non-agency backed collateralized mortgage obligations. To support its various funding commitments, the Parent maintains a $20.0 million line of credit with its subsidiary bank. There were no borrowings outstanding under the line during 2012 or 2011.

Company senior management is responsible for measuring and monitoring the liquidity profile of the organization with oversight by the Company's Asset/Liability Committee. This is done through a series of controls, including a written Contingency Funding Policy and risk monitoring procedures, which include daily, weekly and monthly reporting. In addition, the Company prepares forecasts to project changes in the balance sheet affecting liquidity and to allow the Company to better plan for forecasted changes.

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Capital Management

The Company maintains strong regulatory capital ratios, including those of its banking subsidiary, in excess of the "well-capitalized" guidelines under federal banking regulations. The Company's capital ratios at the end of the last three years are as follows:

	2012	2011	2010	Well-Capitalized Regulatory Guidelines
Regulatory risk-based capital ratios:				
Tier I capital	13.60 %	14.71 %	14.38 %	6.00 %
Total capital	14.93	16.04	15.75	10.00
Leverage ratio	9.14	9.55	10.17	5.00
Tangible common equity to assets	9.25	9.91	10.27	
Dividend payout ratio	79.48	31.06	35.52	

The Company's regulatory risked-based capital amounts and risk-weighted assets at the end of the last three years are as follows:

(In thousands)	2012	2011	2010
Regulatory risk-based capital:			
Tier I capital	$1,906,203	$1,928,690	$1,828,965
Tier II capital	185,938	174,711	173,681
Total capital	2,092,141	2,103,401	2,002,646
Total risk-weighted assets	14,015,648	13,115,261	12,717,868

The Company maintains a stock buyback program and purchases stock in the market under authorizations by its Board of Directors. During 2012 the Company purchased 2,716,368 shares of stock at an average cost of $38.62 per share. At December 31, 2012, 2,127,618 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 levels and alternative investment options. The regular per share cash dividends paid by the Company increased 5.0% in 2012 compared with 2011. In addition, the Company paid a special cash dividend of $1.429 per share in the fourth quarter of 2012. The Company also paid its nineteenth consecutive annual stock dividend in December 2012.

Commitments, Contractual Obligations, and Off-Balance Sheet Arrangements

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 totaling $8.4 billion (including approximately $3.9 billion in unused approved credit card lines) and the contractual amount of standby letters of credit totaling $359.8 million at December 31, 2012. As many commitments expire unused or only partially used, these totals do not necessarily reflect future cash requirements. Management does not anticipate any material losses arising from commitments or contingent liabilities and believes there are no material commitments to extend credit that represent risks of an unusual nature.

A table summarizing contractual cash obligations of the Company at December 31, 2012 and the expected timing of these payments follows:

	Payments Due by Period				
(In thousands)	In One Year or Less	After One Year Through Three Years	After Three Years Through Five Years	After Five Years	Total
	$51,510	$351,249	$100,951	$—	$503,710

Long-term debt obligations, including structured repurchase agreements*					
Operating lease obligations	5,354	8,178	4,810	16,532	34,874
Purchase obligations	69,583	104,131	48,352	4,030	226,096
Time open and C.D.'s *	1,768,087	330,666	132,025	29	2,230,807
Total	$1,894,534	$794,224	$286,138	$20,591	$2,995,487

* Includes principal payments only.

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As of December 31, 2012, the Company has unrecognized tax benefits that, if recognized, would impact the effective tax rate in future periods. Due to the uncertainty of the amounts to be ultimately paid, as well as the timing of such payments, all uncertain tax liabilities that have not been paid have been excluded from the table above. Further detail on the impact of income taxes is located in Note 8 to the consolidated financial statements.

The Company funds a defined benefit pension plan for a portion of its employees. Under the funding policy for the plan, contributions are made as necessary to provide for current service and for any unfunded accrued actuarial liabilities over a reasonable period. During 2012, the Company made a discretionary contribution of $1.5 million to its defined benefit pension plan in order to reduce pension guarantee premiums. However, the Company is not required nor does it expect to make a contribution in 2013.

The Company has investments in several low-income housing partnerships within the areas it serves. These partnerships supply funds for the construction and operation of apartment complexes that provide affordable housing to that segment of the population with lower family income. If these developments successfully attract a specified percentage of residents falling in that lower income range, state and/or federal income tax credits are made available to the partners. The tax credits are normally recognized over ten years, and they play an important part in the anticipated yield from these investments. In order to continue receiving the tax credits each year over the life of the partnership, the low-income residency targets must be maintained. Under the terms of the partnership agreements, the Company has a commitment to fund a specified amount that will be due in installments over the life of the agreements, which ranges from 10 to 15 years. At December 31, 2012, the funded investments totaled $7.8 million and are recorded as other assets in the Company's consolidated balance sheet. Additional unfunded commitments, which are recorded as liabilities, amounted to $6.9 million at December 31, 2012.

The Company regularly purchases various state tax credits arising from third-party property redevelopment. These credits are either resold to third parties or retained for use by the Company. During 2012, purchases and sales of tax credits amounted to $56.9 million and $31.0 million, respectively. At December 31, 2012, the Company had outstanding purchase commitments totaling $149.8 million.

Interest Rate Sensitivity

The Company's Asset/Liability Management Committee (ALCO) measures and manages the Company's interest rate risk on a monthly basis to identify trends and establish strategies to maintain stability in net interest income throughout various rate environments. Analytical modeling techniques provide management insight into the Company's exposure to changing rates. These techniques include net interest income simulations and market value analysis. Management has set guidelines specifying acceptable limits within which net interest income and market value may change under various rate change scenarios. These measurement tools indicate that the Company is currently within acceptable risk guidelines as set by management.

The Company's main interest rate measurement tool, income simulations, projects net interest income under various rate change scenarios in order to quantify the magnitude and timing of potential rate-related changes. Income simulations are able to capture option risks within the balance sheet where expected cash flows may be altered under various rate environments. Modeled rate movements include "shocks, ramps and twists". Shocks are intended to capture interest rate risk under extreme conditions by immediately shifting rates up and down, while ramps measure the impact of gradual changes and twists measure yield curve risk. The size of the balance sheet is assumed to remain constant so that results are not influenced by growth predictions. The table below shows the expected effect that gradual basis point shifts in the swap curve over a twelve month period would have on the Company's net interest income, given a static balance sheet.

	December 31, 2012	September 30, 2012	December 31, 2011

(Dollars in millions)	$ Change in Net Interest Income	% Change in Net Interest Income	$ Change in Net Interest Income	% Change in Net Interest Income	$ Change in Net Interest Income	% Change in Net Interest Income
300 basis points rising	($2.1)	(.36)%	$8.8	1.50%	($2.0)	(.32)%
200 basis points rising	3.1	.51	10.3	1.77	2.2	.34
100 basis points rising	4.9	.82	8.3	1.41	3.5	.56

The Company also employs a sophisticated simulation technique known as a stochastic income simulation. This technique allows management to see a range of results from hundreds of income simulations. The stochastic simulation creates a vector of potential rate paths around the market's best guess (forward rates) concerning the future path of interest rates and allows rates to randomly follow paths throughout the vector. This allows for the modeling of non-biased rate forecasts around the market consensus. Results give management insight into a likely range of rate-related risk as well as worst and best-case rate scenarios.

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The Company also uses market value analysis to help identify longer-term risks that may reside on the balance sheet. This is considered a secondary risk measurement tool by management. The Company measures the market value of equity as the net present value of all asset and liability cash flows discounted along the current swap curve plus appropriate market risk spreads. It is the change in the market value of equity under different rate environments, or effective duration that gives insight into the magnitude of risk to future earnings due to rate changes. Market value analysis also help management understand the price sensitivity of non-marketable bank products under different rate environments.

Under the above scenarios at December 31, 2012, a gradual increase in interest rates of 100 basis points is expected to increase net interest income from the base calculation by $4.9 million, or .82%, and a rise of 200 basis points is expected to increase net interest income by $3.1 million, or .51%. Under a 300 basis points rising rate scenario, net interest income would decrease by $2.1 million, or .36%. Due to the already low interest rate environment, the Company did not model falling rate scenarios. The change in net interest income from the base calculation at December 31, 2012 for the three scenarios shown was lower than projections made at September 30, 2012 and largely due to an increase in longer duration assets in the Company's portfolios of investment securities and resell agreements, which was funded primarily by shorter duration liabilities. These longer duration assets were purchased to protect against the possible continuation of extremely low rates. As a result, while net interest income benefits less when rates rise, a rising rate environment suggests growth in economic activity and greater demand for higher rate lending products. Additionally, but to a lesser extent, higher long-term rates at December 31, 2012 slowed prepayment projections on mortgage-backed securities, such that further rate increases result in less benefit.

Through review and oversight by the ALCO, the Company attempts to engage in strategies that neutralize interest rate risk as much as possible. The Company’s balance sheet remains well-diversified with moderate interest rate risk and is well-positioned for future growth. The use of derivative products is limited and the deposit base is strong and stable. The loan to deposit ratio is still at relatively low levels, which should present the Company with opportunities to fund future loan growth at reasonable costs. The Company believes that its approach to interest rate risk has appropriately considered its susceptibility to both rising and falling rates and has adopted strategies which minimize impacts of interest rate risk.

Derivative Financial Instruments

The Company maintains an overall interest rate risk management strategy that permits the use of derivative instruments to modify exposure to interest rate risk. The Company’s interest rate risk management strategy includes the ability to modify the re-pricing characteristics of certain assets and liabilities so that changes in interest rates do not adversely affect the net interest margin and cash flows. Interest rate swaps are used on a limited basis as part of this strategy. As of December 31, 2012, the Company had entered into three interest rate swaps with a notional amount of $13.2 million which are designated as fair value hedges of certain fixed rate loans. The Company also sells swap contracts to customers who wish to modify their interest rate sensitivity. The Company offsets the interest rate risk of these swaps by purchasing matching contracts with offsetting pay/receive rates from other financial institutions. The notional amount of these types of swaps at December 31, 2012 was $422.4 million.

Credit risk participation agreements arise when the Company contracts, as a guarantor or beneficiary, with other financial institutions to share credit risk associated with certain interest rate swaps. These agreements provide for reimbursement of losses resulting from a third party default on the underlying swap.

The Company enters into foreign exchange derivative instruments as an accommodation to customers and offsets the related foreign exchange risk by entering into offsetting third-party forward contracts with approved, reputable counterparties. In addition, the Company takes proprietary positions in such contracts based on market expectations. This trading activity is managed within a policy of specific controls and limits. Most of the foreign exchange contracts

outstanding at December 31, 2012 mature within six months.

Additionally, interest rate lock commitments issued on residential mortgage loans held for resale are considered derivative instruments. The interest rate exposure on these commitments is economically hedged primarily with forward sale contracts in the secondary market. In late 2011, the Company curtailed the sales of these types of loans. At December 31, 2012, none were held for sale, and thus, no commitments or forward sale contracts were outstanding.

In all of these contracts, the Company is exposed to credit risk in the event of nonperformance by counterparties, who may be bank customers or other financial institutions. The Company controls the credit risk of its financial contracts through credit approvals, limits and monitoring procedures. Because the Company generally enters into transactions only with high quality counterparties, there have been no losses associated with counterparty nonperformance on derivative financial instruments.

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The following table summarizes the notional amounts and estimated fair values of the Company's derivative instruments at December 31, 2012 and 2011. Notional amount, along with the other terms of the derivative, is used to determine the amounts to be exchanged between the counterparties. Because the notional amount does not represent amounts exchanged by the parties, it is not a measure of loss exposure related to the use of derivatives nor of exposure to liquidity risk.

(In thousands)	2012 Notional Amount	Positive Fair Value	Negative Fair Value	2011 Notional Amount	Positive Fair Value	Negative Fair Value
Interest rate swaps	$435,542	$16,334	$(17,060)	$486,207	$19,051	$(20,210)
Interest rate caps	27,736	1	(1)	29,736	11	(11)
Credit risk participation agreements	43,243	9	(196)	41,414	9	(141)
Foreign exchange contracts	47,897	396	(461)	80,535	2,440	(2,343)
Mortgage loan commitments	—	—	—	1,280	20	—
Mortgage loan forward sale contracts	—	—	—	3,650	6	(17)
Total at December 31	$554,418	$16,740	$(17,718)	$642,822	$21,537	$(22,722)

Operating Segments

The Company segregates financial information for use in assessing its performance and allocating resources among three operating segments. The results are determined based on the Company's management accounting process, which assigns balance sheet and income statement items to each responsible segment. These segments are defined by customer base and product type. The management process measures the performance of the operating segments based on the management structure of the Company and is not necessarily comparable with similar information for any other financial institution. Each segment is managed by executives who, in conjunction with the Chief Executive Officer, make strategic business decisions regarding that segment. The three reportable operating segments are Consumer, Commercial and Wealth. Additional information is presented in Note 12 on Segments in the consolidated financial statements.

The Company uses a funds transfer pricing method to value funds used (e.g., loans, fixed assets, cash, etc.) and funds provided (deposits, borrowings, and equity) by the business segments and their components. This process assigns a specific value to each new source or use of funds with a maturity, based on current swap rates, thus determining an interest spread at the time of the transaction. Non-maturity assets and liabilities are valued using weighted average pools. The funds transfer pricing process attempts to remove interest rate risk from valuation, allowing management to compare profitability under various rate environments. The Company also assigns loan charge-offs and recoveries (labeled in the table below as "provision for loan losses") directly to each operating segment instead of allocating an estimated loan loss provision. The operating segments also include a number of allocations of income and expense from various support and overhead centers within the Company.

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The table below is a summary of segment pre-tax income results for the past three years.

(Dollars in thousands)	Consumer	Commercial	Wealth	Segment Totals	Other/Elimination	Consolidated Totals
Year ended December 31, 2012:						
Net interest income	$274,844	$291,393	$39,502	$605,739	$ 34,167	$639,906
Provision for loan losses	(35,496)	(2,824)	(695)	(39,015)	11,728	(27,287)
Non-interest income	114,307	179,824	108,471	402,602	(2,972)	399,630
Investment securities gains, net	—	—	—	—	4,828	4,828
Non-interest expense	(266,892)	(226,795)	(90,643)	(584,330)	(34,139)	(618,469)
Income before income taxes	$86,763	$241,598	$56,635	$384,996	$ 13,612	$398,608
Year ended December 31, 2011:						
Net interest income	$283,555	$283,790	$38,862	$606,207	$ 39,863	$646,070
Provision for loan losses	(47,273)	(16,195)	(712)	(64,180)	12,665	(51,515)
Non-interest income	131,253	162,533	101,836	395,622	(2,705)	392,917
Investment securities gains, net	—	—	—	—	10,812	10,812
Non-interest expense	(269,435)	(221,273)	(89,108)	(579,816)	(37,433)	(617,249)
Income before income taxes	$98,100	$208,855	$50,878	$357,833	$ 23,202	$381,035
2012 vs 2011						
Increase (decrease) in income before income taxes:						
Amount	$(11,337)	$32,743	$5,757	$27,163	$ (9,590)	$17,573
Percent	(11.6)%	15.7%	11.3%	7.6%	(41.3)%	4.6%
Year ended December 31, 2010:						
Net interest income	$308,719	$264,870	$37,988	$611,577	$ 34,355	$645,932
Provision for loan losses	(70,635)	(24,823)	(1,263)	(96,721)	(3,279)	(100,000)
Non-interest income	157,904	154,306	93,745	405,955	(844)	405,111
Investment securities losses, net	—	—	—	—	(1,785)	(1,785)
Non-interest expense	(291,028)	(221,553)	(86,158)	(598,739)	(32,395)	(631,134)
Income (loss) before income taxes	$104,960	$172,800	$44,312	$322,072	$ (3,948)	$318,124
2011 vs 2010						
Increase (decrease) in income before income taxes:						
Amount	$(6,860)	$36,055	$6,566	$35,761	$ 27,150	$62,911
Percent	(6.5)%	20.9%	14.8%	11.1%	N.M.	19.8%

Consumer

The Consumer segment includes consumer deposits, consumer finance, and consumer debit and credit cards. Pre-tax profitability for 2012 was $86.8 million, a decrease of $11.3 million, or 11.6%, from 2011. This decrease was mainly

due to a decline of $8.7 million, or 3.1%, in net interest income, coupled with a decline of $16.9 million, or 12.9%, in non-interest income. These income reductions were partly offset by a decrease of $11.8 million in the provision for loan losses and a $2.5 million decrease in non-interest expense. Net interest income declined due to a $7.9 million decrease in loan interest income and a $9.8 million decrease in net allocated funding credits assigned to the Consumer segment's loan and deposit portfolios, partly offset by a decline of $9.0 million in deposit interest expense. Non-interest income decreased mainly due to declines in bank card fee income (primarily debit card fees) and deposit account fees (mainly overdraft charges). Non-interest expense declined from the same period in the previous year due to lower FDIC insurance expense and corporate management fees, partly offset by higher salaries expense. The provision for loan losses totaled $35.5 million, an $11.8 million decrease from 2011, which was due mainly to lower losses on consumer credit card loans and marine and RV loans. Total average loans in this segment during 2012 decreased 3.0% compared to the prior year due to a decline in held for sale student loans, which the Company no longer originates, and a decline in personal real estate loans. Consumer loans grew, however, due to higher auto loan originations, partly offset by repayments of marine and RV loans. Average deposits increased 4.2% over the prior period, resulting mainly from growth in money market and interest checking deposit accounts, partly offset by a decline in certificates of deposit under $100,000.

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Pre-tax profitability for 2011 was $98.1 million, a decrease of $6.9 million, or 6.5%, from 2010. This decrease was mainly due to a decline of $25.2 million, or 8.2%, in net interest income, coupled with a decline of $26.7 million in non-interest income. These decreases were partly offset by a reduction in the provision for loan losses of $23.4 million and a decline of $21.6 million in non-interest expense. Net interest income declined due to a $34.0 million decrease in loan interest income and a $7.7 million reduction in net allocated funding credits, partly offset by a decline of $16.5 million in deposit interest expense. The decline in loan interest included a $10.6 million decrease in student loan interest, resulting from the Company's sale of most of the student loan portfolios in 2010, and an $8.3 million decrease in interest on marine and RV loans. Non-interest income decreased mainly due to lower gains on the sales of student loans, in addition to declines in overdraft charges and debit card fees. Non-interest expense declined 7.4% from the previous year due mainly to lower FDIC insurance expense, deposit account processing expense and teller services expense, partly offset by higher building rental expense. The provision for loan losses totaled $47.3 million, a $23.4 million decrease from 2010, which was mainly due to lower losses on consumer credit card loans, marine and RV loans, and other consumer loans. Total average loans decreased 23.6% in 2011 compared to the prior year due to the sale of most of the student loan portfolios in 2010 and a decline in consumer loans. Average deposits increased 2.1% over the prior period.

Commercial

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 segment includes the Capital Markets Group, which sells fixed-income securities to individuals, corporations, correspondent banks, public institutions, and municipalities, and also provides investment safekeeping and bond accounting services. Pre-tax income for 2012 increased $32.7 million, or 15.7%, compared to the prior year, mainly due to a lower provision for loan losses and growth in net interest income and non-interest income. Net interest income increased $7.6 million, or 2.7%, due to higher net allocated funding credits of $15.8 million (related to higher average deposit balances), partly offset by a $10.1 million decline in loan interest income. The provision for loan losses in the segment totaled $2.8 million in 2012, a decrease of $13.4 million from 2011. During 2012, net recoveries of $2.7 million were recorded on business loans, compared to net charge-offs of $4.0 million in 2011. This decline in net charge-offs was partly due to recoveries of $3.6 million on two non-performing loans in 2012. In addition, net charge-offs on construction loans decreased $7.2 million. Non-interest income increased by $17.3 million, or 10.6.%, over the previous year due to growth in bank card fees (mainly corporate card), capital market fees and tax credit sales revenue. Non-interest expense increased $5.5 million, or 2.5%, over 2011, mainly due to higher salaries expense and bank card related expenses, partly offset by lower corporate management fees. Average segment loans increased 1.0% compared to 2011 as a result of a growth in business real estate, lease and tax-free loans, partly offset by a decline in construction loans. Average deposits increased 11.5% due to growth in non-interest bearing accounts, money market deposit accounts and interest checking accounts, partly offset by a decline in certificates of deposit over $100,000.

In 2011, pre-tax profitability for the Commercial segment increased $36.1 million, or 20.9%, compared to the prior year. Net interest income increased $18.9 million, or 7.1%, due to higher net allocated funding credits of $29.1 million, partly offset by an $11.4 million decline in loan interest income. The provision for loan losses in this segment totaled $16.2 million in 2011, a decrease of $8.6 million from 2010, due mainly to lower net charge-offs on construction loans of $8.1 million. Non-interest income increased by $8.2 million, or 5.3%, over the previous year due to growth in corporate card fees, partly offset by lower deposit account fees and bond trading income. Non-interest expense decreased slightly from the previous year and included declines in foreclosed real estate and other repossessed property expense and FDIC insurance expense, partly offset by higher bank card related expenses and deposit account cash management expense. Average segment loans decreased .7% compared to 2010 as a result of a decline in construction loans, partly offset by growth in business real estate loans. Average deposits increased 20.7% due to growth in non-interest bearing accounts, certificates of deposit over $100,000 and money market deposit accounts.

Wealth

The Wealth segment provides traditional trust and estate planning, advisory and discretionary investment management services, brokerage services, and includes Private Banking accounts. At December 31, 2012, the Trust group managed investments with a market value of $17.0 billion and administered an additional $13.3 billion in non-managed assets. It also provides investment management services to The Commerce Funds, a series of mutual funds with $1.8 billion in total assets at December 31, 2012. Wealth segment pre-tax profitability for 2012 was $56.6 million compared to $50.9 million in 2011, an increase of $5.8 million, or 11.3%. Net interest income increased $640 thousand, or 1.6%, and was impacted by a $1.8 million decline in deposit interest expense, partly offset by a $1.0 million decrease in net allocated funding credits. Non-interest income increased $6.6 million, or 6.5%, over the prior year due to higher personal and institutional trust fees. Non-interest expense increased $1.5 million, or 1.7%, mainly due to higher salary and benefit costs, partly offset by lower fraud losses and legal and professional fees. Average assets increased $62.9 million, or 9.2%, during 2012 mainly due to higher loan balances originated in this segment. Average deposits also increased $158.5 million, or 10.3%, during 2012 due to growth in money market deposit accounts and interest checking accounts.

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In 2011, pre-tax income for the Wealth segment was $50.9 million compared to $44.3 million in 2010, an increase of $6.6 million, or 14.8%. Net interest income increased $874 thousand, or 2.3%, and was impacted by a $2.2 million increase in assigned net funding credits and a $1.4 million decline in deposit interest expense, offset by a $2.7 million decrease in loan interest income. Non-interest income increased $8.1 million, or 8.6%, over the prior year due to higher trust and brokerage fees. Non-interest expense increased $3.0 million, or 3.4%, mainly due to higher salary expense and fraud losses. Average assets decreased $1.5 million during 2011 mainly due to lower cash balances and overnight investments, partly offset by loan growth. Average deposits increased $203.1 million, or 15.3%, during 2011 due to growth in money market deposit accounts and long-term certificates of deposit.

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 certain administrative functions, the investment securities portfolio, and the effect of certain expense allocations to the segments. Also included in this category is the difference between the Company’s provision for loan losses and net loan charge-offs, which are generally assigned directly to the segments. In 2012, the pre-tax income in this category was $13.6 million, compared to $23.2 million in 2011. This decrease occurred partly due to a $5.7 million decline in net interest income in this category, related to the earnings of the investment portfolio and interest expense on borrowings not allocated to a segment. In addition, unallocated securities gains declined $6.0 million, while unallocated non-interest expense was lower by $3.3 million.

Impact of Recently Issued Accounting Standards

Fair Value Measurements In May 2011, the Financial Accounting Standards Board (FASB) issued ASU 2011-04, “Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs”. The ASU contains guidance on the application of the highest and best use and valuation premise concepts, the measurement of fair values of instruments classified in shareholders’ equity, the measurement of fair values of financial instruments that are managed within a portfolio, and the application of premiums and discounts in a fair value measurement. It also requires additional disclosures about fair value measurements, including information about the unobservable inputs used in fair value measurements within Level 3 of the fair value hierarchy, the sensitivity of recurring fair value measurements within Level 3 to changes in unobservable inputs and the interrelationships between those inputs, and the categorization by level of the fair value hierarchy for items that are not measured at fair value but for which the fair value is required to be disclosed. These amendments were applied prospectively, effective January 1, 2012, and their application did not have a significant effect on the Company’s consolidated financial statements.

Repurchase Agreements In April 2011, the FASB issued ASU 2011-03, “Reconsideration of Effective Control for Repurchase Agreements”. The guidance in the ASU is intended to improve the accounting for repurchase agreements and other similar agreements. Specifically, the ASU modifies the criteria for determining when these transactions would be recorded as a financing arrangement as opposed to a purchase or sale arrangement with a commitment to resell or repurchase. It removes from the assessment of effective control the criterion relating to the transferor’s ability to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee. This new guidance was effective January 1, 2012, and adoption of this guidance did not have a significant effect on the Company’s consolidated financial statements.

Other Comprehensive Income In June 2011, the FASB issued ASU 2011-05, “Presentation of Comprehensive Income”. The ASU increases the prominence of other comprehensive income in financial statements by requiring comprehensive income to be reported in either a single statement or in two consecutive statements which report both net income and other comprehensive income. It eliminates the option to report other comprehensive income and its components in the statement of changes in equity. The ASU was effective for periods beginning January 1, 2012 and required retrospective application. The ASU did not change the components of other comprehensive income, the timing of items reclassified to net income, or the net income basis for income per share calculations. The Company has chosen to present net income and other comprehensive income in two consecutive statements in the accompanying

consolidated financial statements,

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

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Goodwill In September 2011, the FASB issued ASU 2011-08, "Testing Goodwill for Impairment". The ASU allows an entity to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. Previous guidance required, on an annual basis, testing goodwill for impairment by comparing the fair value of a reporting unit to its carrying amount (including goodwill). As a result of this amendment, an entity will not be required to calculate the fair value of a reporting unit unless the entity determines that it is more likely than not that its fair value is less than its carrying amount. The ASU was effective for annual and interim goodwill impairment tests performed for periods beginning January 1, 2012. The adoption of this guidance did not have a significant effect on the Company’s consolidated financial statements.

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

Corporate Governance

The Company has adopted a number of corporate governance measures. These include corporate governance guidelines, a code of ethics that applies to its senior financial officers and the charters for its audit committee, its committee on compensation and human resources, and its committee on governance/directors. This information is available on the Company’s Web site www.commercebank.com under Investor Relations.

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AVERAGE BALANCE SHEETS — AVERAGE RATES AND YIELDS

	Years Ended December 31								
	2012			2011			2010		
(Dollars in thousands)	Average Balance	Interest Income/Expense	Average Rates Earned/Paid	Average Balance	Interest Income/Expense	Average Rates Earned/Paid	Average Balance	Interest Income/Expense	Average Rates Earned/Paid
ASSETS									
Loans:[(A)]									
Business[(B)]	$2,962,699	$102,013	3.44 %	$2,910,668	$104,624	3.59 %	$2,887,427	$110,792	3.84 %
Real estate – construction and land	356,425	15,146	4.25	419,905	18,831	4.48	557,282	22,384	4.02
Real estate – business	2,193,271	98,693	4.50	2,117,031	101,988	4.82	2,029,214	102,451	5.05
Real estate – personal	1,503,357	65,642	4.37	1,433,869	69,048	4.82	1,476,031	76,531	5.18
Consumer	1,180,538	66,402	5.62	1,118,700	70,127	6.27	1,250,076	84,204	6.74
Revolving home equity	446,204	18,586	4.17	468,718	19,952	4.26	484,878	20,916	4.31
Student[(C)]	—	—	—	—	—	—	246,395	5,783	2.35
Consumer credit card	730,697	85,652	11.72	746,724	84,479	11.31	760,079	89,225	11.74
Overdrafts	6,125	—	—	6,953	—	—	7,288	—	—
Total loans	9,379,316	452,134	4.82	9,222,568	469,049	5.09	9,698,670	512,286	5.28
Loans held for sale	9,688	361	3.73	47,227	1,115	2.36	358,492	6,091	1.70
Investment securities:									
U.S. government & federal agency obligations	332,382	12,260	3.69	357,861	17,268	4.83	439,073	9,673	2.20
Government-sponsored enterprise obligations	306,676	5,653	1.84	253,020	5,781	2.28	203,593	4,591	2.25
State & municipal obligations[(B)]	1,376,872	54,056	3.93	1,174,751	51,988	4.43	966,694	45,469	4.70
Mortgage-backed securities	3,852,616	107,527	2.79	3,556,106	114,405	3.22	2,821,485	113,222	4.01
Asset-backed securities	2,925,249	31,940	1.09	2,443,901	30,523	1.25	1,973,734	38,559	1.95
Other marketable securities[(B)]	139,499	6,556	4.70	171,409	8,455	4.93	183,328	8,889	4.85
Trading securities[(B)]	25,107	637	2.54	20,011	552	2.76	21,899	671	3.06
Non-marketable securities[(B)]	118,879	12,558	10.56	107,501	8,283	7.71	113,326	7,216	6.37
Total investment securities	9,077,280	231,187	2.55	8,084,560	237,255	2.93	6,723,132	228,290	3.40
Short-term federal funds sold and securities purchased under agreements to resell	16,393	82	.50	10,690	55	.51	6,542	48	.73
Long-term securities purchased under agreements to resell	892,624	19,174	2.15	768,904	13,455	1.75	150,235	2,549	1.70
	135,319	339	.25	194,176	487	.25	171,883	427	.25

Interest earning deposits with banks												
Total interest earning assets	19,510,620	703,277	3.60		18,328,125	721,416	3.94		17,108,954	749,691	4.38	
Allowance for loan losses	(178,934)				(191,311)				(195,870)			
Unrealized gain on investment securities	257,511				162,984				149,106			
Cash and due from banks	369,020				348,875				368,340			
Land, buildings and equipment - net	357,336				377,200				395,108			
Other assets	385,125				378,642				410,361			
Total assets	$20,700,678				$19,404,515				$18,235,999			
LIABILITIES AND EQUITY												
Interest bearing deposits:												
Savings	$574,336	802	.14		$525,371	852	.16		$478,592	622	.13	
Interest checking and money market	8,430,559	17,880	.21		7,702,901	25,004	.32		6,785,299	28,676	.42	
Time open & C.D.'s of less than $100,000	1,117,236	7,918	.71		1,291,165	11,352	.88		1,660,462	22,871	1.38	
Time open & C.D.'s of $100,000 and over	1,181,426	7,174	.61		1,409,740	9,272	.66		1,323,952	13,847	1.05	
Total interest bearing deposits	11,303,557	33,774	.30		10,929,177	46,480	.43		10,248,305	66,016	.64	
Borrowings:												
Federal funds purchased and securities sold under agreements to repurchase	1,185,978	808	.07		1,035,007	1,741	.17		1,085,121	2,584	.24	
Other borrowings	108,916	3,481	3.20		112,107	3,680	3.28		452,810	14,948	3.30	
Total borrowings	1,294,894	4,289	.33		1,147,114	5,421	.47		1,537,931	17,532	1.14	
Total interest bearing liabilities	12,598,451	38,063	.30	%	12,076,291	51,901	.43	%	11,786,236	83,548	.71	%
Non-interest bearing deposits	5,522,991				4,742,033				4,114,664			
Other liabilities	334,684				476,249				346,312			
Equity	2,244,552				2,109,942				1,988,787			
Total liabilities and equity	$20,700,678				$19,404,515				$18,235,999			
Net interest margin (T/E)		$665,214				$669,515				$666,143		
Net yield on interest earning assets			3.41	%			3.65	%			3.89	%
Percentage increase (decrease) in net interest margin (T/E) compared to the prior			(.64	)%			.51	%			1.83	%

year

(A) Loans on non-accrual status are included in the computation of average balances. Included in interest income above are loan fees and late charges, net of amortization of deferred loan origination fees and costs, which are immaterial. Credit card income from merchant discounts and net interchange fees are not included in loan income.

(B) Interest income and yields are presented on a fully-taxable equivalent basis using the Federal statutory income tax rate. Loan interest income includes tax free loan income (categorized as business loan income) which includes tax equivalent adjustments of $5,803,000 in 2012, $5,538,000 in 2011, $4,620,000 in 2010, $3,922,000 in 2009, $3,553,000 in 2008 and $2,895,000 in 2007. Investment securities interest income include tax equivalent adjustments of $19,505,000 in 2012, $17,907,000 in 2011, $15,593,000 in 2010, $14,779,000 in 2009,

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Years Ended December 31									
2009			2008			2007			
Average Balance	Interest Income/Expense	Average Rates Earned/Paid	Average Balance	Interest Income/Expense	Average Rates Earned/Paid	Average Balance	Interest Income/Expense	Average Rates Earned/Paid	Average Balance Five Year Compound Growth Rate
$3,119,778	$ 116,686	3.74 %	$3,478,927	$ 170,620	4.90 %	$3,110,386	$ 209,523	6.74 %	(.97)%
739,896	26,746	3.61	701,519	34,445	4.91	671,986	49,436	7.36	(11.91)
2,143,675	108,107	5.04	2,281,664	136,955	6.00	2,204,041	154,819	7.02	(.10)
1,585,273	87,085	5.49	1,522,172	88,322	5.80	1,521,066	90,537	5.95	(.23)
1,464,170	101,761	6.95	1,674,497	119,837	7.16	1,558,302	115,184	7.39	(5.40)
495,629	21,456	4.33	474,635	23,960	5.05	443,748	33,526	7.56	.11
344,243	9,440	2.74	13,708	287	2.10	—	—	—	NM
727,422	89,045	12.24	776,810	83,972	10.81	665,964	84,856	12.74	1.87
9,781	—	—	11,926	—	—	13,823	—	—	(15.02)
10,629,867	560,326	5.27	10,935,858	658,398	6.02	10,189,316	737,881	7.24	(1.64)
397,583	8,219	2.07	347,441	14,968	4.31	321,916	21,940	6.82	(50.38)
169,214	6,754	3.99	7,065	364	5.15	9,063	506	5.58	105.53
137,928	4,219	3.06	176,018	7,075	4.02	401,107	15,999	3.99	(5.23)
873,607	43,882	5.02	695,542	37,770	5.43	594,154	33,416	5.62	18.30
2,802,532	136,921	4.89	2,203,921	112,184	5.09	1,828,478	88,909	4.86	16.07
937,435	30,166	3.22	265,546	13,185	4.97	292,043	13,334	4.57	58.54
179,847	9,793	5.45	98,650	4,243	4.30	129,622	7,355	5.67	1.48
16,927	506	2.99	28,840	1,355	4.70	22,321	1,144	5.13	2.38
136,911	6,398	4.67	133,996	7,730	5.77	92,251	5,710	6.19	5.20
5,254,401	238,639	4.54	3,609,578	183,906	5.09	3,369,039	166,373	4.94	21.92
43,811	222	.51	425,273	8,287	1.95	527,304	25,881	4.91	(50.05)
—	—	—	—	—	—	—	—	—	NM
325,744	807	.25	46,670	198	.42	—	—	—	NM
16,651,406	808,213	4.85	15,364,820	865,757	5.63	14,407,575	952,075	6.61	6.25
(181,417)			(145,176)			(132,234)			6.24
24,105			27,068			25,333			59.01
364,579			451,105			463,970			(4.48)
411,366			412,852			400,161			(2.24)
349,164			343,664			315,522			4.07
$17,619,203			$16,454,333			$15,480,327			5.98
$438,748	642	.15	$400,948	1,186	.30	$392,942	2,067	.53	7.89
5,807,753	30,789	.53	5,123,709	59,947	1.17	4,793,849	114,027	2.38	11.95
2,055,952	51,982	2.53	2,149,119	77,322	3.60	2,359,386	110,957	4.70	(13.89)
1,858,543	35,371	1.90	1,629,500	55,665	3.42	1,480,856	73,739	4.98	(4.42)
10,160,996	118,784	1.17	9,303,276	194,120	2.09	9,027,033	300,790	3.33	4.60

968,643	3,699	.38		1,373,625	25,085	1.83		1,696,613	83,464	4.92		(6.91	)
920,467	31,527	3.43		1,092,746	37,905	3.47		292,446	13,775	4.71		(17.93	)
1,889,110	35,226	1.86		2,466,371	62,990	2.55		1,989,059	97,239	4.89		(8.23	)
12,050,106	154,010	1.28	%	11,769,647	257,110	2.18	%	11,016,092	398,029	3.61	%	2.72	
3,660,166				2,946,534				2,850,982				14.14	
176,676				140,333				134,278				20.04	
1,732,255				1,597,819				1,478,975				8.70	
$17,619,203				$16,454,333				$15,480,327				5.98	%
	$ 654,203				$ 608,647				$ 554,046				
		3.93	%			3.96	%			3.85	%		
		7.48	%			9.85	%			5.64	%		

$12,355,000 in 2008 and $13,079,000 in 2007. These adjustments relate to state and municipal obligations, other marketable securities, trading securities, and non-marketable securities.

(C) In December 2008, the Company purchased $358,451,000 of student loans with the intent to hold to maturity. In October 2010, the seller elected to repurchase the loans under the terms of the original agreement.

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QUARTERLY AVERAGE BALANCE SHEETS — AVERAGE RATES AND YIELDS

	Year ended December 31, 2012							
	Fourth Quarter		Third Quarter		Second Quarter		First Quarter	
(Dollars in millions)	Average Balance	Average Rates Earned/Paid	Average Balance	Average Rates Earned/Paid	Average Balance	Average Rates Earned/Paid	Average Balance	Average Rates Earned/Paid
ASSETS								
Loans:								
Business[(A)]	$3,042	3.29 %	$3,019	3.39 %	$2,895	3.58 %	$2,894	3.52 %
Real estate – construction and land	346	4.11	340	4.30	360	4.24	380	4.34
Real estate – business	2,200	4.33	2,183	4.39	2,206	4.71	2,185	4.57
Real estate – personal	1,572	4.15	1,523	4.31	1,476	4.46	1,441	4.58
Consumer	1,273	5.35	1,205	5.54	1,135	5.73	1,108	5.93
Revolving home equity	436	4.13	444	4.17	449	4.17	455	4.18
Consumer credit card	749	11.42	730	11.83	713	11.87	731	11.78
Overdrafts	6	—	5	—	6	—	8	—
Total loans	9,624	4.64	9,449	4.76	9,240	4.95	9,202	4.95
Loans held for sale	9	3.74	9	3.86	9	3.91	12	3.48
Investment securities:								
U.S. government & federal agency obligations	341	5.11	329	(.07)	331	7.58	328	2.08
Government-sponsored enterprise obligations	400	1.72	276	1.65	265	2.06	283	2.01
State & municipal obligations[(A)]	1,532	3.67	1,388	3.89	1,323	4.03	1,263	4.17
Mortgage-backed securities	3,448	2.79	3,767	2.62	4,010	2.89	4,191	2.85
Asset-backed securities	3,158	.99	2,879	1.10	2,900	1.13	2,762	1.16
Other marketable securities[(A)]	138	5.35	122	4.50	136	4.92	163	4.11
Trading securities[(A)]	21	2.01	24	2.34	23	2.65	33	2.95
Non-marketable securities[(A)]	119	17.51	117	7.54	123	8.60	117	8.55
Total investment securities	9,157	2.59	8,902	2.29	9,111	2.75	9,140	2.56
Short-term federal funds sold and securities purchased under agreements to resell	10	.46	19	.49	22	.53	14	.50
Long-term securities purchased under agreements to resell	1,022	2.10	848	2.31	850	2.17	850	2.02
Interest earning deposits with banks	209	.25	81	.20	163	.28	88	.25
Total interest earning assets	20,031	3.52	19,308	3.49	19,395	3.75	19,306	3.66
Allowance for loan losses	(174)		(177)		(181)		(184)	
Unrealized gain on investment securities	282		275		243		230	

Cash and due from banks	385			366			358			367		
Land, buildings and equipment – net	359			353			356			361		
Other assets	382			392			378			387		
Total assets	$21,265			$20,517			$20,549			$20,467		
LIABILITIES AND EQUITY												
Interest bearing deposits:												
Savings	$581	.13		$582	.15		$584	.12		$550	.15	
Interest checking and money market	8,638	.19		8,401	.21		8,369	.21		8,312	.24	
Time open & C.D.'s under $100,000	1,084	.68		1,101	.70		1,129	.71		1,156	.73	
Time open & C.D.'s $100,000 & over	1,030	.65		1,005	.69		1,250	.59		1,444	.53	
Total interest bearing deposits	11,333	.28		11,089	.30		11,332	.30		11,462	.32	
Borrowings:												
Federal funds purchased and securities sold under agreements to repurchase	1,130	.07		1,217	.07		1,110	.06		1,287	.07	
Other borrowings	104	3.25		109	3.11		111	3.16		112	3.26	
Total borrowings	1,234	.33		1,326	.32		1,221	.35		1,399	.33	
Total interest bearing liabilities	12,567	.28	%	12,415	.30	%	12,553	.30	%	12,861	.32	%
Non-interest bearing deposits	6,013			5,536			5,405			5,132		
Other liabilities	399			296			368			276		
Equity	2,286			2,270			2,223			2,198		
Total liabilities and equity	$21,265			$20,517			$20,549			$20,467		
Net interest margin (T/E)	$168			$160			$171			$166		
Net yield on interest earning assets		3.35	%		3.30	%		3.55	%		3.45	%

(A) Includes tax equivalent calculations.

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(Dollars in millions)	Year ended December 31, 2011							
	Fourth Quarter		Third Quarter		Second Quarter		First Quarter	
	Average Balance	Average Rates Earned/Paid	Average Balance	Average Rates Earned/Paid	Average Balance	Average Rates Earned/Paid	Average Balance	Average Rates Earned/Paid
ASSETS								
Loans:								
Business(A)	$2,819	3.53 %	$2,815	3.56 %	$2,959	3.64 %	$3,053	3.65 %
Real estate – construction and land	387	4.52	412	4.42	430	4.51	452	4.49
Real estate – business	2,162	4.67	2,123	4.74	2,101	4.94	2,081	4.92
Real estate – personal	1,421	4.64	1,430	4.75	1,441	4.87	1,444	5.00
Consumer	1,111	6.08	1,105	6.20	1,112	6.32	1,147	6.47
Revolving home equity	465	4.24	467	4.27	468	4.24	475	4.28
Consumer credit card	734	11.62	735	11.59	743	11.13	775	10.92
Overdrafts	7	—	7	—	7	—	7	—
Total loans	9,106	5.01	9,094	5.07	9,261	5.12	9,434	5.15
Loans held for sale	37	2.55	42	2.57	52	2.37	58	2.08
Investment securities:								
U.S. government & federal agency obligations	329	2.49	328	3.40	342	9.72	435	3.84
Government-sponsored enterprise obligations	305	1.93	262	2.92	235	2.23	209	2.07
State & municipal obligations(A)	1,239	4.16	1,185	4.20	1,160	4.75	1,113	4.63
Mortgage-backed securities	4,453	2.71	3,765	2.95	3,058	3.63	2,929	3.93
Asset-backed securities	2,646	1.12	2,403	1.15	2,403	1.31	2,321	1.44
Other marketable securities(A)	165	5.39	173	4.27	173	4.18	176	5.91
Trading securities(A)	20	2.87	21	2.52	20	2.78	19	2.88
Non-marketable securities(A)	110	10.81	110	6.59	105	6.24	104	7.04
Total investment securities	9,267	2.56	8,247	2.69	7,496	3.34	7,306	3.28
Short-term federal funds sold and securities purchased under agreements to resell	10	.39	11	.47	16	.53	5	.80
Long-term securities purchased under agreements to resell	850	1.97	850	1.83	804	1.58	568	1.54
Interest earning deposits with banks	123	.25	326	.26	180	.25	146	.25
Total interest earning assets	19,393	3.67	18,570	3.77	17,809	4.15	17,517	4.20
Allowance for loan losses	(186)		(190)		(193)		(196)	
Unrealized gain on investment securities	189		186		147		129	
Cash and due from banks	367		347		334		346	

Land, buildings and equipment – net	370			375			379			385		
Other assets	382			376			387			370		
Total assets	$20,515			$19,664			$18,863			$18,551		
LIABILITIES AND EQUITY												
Interest bearing deposits:												
Savings	$529	.17		$534	.19		$538	.14		$500	.14	
Interest checking and money market	8,068	.29		7,756	.32		7,581	.33		7,399	.37	
Time open & C.D.'s under $100,000	1,186	.75		1,231	.78		1,324	.90		1,426	1.06	
Time open & C.D.'s $100,000 & over	1,368	.59		1,373	.62		1,466	.67		1,434	.76	
Total interest bearing deposits	11,151	.37		10,894	.40		10,909	.43		10,759	.50	
Borrowings:												
Federal funds purchased and securities sold under agreements to repurchase	1,147	.05		1,017	.11		952	.29		1,023	.25	
Other borrowings	112	3.26		112	3.28		112	3.29		112	3.30	
Total borrowings	1,259	.33		1,129	.43		1,064	.61		1,135	.55	
Total interest bearing liabilities	12,410	.37	%	12,023	.40	%	11,973	.45	%	11,894	.51	%
Non-interest bearing deposits	5,173			4,779			4,571			4,437		
Other liabilities	790			729			208			168		
Equity	2,142			2,133			2,111			2,052		
Total liabilities and equity	$20,515			$19,664			$18,863			$18,551		
Net interest margin (T/E)	$168			$164			$171			$167		
Net yield on interest earning assets		3.44	%		3.51	%		3.85	%		3.85	%

(A) Includes tax equivalent calculations.

SUMMARY OF QUARTERLY STATEMENTS OF INCOME

Year ended December 31, 2012	For the Quarter Ended			
(In thousands, except per share data)	12/31/2012	9/30/2012	6/30/2012	3/31/2012
Interest income	$170,185	$163,194	$174,624	$169,966
Interest expense	(8,932)	(9,383)	(9,519)	(10,229)
Net interest income	161,253	153,811	165,105	159,737
Non-interest income	103,309	100,922	100,816	94,583
Investment securities gains (losses), net	(3,728)	3,180	1,336	4,040
Salaries and employee benefits	(94,553)	(89,292)	(87,511)	(89,543)
Other expense	(63,724)	(64,099)	(68,829)	(60,918)
Provision for loan losses	(8,326)	(5,581)	(5,215)	(8,165)
Income before income taxes	94,231	98,941	105,702	99,734
Income taxes	(27,628)	(32,155)	(34,466)	(32,920)
Non-controlling interest	188	(780)	(503)	(1,015)
Net income attributable to Commerce Bancshares, Inc.	$66,791	$66,006	$70,733	$65,799
Net income per common share — basic*	$.73	$.71	$.77	$.70
Net income per common share — diluted*	$.72	$.72	$.76	$.70
Weighted average shares — basic*	90,825	91,239	91,774	92,632
Weighted average shares — diluted*	90,999	91,552	92,056	92,984

Year ended December 31, 2011	For the Quarter Ended			
(In thousands, except per share data)	12/31/2011	9/30/2011	6/30/2011	3/31/2011
Interest income	$173,223	$170,835	$178,087	$175,826
Interest expense	(11,466)	(12,205)	(13,377)	(14,853)
Net interest income	161,757	158,630	164,710	160,973
Non-interest income	94,035	101,632	101,344	95,906
Investment securities gains, net	4,942	2,587	1,956	1,327
Salaries and employee benefits	(88,010)	(85,700)	(84,223)	(87,392)
Other expense	(68,020)	(68,046)	(69,290)	(66,568)
Provision for loan losses	(12,143)	(11,395)	(12,188)	(15,789)
Income before income taxes	92,561	97,708	102,309	88,457
Income taxes	(29,514)	(31,699)	(32,692)	(27,507)
Non-controlling interest	(1,543)	(657)	(583)	(497)
Net income attributable to Commerce Bancshares, Inc.	$61,504	$65,352	$69,034	$60,453
Net income per common share — basic*	$.66	$.69	$.72	$.63
Net income per common share — diluted*	$.66	$.69	$.71	$.63
Weighted average shares — basic*	92,814	93,951	95,410	95,330
Weighted average shares — diluted*	93,086	94,224	95,837	95,737

Year ended December 31, 2010	For the Quarter Ended			
(In thousands, except per share data)	12/31/2010	9/30/2010	6/30/2010	3/31/2010
Interest income	$177,436	$178,916	$185,057	$188,069
Interest expense	(16,759)	(19,479)	(21,949)	(25,359)
Net interest income	160,677	159,437	163,108	162,710
Non-interest income	110,454	100,010	101,458	93,189
Investment securities gains (losses), net	1,204	16	660	(3,665)
Salaries and employee benefits	(86,562)	(85,442)	(87,108)	(87,438)
Other expense	(77,469)	(70,144)	(68,685)	(68,286)
Provision for loan losses	(21,647)	(21,844)	(22,187)	(34,322)
Income before income taxes	86,657	82,033	87,246	62,188

Income taxes	(24,432)	(26,012)	(27,428)	(18,377)
Non-controlling interest	(304)	(136)	(84)	359
Net income attributable to Commerce Bancshares, Inc.	$61,921	$55,885	$59,734	$44,170
Net income per common share — basic*	$.65	$.57	$.62	$.46
Net income per common share — diluted*	$.64	$.58	$.61	$.46
Weighted average shares — basic*	95,437	96,129	96,071	95,937
Weighted average shares — diluted*	95,837	96,535	96,528	96,460

* Restated for the 5% stock dividend distributed in 2012.

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Item 7a. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information required by this item is set forth on pages 43 through 45 of Management's Discussion and Analysis of Financial Condition and Results of Operations.

Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
Commerce Bancshares, Inc.:

We have audited the accompanying consolidated balance sheets of Commerce Bancshares, Inc. and subsidiaries (the Company) as of December 31, 2012 and 2011, and the related consolidated statements of income, comprehensive income, changes in equity, and cash flows for each of the years in the three-year period ended December 31, 2012. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Commerce Bancshares, Inc. and subsidiaries as of December 31, 2012 and 2011, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2012, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2012, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 22, 2013 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

Kansas City, Missouri
February 22, 2013

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Commerce Bancshares, Inc. and Subsidiaries
CONSOLIDATED BALANCE SHEETS

	December 31	
	2012	2011
	(In thousands)	
ASSETS		
Loans	$9,831,384	$9,177,478
Allowance for loan losses	(172,532)	(184,532)
Net loans	9,658,852	8,992,946
Loans held for sale	8,827	31,076
Investment securities:		
Available for sale ($736,183,000 and $418,046,000 pledged in 2012 and 2011, respectively, to secure repurchase agreements)	9,522,248	9,224,702
Trading	28,837	17,853
Non-marketable	118,650	115,832
Total investment securities	9,669,735	9,358,387
Short-term federal funds sold and securities purchased under agreements to resell	27,595	11,870
Long-term securities purchased under agreements to resell	1,200,000	850,000
Interest earning deposits with banks	179,164	39,853
Cash and due from banks	573,066	465,828
Land, buildings and equipment – net	357,612	360,146
Goodwill	125,585	125,585
Other intangible assets – net	5,300	7,714
Other assets	353,853	405,962
Total assets	$22,159,589	$20,649,367
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Non-interest bearing	$6,299,903	$5,377,549
Savings, interest checking and money market	9,817,943	8,933,941
Time open and C.D.'s of less than $100,000	1,074,618	1,166,104
Time open and C.D.'s of $100,000 and over	1,156,189	1,322,289
Total deposits	18,348,653	16,799,883
Federal funds purchased and securities sold under agreements to repurchase	1,083,550	1,256,081
Other borrowings	103,710	111,817
Other liabilities	452,102	311,225
Total liabilities	19,988,015	18,479,006
Commerce Bancshares, Inc. stockholders' equity:		
Preferred stock, $1 par value Authorized and unissued 2,000,000 shares	—	—
Common stock, $5 par value Authorized 100,000,000 shares; issued 91,729,235 and 89,277,398 shares in 2012 and 2011, respectively	458,646	446,387
Capital surplus	1,102,507	1,042,065
Retained earnings	477,210	575,419
Treasury stock of 196,922 and 217,755 shares in 2012 and 2011, respectively, at cost	(7,580)	(8,362)
Accumulated other comprehensive income	136,344	110,538
Total Commerce Bancshares, Inc. stockholders' equity	2,167,127	2,166,047
Non-controlling interest	4,447	4,314
Total equity	2,171,574	2,170,361

Total liabilities and equity	$22,159,589	$20,649,367

See accompanying notes to consolidated financial statements.

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Commerce Bancshares, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF INCOME

	For the Years Ended December 31		
(In thousands, except per share data)	2012	2011	2010
INTEREST INCOME			
Interest and fees on loans	$446,331	$463,511	$507,666
Interest on loans held for sale	361	1,115	6,091
Interest on investment securities	211,682	219,348	212,697
Interest on short-term federal funds sold and securities purchased under agreements to resell	82	55	48
Interest on long-term securities purchased under agreements to resell	19,174	13,455	2,549
Interest on deposits with banks	339	487	427
Total interest income	677,969	697,971	729,478
INTEREST EXPENSE			
Interest on deposits:			
Savings, interest checking and money market	18,682	25,856	29,298
Time open and C.D.'s of less than $100,000	7,918	11,352	22,871
Time open and C.D.'s of $100,000 and over	7,174	9,272	13,847
Interest on federal funds purchased and securities sold under agreements to repurchase	808	1,741	2,584
Interest on other borrowings	3,481	3,680	14,946
Total interest expense	38,063	51,901	83,546
Net interest income	639,906	646,070	645,932
Provision for loan losses	27,287	51,515	100,000
Net interest income after provision for loan losses	612,619	594,555	545,932
NON-INTEREST INCOME			
Bank card transaction fees	154,197	157,077	148,888
Trust fees	94,679	88,313	80,963
Deposit account charges and other fees	79,485	82,651	92,637
Capital market fees	21,066	19,846	21,098
Consumer brokerage services	10,162	10,018	9,190
Loan fees and sales	6,037	7,580	23,116
Other	34,004	27,432	29,219
Total non-interest income	399,630	392,917	405,111
INVESTMENT SECURITIES GAINS (LOSSES), NET			
Impairment reversals on securities	11,223	2,190	13,058
Noncredit-related reversals on securities not expected to be sold	(12,713)	(4,727)	(18,127)
Net impairment losses	(1,490)	(2,537)	(5,069)
Realized gains on sales and fair value adjustments	6,318	13,349	3,284
Investment securities gains (losses), net	4,828	10,812	(1,785)
NON-INTEREST EXPENSE			
Salaries and employee benefits	360,899	345,325	346,550
Net occupancy	45,534	46,434	46,987
Equipment	20,147	22,252	23,324
Supplies and communication	22,321	22,448	27,113
Data processing and software	73,798	68,103	67,935
Marketing	15,106	16,767	18,161
Deposit insurance	10,438	13,123	19,246
Debit overdraft litigation	—	18,300	—

Debt extinguishment	—	—	11,784
Other	70,226	64,497	70,034
Total non-interest expense	618,469	617,249	631,134
Income before income taxes	398,608	381,035	318,124
Less income taxes	127,169	121,412	96,249
Net income	271,439	259,623	221,875
Less non-controlling interest expense	2,110	3,280	165
NET INCOME ATTRIBUTABLE TO COMMERCE BANCSHARES, INC.	$269,329	$256,343	$221,710
Net income per common share - basic	$2.91	$2.70	$2.30
Net income per common share - diluted	$2.90	$2.69	$2.29

See accompanying notes to consolidated financial statements.

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Commerce Bancshares, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	For the Years Ended December 31		
(In thousands)	2012	2011	2010
Net income	$271,439	$259,623	$221,875
Other comprehensive income (loss):			
Available for sale debt securities for which a portion of an other-than-temporary impairment (OTTI) has been recorded in earnings:			
Unrealized holding gains subsequent to initial OTTI recognition	12,203	5,184	22,973
Income tax expense	(4,637)	(1,970)	(8,730)
Net unrealized gains on OTTI securities	7,566	3,214	14,243
Other available for sale investment securities:			
Unrealized holding gains	39,271	78,059	6,412
Income tax expense on unrealized gains	(14,927)	(29,663)	(2,470)
Reclassification adjustment for gains included in net income	(357)	(177)	(3,488)
Reclassification adjustment for tax expense on gains included in net income	139	68	1,359
Net unrealized gains on other securities	24,126	48,287	1,813
Prepaid pension cost:			
Amortization of accumulated pension loss	2,953	1,949	2,208
Net loss arising during period	(12,447)	(8,898)	(786)
Income tax (expense) benefit on change in pension loss	3,608	2,641	(540)
Change in pension loss	(5,886)	(4,308)	882
Other comprehensive income	25,806	47,193	16,938
Comprehensive income	297,245	306,816	238,813
Non-controlling interest expense	(2,110)	(3,280)	(165)
Comprehensive income attributable to Commerce Bancshares, Inc.	$295,135	$303,536	$238,648

See accompanying notes to consolidated financial statements.

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Commerce Bancshares, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Years Ended December 31		
(In thousands)	2012	2011	2010
OPERATING ACTIVITIES			
Net income	$271,439	$259,623	$221,875
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	27,287	51,515	100,000
Provision for depreciation and amortization	43,448	46,743	48,924
Amortization of investment security premiums, net	36,238	18,972	21,635
Deferred income tax (benefit) expense	16,234	(2,836)	(9,085)
Investment securities (gains) losses, net	(4,828)	(10,812)	1,785
Gain on sale of held to maturity student loans	—	—	(6,914)
Net gains on sales of loans held for sale	(376)	(2,040)	(10,402)
Proceeds from sales of loans held for sale	22,720	87,732	635,743
Originations of loans held for sale	—	(52,995)	(344,360)
Net (increase) decrease in trading securities	(9,645)	2,354	(928)
Stock-based compensation	5,001	4,731	6,021
(Increase) decrease in interest receivable	3,149	(2,010)	12,041
Decrease in interest payable	(1,272)	(4,598)	(9,462)
Increase (decrease) in income taxes payable	(13,395)	14,519	2,714
Net tax benefit related to equity compensation plans	(2,094)	(1,065)	(1,178)
Other changes, net	(10,794)	(2,472)	2,768
Net cash provided by operating activities	383,112	407,361	671,177
INVESTING ACTIVITIES			
Proceeds from sales of available for sale securities	16,875	19,833	78,640
Proceeds from maturities/pay downs of available for sale securities	3,080,664	2,562,551	2,308,323
Purchases of available for sale securities	(3,182,857)	(4,517,463)	(3,217,600)
Net (increase) decrease in loans	(693,193)	168,983	644,314
Long-term securities purchased under agreements to resell	(575,000)	(500,000)	(450,000)
Repayments of long-term securities purchased under agreements to resell	225,000	100,000	—
Purchases of land, buildings and equipment	(34,969)	(21,332)	(18,528)
Sales of land, buildings and equipment	2,643	2,593	397
Net cash used in investing activities	(1,160,837)	(2,184,835)	(654,454)
FINANCING ACTIVITIES			
Net increase in non-interest bearing, savings, interest checking and money market deposits	1,777,058	1,981,201	1,300,555
Net decrease in time open and C.D.'s	(257,586)	(255,769)	(469,557)
Long-term securities sold under agreements to repurchase	—	—	400,000
Repayment of long-term securities sold under agreements to repurchase	—	—	(500,000)
Net increase (decrease) in short-term federal funds purchased and securities sold under agreements to repurchase	(172,531)	273,254	(20,364)
Repayment of other long-term borrowings	(8,107)	(456)	(623,789)
Purchases of treasury stock	(104,909)	(101,154)	(40,984)
Issuance of stock under stock purchase and equity compensation plans	15,588	15,349	11,310
Net tax benefit related to equity compensation plans	2,094	1,065	1,178
Cash dividends paid on common stock	(211,608)	(79,140)	(78,231)
Net cash provided by (used in) financing activities	1,039,999	1,834,350	(19,882)

Increase (decrease) in cash and cash equivalents	262,274	56,876	(3,159)
Cash and cash equivalents at beginning of year	517,551	460,675	463,834
Cash and cash equivalents at end of year	$779,825	$517,551	$460,675
Income tax payments, net	$119,166	$106,653	$100,610
Interest paid on deposits and borrowings	$39,335	$56,499	$93,008
Loans transferred to foreclosed real estate	$8,167	$22,957	$16,440

See accompanying notes to consolidated financial statements.

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Commerce Bancshares, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

	Commerce Bancshares, Inc. Shareholders						
(In thousands, except per share data)	Common Stock	Capital Surplus	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Non-Controlling Interest	Total
Balance, December 31, 2009	$415,637	$854,490	$568,532	$(838)	$ 46,407	$ 1,677	$1,885,905
Net income			221,710			165	221,875
Other comprehensive income					16,938		16,938
Distributions to non-controlling interest						(365)	(365)
Purchase of treasury stock				(40,984)			(40,984)
Cash dividends paid ($.812 per share)			(78,231)				(78,231)
Net tax benefit related to equity compensation plans		1,178					1,178
Stock-based compensation		6,021					6,021
Issuance under stock purchase and equity compensation plans, net	2,196	3,102		6,012			11,310
5% stock dividend, net	16,109	106,502	(156,233)	33,439			(183)
Balance, December 31, 2010	433,942	971,293	555,778	(2,371)	63,345	1,477	2,023,464
Net income			256,343			3,280	259,623
Other comprehensive income					47,193		47,193
Distributions to non-controlling interest						(443)	(443)
Purchase of treasury stock				(101,154)			(101,154)
Cash dividends paid ($.834 per share)			(79,140)				(79,140)
Net tax benefit related to equity compensation plans		1,065					1,065
Stock-based compensation		4,731					4,731
Issuance under stock purchase and equity compensation plans, net	2,539	4,061		8,749			15,349
5% stock dividend, net	9,906	60,915	(157,562)	86,414			(327)
Balance, December 31, 2011	446,387	1,042,065	575,419	(8,362)	110,538	4,314	2,170,361
Net income			269,329			2,110	271,439
Other comprehensive income					25,806		25,806
Distributions to non-controlling interest						(1,977)	(1,977)
Purchase of treasury stock				(104,909)			(104,909)
Cash dividends paid ($2.305 per share)			(211,608)				(211,608)
Net tax benefit related to equity compensation plans		2,094					2,094
Stock-based compensation		5,001					5,001

Issuance under stock purchase and equity compensation plans, net		(16,905)		32,493			15,588
5% stock dividend, net	12,259	70,252	(155,930)	73,198			(221)
Balance, December 31, 2012	$458,646	$1,102,507	$477,210	$(7,580)	$ 136,344	$ 4,447	$2,171,574

See accompanying notes to consolidated financial statements.

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Commerce Bancshares, Inc. and Subsidiaries
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Nature of Operations

Commerce Bancshares, Inc. and its subsidiaries (the Company) conducts its principal activities from approximately 360 locations throughout Missouri, Illinois, Kansas, Oklahoma and Colorado. Principal activities include retail and commercial banking, investment management, securities brokerage, mortgage banking, credit related insurance and private equity investment activities.

Basis of Presentation

The Company follows accounting principles generally accepted in the United States of America (GAAP) and reporting practices applicable to the banking industry. The preparation of financial statements under GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and notes. These estimates are based on information available to management at the time the estimates are made. While the consolidated financial statements reflect management's best estimates and judgments, actual results could differ from those estimates. The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries (after elimination of all material intercompany balances and transactions). Certain amounts for prior years have been reclassified to conform to the current year presentation. Such reclassifications had no effect on net income or total assets.

Cash and Cash Equivalents

In the accompanying consolidated statements of cash flows, cash and cash equivalents include "Cash and due from banks", "Short-term federal funds sold and securities purchased under agreements to resell", and "Interest earning deposits with banks" as segregated in the accompanying consolidated balance sheets.

Loans and Related Earnings

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding principal balances, net of undisbursed loan proceeds, the allowance for loan losses, and any deferred fees and costs on originated loans. Origination fee income received on loans and amounts representing the estimated direct costs of origination are deferred and amortized to interest income over the life of the loan using the interest method. Prepayment premium or yield maintenance agreements are generally required on all term commercial loans with fixed rate intervals of 3 years or more.

Interest on loans is accrued based upon the principal amount outstanding. Interest income is recognized primarily on the level yield method. Loan and commitment fees, net of costs, are deferred and recognized in income over the term of the loan or commitment as an adjustment of yield. Annual fees charged on credit card loans are capitalized to principal and amortized over 12 months to loan fees and sales. Other credit card fees, such as cash advance fees and late payment fees, are recognized in income as an adjustment of yield when charged to the cardholder's account.

Non-Accrual Loans

Loans are placed on non-accrual status when management does not expect to collect payments consistent with acceptable and agreed upon terms of repayment. Business, construction real estate, business real estate, and personal real estate loans that are contractually 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. Consumer, revolving home equity and credit card loans are exempt under regulatory rules from being classified as non-accrual. When a loan is placed on non-accrual status, any interest previously accrued but not collected is reversed against current income, and the loan is charged off to the extent uncollectible. Principal and interest payments received on non-accrual loans are generally applied to principal. Interest is included in income only after all previous loan charge-offs have been recovered and is

recorded only as received. The loan is returned to accrual status only when the borrower has brought all past due principal and interest payments current, and, in the opinion of management, the borrower has demonstrated the ability to make future payments of principal and interest as scheduled. A six month history of sustained payment performance is generally required before reinstatement of accrual status.

Restructured Loans

A loan is accounted for as a troubled debt restructuring if the Company, for economic or legal reasons related to the borrowers' financial difficulties, grants a concession to the borrower that it would not otherwise consider. A troubled debt restructuring typically involves (1) modification of terms such as a reduction of the stated interest rate, loan principal, or accrued interest, (2) a loan renewal at a stated interest rate lower than the current market rate for a new loan with similar risk, or (3) debt that was not reaffirmed in bankruptcy. Business, business real estate, construction real estate and personal real estate troubled debt restructurings with impairment charges are placed on non-accrual status. The Company measures the impairment loss of a troubled debt restructuring in the same manner as described below. Troubled debt restructurings which are performing under their contractual terms continue to accrue interest which is recognized in current earnings.

Impaired Loans

Loans are evaluated regularly by management for impairment. Included in impaired loans are all non-accrual loans, as well as loans that have been classified as troubled debt restructurings. Once a loan has been identified as impaired, impairment is measured based on either the present value of the expected future cash flows at the loan's initial effective interest rate or the fair value of the collateral if collateral dependent. Factors considered in determining impairment include delinquency status, cash flow analysis, credit analysis, and collateral value and availability.

Loans Held for Sale

Loans held for sale include student loans and certain fixed rate residential mortgage loans. These loans are typically classified as held for sale upon origination based upon management's intent to sell the production of these loans. They are carried at the lower of aggregate cost or fair value. Fair value is determined based on prevailing market prices for loans with similar characteristics, sale contract prices, or, for those portfolios for which management has concerns about contractual performance, discounted cash flow analyses. Declines in fair value below cost (and subsequent recoveries) are recognized in loan fees and sales. Deferred fees and costs related to these loans are not amortized but are recognized as part of the cost basis of the loan at the time it is sold. Gains or losses on sales are recognized upon delivery and included in loan fees and sales.

Allowance/Provision for Loan Losses

The allowance for loan losses is maintained at a level believed to be appropriate by management to provide for probable loan losses inherent in the portfolio as of the balance sheet date, including losses on known or anticipated problem loans as well as for loans which are not currently known to require specific allowances. Management has established a process to determine the amount of the allowance for loan losses which assesses the risks and losses inherent in its portfolio. Business, construction real estate and business real estate loans are normally larger and more complex, and their collection rates are harder to predict. These loans are more likely to be collateral dependent and are allocated a larger reserve, due to their potential volatility. Personal real estate, credit card, consumer and revolving home equity loans are individually smaller and perform in a more homogenous manner, making loss estimates more predictable. Management's process provides an allowance consisting of a specific allowance component based on certain individually evaluated loans and a general component based on estimates of reserves needed for pools of loans.

Loans subject to individual evaluation generally consist of business, construction real estate, business real estate and personal real estate loans on non-accrual status. These impaired loans are evaluated individually for the impairment of repayment potential and collateral adequacy, and in conjunction with current economic conditions and loss experience, allowances are estimated. Other impaired loans identified as performing troubled debt restructurings are collectively evaluated because they have similar risk characteristics. Loans which have not been identified as impaired are segregated by loan type and sub-type and are collectively evaluated. Reserves calculated for these loan pools are estimated using a consistent methodology that considers historical loan loss experience by loan type, delinquencies, current economic factors, loan risk ratings and industry concentrations.

The Company's estimate of the allowance for loan losses and the corresponding provision for loan losses is based on various judgments and assumptions made by management. The amount of the allowance for loan losses is highly dependent on management's estimates affecting valuation, appraisal of collateral, evaluation of performance and status, and the amount and timing of future cash flows expected to be received on impaired loans. Factors that influence these judgments include past loan loss experience, current loan portfolio composition and characteristics, trends in portfolio risk ratings, levels of non-performing assets, prevailing regional and national economic conditions, and the Company's ongoing loan review process.

The estimates, appraisals, evaluations, and cash flows utilized by management may be subject to frequent adjustments due to changing economic prospects of borrowers or properties. These estimates are reviewed periodically and adjustments, if necessary, are recorded in the provision for loan losses in the periods in which they become known.

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Loans, or portions of loans, are charged off to the extent deemed uncollectible. Loan charge-offs reduce the allowance for loan losses, and recoveries of loans previously charged off are added back to the allowance. Business, business real estate, construction real estate and personal real estate loans are generally charged down to estimated collectible balances when they are placed on non-accrual status. Consumer loans and related accrued interest are normally charged down to the fair value of related collateral (or are charged off in full if no collateral) once the loans are more than 120 days delinquent. Credit card loans are charged off against the allowance for loan losses when the receivable is more than 180 days past due. The interest and fee income previously capitalized but not collected on credit card charge-offs is reversed against interest income.

Operating, Direct Financing and Sales Type Leases
The net investment in direct financing and sales type leases is included in loans on the Company's consolidated balance sheets and consists of the present values of the sum of the future minimum lease payments and estimated residual value of the leased asset. Revenue consists of interest earned on the net investment and is recognized over the lease term as a constant percentage return thereon. The net investment in operating leases is included in other assets on the Company's consolidated balance sheets. It is carried at cost, less the amount depreciated to date. Depreciation is recognized, on the straight-line basis, over the lease term to the estimated residual value. Operating lease revenue consists of the contractual lease payments and is recognized over the lease term in other non-interest income. Estimated residual values are established at lease inception utilizing contract terms, past customer experience, and general market data and are reviewed and adjusted, if necessary, on an annual basis.

Investments in Debt and Equity Securities
The Company has classified the majority of its investment portfolio as available for sale. From time to time, the Company sells securities and utilizes the proceeds to reduce borrowings, fund loan growth, or modify its interest rate profile. Securities classified as available for sale are carried at fair value. Changes in fair value, excluding certain losses associated with other-than-temporary impairment (OTTI), are reported in other comprehensive income (loss), a component of stockholders' equity. Securities are periodically evaluated for OTTI in accordance with guidance provided in ASC 320-10-35. For securities with OTTI, the entire loss in fair value is required to be recognized in current earnings if the Company intends to sell the securities or believes it likely that it will be required to sell the security before the anticipated recovery. If neither condition is met, but the Company does not expect to recover the amortized cost basis, the Company determines whether a credit loss has occurred, and the loss is then recognized in current earnings. The noncredit-related portion of the overall loss is reported in other comprehensive income (loss). Mortgage and asset-backed securities whose credit ratings are below AA at their purchase date are evaluated for OTTI under ASC 325-40-35, which requires evaluations for OTTI at purchase date and in subsequent periods. Gains and losses realized upon sales of securities are calculated using the specific identification method and are included in Investment securities gains (losses), net, in the consolidated statements of income. Premiums and discounts are amortized to interest income over the estimated lives of the securities. Prepayment experience is continually evaluated to determine the appropriate estimate of the future rate of prepayment. When a change in a bond's estimated remaining life is necessary, a corresponding adjustment is made in the related amortization of premium or discount accretion.

Non-marketable securities include certain private equity investments, consisting of both debt and equity instruments. These securities are carried at fair value in accordance with ASC 946-10-15, with changes in fair value reported in current earnings. In the absence of readily ascertainable market values, fair value is estimated using internally developed models. Changes in fair value and gains and losses from sales are included in Investment securities gains (losses), net. Other non-marketable securities acquired for debt and regulatory purposes are accounted for at cost.

Trading account securities, which are bought and held principally for the purpose of resale in the near term, are carried at fair value. Gains and losses, both realized and unrealized, are recorded in non-interest income.

Purchases and sales of securities are recognized on a trade date basis. A receivable or payable is recognized for pending transaction settlements.

Securities Purchased under Agreements to Resell and Securities Sold under Agreements to Repurchase
The Company periodically enters into investments of securities under agreements to resell with large financial institutions. These agreements are accounted for as collateralized financing transactions. Securities pledged by the counterparties to secure these agreements are delivered to a third party custodian. Collateral is valued daily, and the Company may require counterparties to deposit additional collateral, or the Company may return collateral pledged when appropriate to maintain full collateralization for these transactions. At December 31, 2012, the Company had entered into $1.2 billion of long-term agreements to resell and had accepted securities valued at $1.3 billion as collateral.

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Securities sold under agreements to repurchase are offered to cash management customers as an automated, collateralized investment account and totaled $659.0 million at December 31, 2012. Securities sold are also used by the Bank to obtain additional borrowed funds at favorable rates, and at December 31, 2012, such securities sold totaled $400.0 million of long-term structured repurchase agreements. As of December 31, 2012, the Company had pledged $2.1 billion of available for sale securities as collateral for repurchase agreements.

As permitted by current accounting guidance, the Company offsets certain securities purchased under agreements to resell against securities sold under agreements to repurchase in its balance sheet presentation. These agreements, which are not included in the balance sheet amounts above, are further discussed in Note 3, Investment Securities.

Land, Buildings and Equipment
Land is stated at cost, and buildings and equipment are stated at cost, including capitalized interest when appropriate, less accumulated depreciation. Depreciation is computed using straight-line and accelerated methods. The Company generally assigns depreciable lives of 30 years for buildings, 10 years for building improvements, and 3 to 8 years for equipment. Leasehold improvements are amortized over the shorter of their estimated useful lives or remaining lease terms. Maintenance and repairs are charged to non-interest expense as incurred.

Foreclosed Assets
Foreclosed assets consist of property that has been repossessed and is comprised of commercial and residential real estate and other non-real estate property, including auto and recreational and marine vehicles. The assets are initially recorded at the lower of the loan balance or fair value less estimated selling costs. Initial valuation adjustments are charged to the allowance for loan losses. Fair values are estimated primarily based on appraisals, third-party price opinions, or internally developed pricing models. After initial recognition, fair value estimates are updated periodically, and the assets may be marked down further, reflecting a new cost basis. These valuation adjustments, in addition to gains and losses realized on sales and net operating expenses, are recorded in other non-interest expense.

Intangible Assets
Goodwill and intangible assets that have indefinite useful lives are not amortized but are tested annually for impairment. Intangible assets that have finite useful lives, such as core deposit intangibles and mortgage servicing rights, are amortized over their estimated useful lives. Core deposit intangibles are amortized over periods of 8 to 14 years, representing their estimated lives, using accelerated methods. Mortgage servicing rights are amortized in proportion to and over the period of estimated net servicing income, considering appropriate prepayment assumptions.

When facts and circumstances indicate potential impairment of amortizable intangible assets, the Company evaluates the recoverability of the asset carrying value, using estimates of undiscounted future cash flows over the remaining asset life. Any impairment loss is measured by the excess of carrying value over fair value. Goodwill impairment tests are performed on an annual basis or when events or circumstances dictate. In these tests, the fair value of each reporting unit, or segment, is compared to the carrying amount of that reporting unit in order to determine if impairment is indicated. If so, the implied fair value of the reporting unit's goodwill is compared to its carrying amount, and the impairment loss is measured by the excess of the carrying value over fair value. There has been no impairment resulting from goodwill impairment tests. However, adverse changes in the economic environment, operations of the reporting unit, or other factors could result in a decline in the implied fair value.

Income Taxes
Amounts provided for income tax expense are based on income reported for financial statement purposes and do not necessarily represent amounts currently payable under tax laws. Deferred income taxes are provided for temporary differences between the financial reporting bases and income tax bases of the Company's assets and liabilities, net operating losses, and tax credit carryforwards. Deferred tax assets and liabilities are measured using the enacted tax rates that are expected to apply to taxable income when such assets and liabilities are anticipated to be settled or

realized. The effect on deferred tax assets and liabilities of a change in tax rates is recognized as tax expense or benefit in the period that includes the enactment date of the change. In determining the amount of deferred tax assets to recognize in the financial statements, the Company evaluates the likelihood of realizing such benefits in future periods. A valuation allowance is established if it is more likely than not that all or some portion of the deferred tax asset will not be realized. The Company recognizes interest and penalties related to income taxes within income tax expense in the consolidated statements of income.

The Company and its eligible subsidiaries file a consolidated federal income tax return. State and local income tax returns are filed on a combined, consolidated or separate return basis based upon each jurisdiction's laws and regulations.

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Derivatives
As required by current accounting guidance, all derivatives are carried at fair value on the balance sheet. Accounting for changes in the fair value of derivatives (gains and losses) differs depending on whether a qualifying hedge relationship has been designated and on the type of hedge relationship. Derivatives used to hedge the exposure to change in the fair value of an asset, liability, or firm commitment attributable to a particular risk are considered fair value hedges. Under the fair value hedging model, gains or losses attributable to the change in fair value of the derivative, as well as gains and losses attributable to the change in fair value of the hedged item, are recognized in current earnings. Derivatives used to hedge the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges. Under the cash flow hedging model, the effective portion of the gain or loss related to the derivative is recognized as a component of other comprehensive income and reclassified to earnings in the same period in which the hedged transaction affects earnings. The ineffective portion is recognized in current earnings. For derivatives that are not part of a hedging relationship, any gain or loss is recognized immediately in current earnings.

The Company formally documents all hedging relationships between hedging instruments and the hedged item, as well as its risk management objective. At December 31, 2012, the Company had three interest rate swaps designated as fair value hedges. The Company performs quarterly assessments, using the regression method, to determine whether the hedging relationship has been highly effective in offsetting changes in fair values.

Other derivatives held by the Company do not qualify for hedge accounting, and gains and losses on these derivatives, as mentioned above, are recognized in current earnings. These include interest rate swaps and caps, which are offered to customers to assist in managing their risks of adverse changes in interest rates. Each contract between the Company and a customer is offset by a contract between the Company and an institutional counterparty, thus minimizing the Company's exposure to rate changes. The Company also enters into certain contracts, known as credit risk participation agreements, to buy or sell credit protection on specific interest rate swaps. It also purchases and sells forward foreign exchange contracts, either in connection with customer transactions, or for its own trading purposes. In addition, in previous years the Company's general practice was to sell fixed rate mortgage loans in the secondary market. Both the mortgage loan commitments and the related sales contracts were accounted for as derivatives.

The Company has master netting arrangements with various counterparties but does not offset derivative assets and liabilities under these arrangements in its consolidated balance sheet.

Additional information about derivatives held by the Company and valuation methods employed is provided in Note 15, Fair Value Measurements and Note 17, Derivative Instruments.

Pension Plan
The Company’s pension plan is described in Note 9, Employee Benefit Plans. The funded status of the plan is recognized as an asset or liability in the consolidated balance sheet, and changes in that funded status are recognized in the year in which the changes occur through other comprehensive income. Plan assets and benefit obligations are measured as of fiscal year end. The measurement of the projected benefit obligation and pension expense involve actuarial valuation methods and the use of various actuarial and economic assumptions. The Company monitors the assumptions and updates them periodically. Due to the long-term nature of the pension plan obligation, actual results may differ significantly from estimations. Such differences are adjusted over time as the assumptions are replaced by facts and values are recalculated.

Stock-Based Compensation
The Company’s stock-based employee compensation plan is described in Note 10, Stock-Based Compensation and Directors Stock Purchase Plan. In accordance with the requirements of ASC 718-10-30-3 and 35-2, the Company measures the cost of stock-based compensation based on the grant-date fair value of the award, recognizing the cost

over the requisite service period. The fair value of an award is estimated using the Black-Scholes option-pricing model. The expense recognized is based on an estimation of the number of awards for which the requisite service is expected to be rendered and is included in salaries and employee benefits in the accompanying consolidated statements of income.

Treasury Stock

Purchases of the Company’s common stock are recorded at cost. Upon re-issuance for acquisitions, exercises of stock-based awards or other corporate purposes, treasury stock is reduced based upon the average cost basis of shares held.

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Income per Share

Basic income per share is computed using the weighted average number of common shares outstanding during each year. Diluted income per share includes the effect of all dilutive potential common shares (primarily stock options and stock appreciation rights) outstanding during each year. The Company applies the two-class method of computing income per share. The two-class method is an earnings allocation formula that determines income per share for common stock and for participating securities, according to dividends declared and participation rights in undistributed earnings. The Company’s restricted share awards are considered to be a class of participating security. All per share data has been restated to reflect the 5% stock dividend distributed in December 2012.

2. Loans and Allowance for Loan Losses

Major classifications within the Company’s held to maturity loan portfolio at December 31, 2012 and 2011 are as follows:

(In thousands)	2012	2011
Commercial:		
Business	$3,134,801	$2,808,265
Real estate — construction and land	355,996	386,598
Real estate — business	2,214,975	2,180,100
Personal Banking:		
Real estate — personal	1,584,859	1,428,777
Consumer	1,289,650	1,114,889
Revolving home equity	437,567	463,587
Consumer credit card	804,245	788,701
Overdrafts	9,291	6,561
Total loans	$9,831,384	$9,177,478

Loans to directors and executive officers of the Parent and its significant subsidiaries, and to their associates, are summarized as follows:

(In thousands)	
Balance at January 1, 2012	$62,788
Additions	289,843
Amounts collected	(291,094)
Amounts written off	—
Balance, December 31, 2012	$61,537

Management believes all loans to directors and executive officers have been made in the ordinary course of business with normal credit terms, including interest rate and collateral considerations, and do not represent more than a normal risk of collection. There were no outstanding loans at December 31, 2012 to principal holders (over 10% ownership) of the Company’s common stock.

The Company’s lending activity is generally centered in Missouri, Illinois, Kansas and other nearby states including Oklahoma, Colorado, Iowa, Ohio, and others. The Company maintains a diversified portfolio with limited industry concentrations of credit risk. Loans and loan commitments are extended under the Company’s normal credit standards, controls, and monitoring features. Most loan commitments are short or intermediate term in nature. Commercial loan maturities generally range from three to seven years. Collateral is commonly required and would include such assets as marketable securities and cash equivalent assets, accounts receivable and inventory, equipment, other forms of personal property, and real estate. At December 31, 2012, unfunded loan commitments totaled $8.4 billion (which included $3.9 billion in unused approved lines of credit related to credit card loan agreements) which could be drawn by customers subject to certain review and terms of agreement. At December 31, 2012, loans totaling $3.3 billion were pledged at the FHLB as collateral for borrowings and letters of credit obtained to secure public deposits.

Additional loans of $1.2 billion were pledged at the Federal Reserve Bank as collateral for discount window borrowings.

The Company has a net investment in direct financing and sales type leases of $311.6 million and $241.8 million at December 31, 2012 and 2011, respectively, which is included in business loans on the Company’s consolidated balance sheets. This investment includes deferred income of $23.6 million and $20.8 million at December 31, 2012 and 2011, respectively. The net investment in operating leases amounted to $21.1 million and $20.1 million at December 31, 2012 and 2011, respectively, and is included in other assets on the Company’s consolidated balance sheets.

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Allowance for loan losses

A summary