COMERICA INC /NEW/
Form 10-Q
November 01, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2011

Or

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

For the transition period from _____ to _____

Commission file number 1-10706

Comerica Incorporated

(Exact name of registrant as specified in its charter)

Delaware	**38-1998421**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

Comerica Bank Tower

1717 Main Street, MC 6404

Dallas, Texas 75201

(Address of principal executive offices)

(Zip Code)

(214) 462-6831

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

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

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

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

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

$5 par value common stock:

Outstanding as of October 26, 2011: 198,682,417 shares

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COMERICA INCORPORATED AND SUBSIDIARIES

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Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

CONSOLIDATED BALANCE SHEETS

Comerica Incorporated and Subsidiaries

(in millions, except share data)	September 30, 2011 (unaudited)	December 31, 2010	September 30, 2010 (unaudited)
ASSETS			
Cash and due from banks	$ 981	$ 668	$ 863
Federal funds sold and securities purchased under agreements to resell			100
Interest-bearing deposits with banks	4,217	1,415	3,031
Other short-term investments	137	141	115
Investment securities available-for-sale	9,732	7,560	6,816
Commercial loans	23,113	22,145	21,432
Real estate construction loans	1,648	2,253	2,444
Commercial mortgage loans	10,539	9,767	10,180
Residential mortgage loans	1,643	1,619	1,586
Consumer loans	2,309	2,311	2,403
Lease financing	927	1,009	1,053
International loans	1,046	1,132	1,182
Total loans	41,225	40,236	40,280
Less allowance for loan losses	(767)	(901)	(957)
Net loans	40,458	39,335	39,323
Premises and equipment	685	630	639
Customers liability on acceptances outstanding	8	9	13
Accrued income and other assets	4,670	3,909	4,104
Total assets	$ 60,888	$ 53,667	$ 55,004
LIABILITIES AND SHAREHOLDERS EQUITY			
Noninterest-bearing deposits	$ 19,116	$ 15,538	$ 15,763
Money market and NOW deposits	20,237	17,622	17,288
Savings deposits	1,771	1,397	1,363
Customer certificates of deposit	5,980	5,482	5,723
Other time deposits	45		
Foreign office time deposits	303	432	494
Total interest-bearing deposits	28,336	24,933	24,868
Total deposits	47,452	40,471	40,631
Short-term borrowings	164	130	179
Acceptances outstanding	8	9	13
Accrued expenses and other liabilities	1,304	1,126	1,085
Medium- and long-term debt	5,009	6,138	7,239

Total liabilities	53,937	47,874	49,147
Common stock - $5 par value:			
Authorized - 325,000,000 shares			
Issued - 228,164,824 shares at 9/30/11 and 203,878,110 shares at 12/31/10 and 9/30/10	1,141	1,019	1,019
Capital surplus	2,162	1,481	1,473
Accumulated other comprehensive loss	(230)	(389)	(238)
Retained earnings	5,471	5,247	5,171
Less cost of common stock in treasury - 29,238,425 shares at 9/30/11, 27,342,518 shares at 12/31/10, and 27,394,831 shares at 9/30/10	(1,593)	(1,565)	(1,568)
Total shareholders equity	6,951	5,793	5,857
Total liabilities and shareholders equity	$ 60,888	$ 53,667	$ 55,004

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF INCOME (unaudited)

Comerica Incorporated and Subsidiaries

(in millions, except per share data)	Three Months Ended September 30, 2011	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
INTEREST INCOME				
Interest and fees on loans	$ 405	$ 399	$ 1,149	$ 1,223
Interest on investment securities	54	55	170	177
Interest on short-term investments	4	2	9	8
Total interest income	463	456	1,328	1,408
INTEREST EXPENSE				
Interest on deposits	24	27	69	91
Interest on medium- and long-term debt	16	25	50	76
Total interest expense	40	52	119	167
Net interest income	423	404	1,209	1,241
Provision for loan losses	38	122	134	423
Net interest income after provision for loan losses	385	282	1,075	818
NONINTEREST INCOME				
Service charges on deposit accounts	53	51	156	159
Fiduciary income	37	38	115	115
Commercial lending fees	22	22	64	66
Letter of credit fees	19	19	55	56
Card fees	17	15	47	43
Foreign exchange income	11	8	30	28
Bank-owned life insurance	10	9	27	26
Brokerage fees	5	6	17	18
Net securities gains	12		18	3
Other noninterest income	15	18	81	60
Total noninterest income	201	186	610	574
NONINTEREST EXPENSES				
Salaries	192	187	565	535
Employee benefits	53	47	153	136
Total salaries and employee benefits	245	234	718	671
Net occupancy expense	44	40	122	120
Equipment expense	17	15	49	47
Outside processing fee expense	25	23	74	69
Software expense	22	22	65	66
Merger and restructuring charges	33		38	
FDIC insurance expense	8	14	35	47
Legal fees	12	9	29	26
Advertising expense	7	7	21	23
Other real estate expense	5	7	19	24
Litigation and operational losses	8	2	16	5
Provision for credit losses on lending-related commitments	(3)	(6)	(8)	1

Other noninterest expenses	37	35	106	104
Total noninterest expenses	460	402	1,284	1,203
Income from continuing operations before income taxes	126	66	401	189
Provision for income taxes	28	7	104	25
Income from continuing operations	98	59	297	164
Income from discontinued operations, net of tax				17
NET INCOME	98	59	297	181
Less:				
Preferred stock dividends				123
Income allocated to participating securities	1		3	
Net income attributable to common shares	$ 97	$ 59	$ 294	$ 58
Basic earnings per common share:				
Income from continuing operations	$ 0.51	$ 0.34	$ 1.63	$ 0.24
Net income	0.51	0.34	1.63	0.34
Diluted earnings per common share:				
Income from continuing operations	0.51	0.33	1.61	0.24
Net income	0.51	0.33	1.61	0.34
Cash dividends declared on common stock	20	9	55	26
Cash dividends declared per common share	0.10	0.05	0.30	0.15

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY (unaudited)

Comerica Incorporated and Subsidiaries

(in millions, except per share data)	Preferred Stock	Common Stock Shares Outstanding	Common Stock Amount	Capital Surplus	Accumulated Other Comprehensive Loss	Retained Earnings	Treasury Stock	Total Shareholders Equity
BALANCE AT DECEMBER 31, 2009	$ 2,151	151.2	$ 894	$ 740	$ (336)	$ 5,161	$ (1,581)	$ 7,029
Net income						181		181
Other comprehensive income, net of tax					98			98
Total comprehensive income								279
Cash dividends declared on preferred stock						(38)		(38)
Cash dividends declared on common stock ($0.15 per share)						(26)		(26)
Purchase of common stock		(0.1)					(4)	(4)
Issuance of common stock		25.1	125	724				849
Redemption of preferred stock	(2,250)							(2,250)
Redemption discount accretion on preferred stock	94					(94)		
Accretion of discount on preferred stock	5					(5)		
Net issuance of common stock under employee stock plans		0.3		(11)		(8)	16	(3)
Share-based compensation				24				24
Other				(4)			1	(3)
BALANCE AT SEPTEMBER 30, 2010	$	176.5	$ 1,019	$ 1,473	$ (238)	$ 5,171	$ (1,568)	$ 5,857
BALANCE AT DECEMBER 31, 2010	$	176.5	$ 1,019	$ 1,481	$ (389)	$ 5,247	$ (1,565)	$ 5,793
Net income						297		297
Other comprehensive income, net of tax					159			159
Total comprehensive income								456
Cash dividends declared on common stock ($0.30 per share)						(55)		(55)
Purchase of common stock		(2.7)					(75)	(75)
Acquisition of Sterling Bancshares, Inc.		24.3	122	681				803
Net issuance of common stock under employee stock plans		0.8		(29)		(18)	47	
Share-based compensation				29				29
BALANCE AT SEPTEMBER 30, 2011	$	198.9	$ 1,141	$ 2,162	$ (230)	$ 5,471	$ (1,593)	$ 6,951

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

Comerica Incorporated and Subsidiaries

(in millions)	Nine Months Ended September 30, 2011	2010
OPERATING ACTIVITIES		
Net income	$ 297	$ 181
Income from discontinued operations, net of tax		17
Income from continuing operations, net of tax	297	164
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	134	423
Provision for credit losses on lending-related commitments	(8)	1
Provision (benefit) for deferred income taxes	52	(4)
Depreciation and software amortization	90	94
Share-based compensation expense	29	24
Net amortization of securities	27	14
Accretion of loan purchase discount	(27)	
Net securities gains	(18)	(3)
Excess tax benefits from share-based compensation arrangements	(1)	(1)
Net decrease in trading securities	14	14
Net (increase) decrease in loans held-for-sale	(10)	9
Net decrease in accrued income receivable	2	12
Net decrease in accrued expenses	1	16
Other, net	174	215
Discontinued operations, net		17
Net cash provided by operating activities	756	995
INVESTING ACTIVITIES		
Proceeds from maturities and redemptions of investment securities available-for-sale	1,757	1,397
Proceeds from sales of investment securities available-for-sale	773	149
Purchases of investment securities available-for-sale	(3,007)	(775)
Proceeds from sales of indirect private equity and venture capital funds	33	
Net decrease in loans	819	1,350
Net increase in fixed assets	(92)	(65)
Net decrease (increase) in customers liability on acceptances outstanding	1	(2)
Cash and cash equivalents acquired in acquisition of Sterling Bancshares, Inc.	721	
Sales of Federal Home Loan Bank stock	33	123
Net cash provided by investing activities	1,038	2,177
FINANCING ACTIVITIES		
Net increase in deposits	2,898	917
Net increase (decrease) in short-term borrowings	12	(283)
Net increase (decrease) in acceptances outstanding	(1)	2
Proceeds from issuance of medium- and long-term debt		298
Repayments of medium- and long-term debt	(1,464)	(2,101)
Redemption of medium- and long-term debt		(2,165)
Proceeds from issuance of common stock		849
Redemption of preferred stock		(2,250)
Proceeds from issuance of common stock under employee stock plans	3	4
Excess tax benefits from share-based compensation arrangements	1	1
Purchase of common stock for treasury	(75)	(4)

Dividends paid on common stock		(53)		(25)
Dividends paid on preferred stock				(38)
Net cash provided by (used in) financing activities		1,321		(4,795)
Net increase (decrease) in cash and cash equivalents		3,115		(1,623)
Cash and cash equivalents at beginning of period		2,083		5,617
Cash and cash equivalents at end of period	$	5,198	$	3,994
Interest paid	$	113	$	180
Income taxes, tax deposits and tax-related interest paid	$	48	$	48
Noncash investing and financing activities:				
Loans transferred to other real estate	$	41	$	83
Net noncash assets acquired in stock acquisition of Sterling Bancshares, Inc.		82		

See notes to consolidated financial statements.

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Notes to Consolidated Financial Statements (unaudited)

Comerica Incorporated and Subsidiaries

NOTE 1   BASIS OF PRESENTATION AND ACCOUNTING POLICIES

The accompanying unaudited consolidated financial statements were prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, the statements do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation were included. The results of operations for the nine months ended September 30, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011. Certain items in prior periods were reclassified to conform to the current presentation. For further information, refer to the consolidated financial statements and footnotes thereto included in the Annual Report of Comerica Incorporated and Subsidiaries (the Corporation) on Form 10-K for the year ended December 31, 2010.

Recently Adopted Accounting Pronouncements

In the third quarter 2011, the Corporation adopted Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2011-02, Receivables (Topic 310): A Creditor s Determination of Whether a Restructuring is a Troubled Debt Restructuring, (ASU 2011-02), which clarifies existing guidance used by creditors to determine when a modification represents a troubled debt restructuring (TDR). As a result, the Corporation reassessed loan restructurings that occurred on or after January 1, 2011 to identify modifications that would be considered TDRs as a result of these clarifications. The Corporation identified additional TDRs of $9 million as a result of the reassessment. Impairment on these loans was previously measured as part of a homogeneous pool of loans with similar risk characteristics. Since these modifications are considered TDRs, specific allowances were established for these loans based on an individual assessment of impairment. The additional allowance associated with these loans was $1 million, compared to the allowance previously measured as part of a homogeneous pool of loans. At September 30, 2011, the allowance for credit losses associated with these loan balances was $4 million.

Pending Accounting Pronouncements

In September 2011, the FASB issued ASU No. 2011-08, Intangibles Goodwill and Other (Topic 350): Testing Goodwill for Impairment, (ASU 2011-08). The Corporation will adopt ASU 2011-08, which allows companies to use a qualitative approach to test goodwill for impairment, in its consolidated financial statements for the year ended December 30, 2011. The provisions of ASU 2011-08 give companies the option to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining the need to perform step one of the annual test for goodwill impairment. The adoption of ASU 2011-08 will not have any effect on the Corporation s financial condition and results of operations.

In June 2011, the FASB issued ASU No. 2011-05, Comprehensive Income (Topic 220): Presentation of Comprehensive Income, (ASU 2011-05). The Corporation will adopt ASU 2011-05, which revises the presentation of comprehensive income in the financial statements, in the first quarter 2012. The provisions of ASU 2011-05 give companies the option to present total comprehensive income, components of net income, and components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. While the provisions of ASU 2011-05 will amend the presentation of comprehensive income, the adoption of ASU 2011-05 will not have any effect on the Corporation s financial condition and results of operations.

In May 2011, the FASB issued ASU No. 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs, (ASU 2011-04). The Corporation will adopt ASU 2011-04, which generally aligns the principles of fair value measurements with International Financial Reporting Standards (IFRSs), in the first quarter 2012. The provisions of ASU 2011-04 clarify the application of existing fair value measurement requirements, and expand the disclosure requirements for fair value measurements. While the provisions of ASU 2011-04 will increase the Corporation s fair value disclosures the Corporation does not expect the adoption of ASU 2011-04 to have any effect on the Corporation s financial condition and results of operations.

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Notes to Consolidated Financial Statements (unaudited)

Comerica Incorporated and Subsidiaries

NOTE 2 ACQUISITION

On July 28, 2011 (the acquisition date), the Corporation acquired all the outstanding common stock of Sterling Bancshares, Inc. (Sterling), a bank holding company headquartered in Houston, Texas, in a stock-for-stock transaction. Sterling common shareholders and holders of outstanding Sterling phantom stock units received 0.2365 shares of the Corporation s common stock in exchange for each share of Sterling common stock or phantom stock unit. As a result, the Corporation issued approximately 24 million common shares with an acquisition date fair value of $793 million, based on the Corporation s closing stock price of $32.67 on July 27, 2011. Based on the merger agreement, outstanding and unexercised options to purchase Sterling common stock were converted into fully vested options to purchase common stock of the Corporation. In addition, outstanding warrants to purchase Sterling common stock were converted into warrants to purchase common stock of the Corporation. Including an insignificant amount of cash paid in lieu of fractional shares, the fair value of total consideration paid was $803 million. The acquisition of Sterling significantly expands the Corporation s presence in Texas, particularly in the Houston and San Antonio areas, and gives the Corporation the ability to leverage additional marketing capacity to offer a wide array of products through a larger distribution network, particularly to middle market and small business companies.

The assets and liabilities of Sterling were recorded on the consolidated balance sheet at estimated fair value on the acquisition date. The purchase price allocation may change as additional information becomes available and additional analyses are completed. The following table presents the amounts recorded on the consolidated balance sheet on the acquisition date.

(dollar amounts in millions)	Initial Allocation
Fair value of consideration paid:	
Common stock issued (24,283,711 shares)	$ 793
Warrants issued	7
Stock options issued	3
Total consideration paid	803
Fair value of identifiable assets acquired:	
Cash and cash equivalents	721
Investment securities available-for-sale	1,492
Total loans	2,093
Premises and equipment	34
Core deposit intangible	34
Accrued income and other assets	304
Total identifiable assets acquired	4,678
Fair value of liabilities assumed:	
Deposits	4,029
Short-term borrowings	22
Medium- and long-term debt	262
Accrued expenses and other liabilities	47
Total liabilities assumed	4,360
Fair value of net identifiable assets acquired	318

Goodwill resulting from acquisition	$	485

Initial goodwill of $485 million was recorded after adjusting for the fair value of net identifiable assets acquired. The goodwill resulting from the acquisition represents the inherent long-term value expected from the business opportunities created from combining Sterling with the Corporation. None of the goodwill recognized will be deductible for income tax purposes. For further information regarding goodwill, refer to Note 6 to these unaudited consolidated financial statements.

The core deposit intangible is being amortized on an accelerated basis over the estimated life, currently expected to be approximately 10 years.

Notes to Consolidated Financial Statements (unaudited)

Comerica Incorporated and Subsidiaries

NOTE 2 ACQUISITION (continued)

The results of operations acquired in the Sterling transaction have been included in the Corporation s financial results since July 28, 2011. The following table discloses the impact of Sterling (excluding the impact of acquisition-related expenses discussed below) since the acquisition date through the period ended September 30, 2011. The table also presents pro forma results had the acquisition taken place on January 1, 2010. The pro forma financial information combines the historical results of Sterling and the Corporation and includes the estimated impact of purchase accounting adjustments. The pro forma includes adjustments to give effect to purchase accounting adjustments and changes in Sterling s financial structure resulting from the acquisition as if they had occurred on January 1, 2010, including estimated accretion of the purchase discount on the loan portfolio and related adjustments to Sterling s provision for loan losses for the impact of the pro forma remaining purchase discounts on the estimate of probable loss in the loan portfolio. Accretion estimates were based on the acquisition date purchase discount on the loan portfolio, as it was not practicable to determine the amount of discount that would have been recorded based on economic conditions that existed on January 1, 2010. The pro forma results are not indicative of what would have occurred had the acquisition taken place on the indicated date. Additionally, expected operating cost savings as a result of the acquisition are not reflected in the pro forma results, and acquisition-related expenses are included in the 2011 period in which they were incurred.

	Sterling Actual from Acquisition Date through September 30,	Pro Forma Combined Nine Months Ended September 30,	
(in millions)	2011	2011	2010
Total revenue (a)	$ 64	$ 1,930	$ 2,038
Net income	30	281	213

(a) Net interest income and noninterest income.

The Corporation committed to a restructuring plan in connection with the completion of the acquisition of Sterling. The restructuring plan, which is expected to be substantially completed by December 31, 2012, is intended to streamline operations across the combined organization. The restructuring plan is expected to result in cumulative costs of approximately $125 million ($80 million, after-tax) through the end of the plan, primarily encompassing facilities and contract termination charges, systems integration and related charges, severance and other employee-related charges, and transaction-related costs. The Corporation recognized acquisition-related expenses of $33 million and $38 million ($21 million and $24 million after-tax, respectively) for the three- and nine-month periods ended September 30, 2011, respectively, recorded in merger and restructuring charges in the consolidated statements of income. Merger and restructuring charges include the incremental costs to integrate the operations of Sterling and do not reflect the costs of the fully integrated combined organization. Merger and restructuring charges comprised the following for the three- and nine-month periods ended September 30, 2011.

		Total Incurred To-Date	
(in millions)	Total Expected Per Plan	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2011
Facilities and contract termination charges	$ 57	$	$
Systems integration and related charges	32	10	14
Severance and other employee-related charges	28	17	17
Transaction costs	8	6	7

Total merger and restructuring charges	$ 125	$ 33	$ 38

The following table presents the changes in restructuring reserves for the three- and nine- month periods ended September 30, 2011.

(in millions)	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2011
Balance at beginning of period	$	$
Merger and restructuring charges	33	38
Payments	(24)	(29)
Balance at September 30, 2011	$ 9	$ 9

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Notes to Consolidated Financial Statements (unaudited)

Comerica Incorporated and Subsidiaries

NOTE 2 ACQUISITION (continued)

In connection with the acquisition of Sterling, the Corporation acquired loans both with and without evidence of credit quality deterioration since origination. The acquired loans were initially recorded at fair value with no carryover of any allowance for loan losses. The Corporation reviewed the loans with evidence of credit quality deterioration at acquisition to determine if it was probable that the Corporation would not be able to collect all contractual amounts due, including both principal and interest. When both conditions existed, such loans were accounted for as purchased credit-impaired (PCI). The Corporation aggregated the acquired PCI loans into pools of loans based on common risk characteristics.

The Corporation estimated the total cash flows expected to be collected from the pools of acquired PCI loans, which included undiscounted expected principal and interest, using credit risk, interest rate and prepayment risk models that incorporated management s best estimate of current key assumptions such as default rates, loss severity and payment speeds. The excess of the undiscounted total cash flows expected to be collected over the fair value of the related PCI loans represents the accretable yield, which is recognized as interest income on a level-yield basis over the life of the related loan pools. The difference between the undiscounted contractual principal and interest and the undiscounted total cash flows expected to be collected is the nonaccretable difference, which reflects the impact of estimated credit losses and other factors. Subsequent increases in expected cash flows will result in a recovery of any previously recorded allowance for loan losses, to the extent applicable, and a reclassification from nonaccretable difference to accretable yield, which is recognized prospectively over the then remaining lives of the loan pools. Subsequent decreases in expected cash flows will result in an impairment charge to the provision for loan losses, resulting in an addition to the allowance for loan losses, and a reclassification from accretable yield to nonaccretable difference. A loan disposal, which may include a loan sale, receipt of payment in full from the borrower or foreclosure, results in removal of the loan from the acquired PCI loan pool at its allocated carrying amount. Refinanced or restructured loans remain within the acquired PCI loan pools.

The acquired PCI loan portfolio was accounted for at fair value at acquisition date as follows.

(in millions)		Acquired PCI Loans
Contractually required principal and interest (a)	$	328
Contractual cash flows not expected to be collected (nonaccretable difference)		176
Expected cash flows		152
Interest component of expected cash flows (accretable yield)		24
Fair value at acquisition	$	128

(a) Excludes loans fully charged off prior to acquisition date with no expectation of future cash flows.

The carrying amount and the related outstanding balance of acquired PCI loans included in the consolidated balance sheets at September 30, 2011 were as follows. The outstanding balance represents the total amount owed as of September 30, 2011, including accrued but unpaid interest and any amounts previously charged off. No allowance for loan losses was required on any of the acquired PCI loan pools at September 30, 2011.

(in millions)	September 30, 2011
Acquired PCI loans:	
Carrying amount	$ 113
Outstanding balance	262

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Notes to Consolidated Financial Statements (unaudited)

Comerica Incorporated and Subsidiaries

NOTE 2 ACQUISITION (continued)

Changes in the accretable yield for acquired PCI loans for the three- and nine-months ended September 30, 2011 were as follows.

(in millions)	Three and Nine Months Ended September 30, 2011
Balance at beginning of period	$
Additions	24
Disposals of loans	(1)
Accretion	(1)
Balance at September 30, 2011	$ 22

For acquired loans not deemed credit-impaired at acquisition, the differences between the initial fair value and the unpaid principal balance are recognized as interest income on a level-yield basis over the lives of the related loans. Subsequent to acquisition date, methods utilized to estimate the required allowance for loan losses for these loans is similar to originated loans; however, the estimate of loss is based on the unpaid principal balance less the remaining purchase discount. As such, a provision for loan losses will be recorded only to the extent that the estimated loss exceeds any remaining purchase discounts.

Information regarding acquired loans not deemed credit-impaired at acquisition date was as follows.

(in millions)	Nonimpaired Loans
Contractually required principal and interest	$ 2,465
Contractual cash flows not expected to be collected	208
Fair value at acquisition	1,965

The following table summarizes changes in the purchase discount for acquired loans not deemed credit-impaired at acquisition for the three- and nine-month periods ended September 30, 2011.

(in millions)	Three and Nine Months Ended September 30, 2011
Balance at beginning of period	$
Additions	148
Accretion	(26)
Balance at September 30, 2011	$ 122

NOTE 3 FAIR VALUE MEASUREMENTS

The Corporation utilizes fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. The determination of fair values of financial instruments often requires the use of estimates. In cases where quoted market values in an active market are not available, the Corporation uses present value techniques and other valuation methods to estimate the fair values of its financial instruments. These valuation methods require considerable judgment and the resulting estimates of fair value can be significantly affected by the assumptions made and methods used.

Fair value is an estimate of the exchange price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (i.e., not a forced transaction, such as a liquidation or distressed sale) between market participants at the measurement date. However, fair value estimates in many instances cannot be substantiated by comparison to independent markets and, in many cases, may not be realizable in a current sale of the financial instrument.

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Notes to Consolidated Financial Statements (unaudited)

Comerica Incorporated and Subsidiaries

NOTE 3 FAIR VALUE MEASUREMENTS (continued)

Trading securities, investment securities available-for-sale, derivatives and deferred compensation plan liabilities are recorded at fair value on a recurring basis. Additionally, from time to time, the Corporation may be required to record other assets and liabilities at fair value on a nonrecurring basis, such as impaired loans, other real estate (primarily foreclosed property), nonmarketable equity securities and certain other assets and liabilities. These nonrecurring fair value adjustments typically involve write-downs of individual assets or application of lower of cost or fair value accounting.

The Corporation categorizes assets and liabilities recorded at fair value into a three-level hierarchy, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1	Valuation is based upon quoted prices for identical instruments traded in active markets.
Level 2	Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
Level 3	Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

Following is a description of the valuation methodologies and key inputs used to measure financial assets and liabilities recorded at fair value, as well as a description of the methods and significant assumptions used to estimate fair value disclosures for financial instruments not recorded at fair value in their entirety on a recurring basis. For financial assets and liabilities recorded at fair value, the description includes the level of the fair value hierarchy in which the assets or liabilities are classified. Transfers of assets or liabilities between levels of the fair value hierarchy are recognized at the beginning of the reporting period, when applicable.

Cash and due from banks, federal funds sold and securities purchased under agreements to resell, and interest-bearing deposits with banks

Due to the short-term nature, the carrying amount of these instruments approximates the estimated fair value.

Trading securities and associated deferred compensation plan liabilities

Securities held for trading purposes and associated deferred compensation plan liabilities are recorded at fair value and included in other short-term investments and accrued expenses and other liabilities, respectively, on the consolidated balance sheets. Level 1 securities held for trading purposes include assets related to employee deferred compensation plans, which are invested in mutual funds, U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets and other securities traded on an active exchange, such as the New York Stock Exchange. Deferred compensation plan liabilities represent the fair value of the obligation to the employee, which corresponds to the fair value of the invested assets. Level 2 trading securities include municipal bonds and mortgage-backed securities issued by U.S. government-sponsored entities and corporate debt securities. Securities classified as Level 3 include securities in less liquid markets and securities not rated by a credit agency. The methods used to value trading securities are the same as the methods used to value investment securities available-for-sale, discussed below.

Loans held-for-sale

Loans held-for-sale, included in other short-term investments on the consolidated balance sheets, are recorded at the lower of cost or fair value. The fair value of loans held-for-sale is based on what secondary markets are currently offering for portfolios with similar characteristics. As such, the Corporation classifies loans held-for-sale subjected to nonrecurring fair value adjustments as Level 2.

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Notes to Consolidated Financial Statements (unaudited)

Comerica Incorporated and Subsidiaries

NOTE 3 FAIR VALUE MEASUREMENTS (continued)

Investment securities available-for-sale

Investment securities available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available or the market is deemed to be inactive at the measurement date, an adjustment to the quoted prices may be necessary. In some circumstances, the Corporation may conclude that a change in valuation technique or the use of multiple valuation techniques may be appropriate to estimate an instrument s fair value. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets and money market funds. Level 2 securities include residential mortgage-backed securities issued by U.S. government-sponsored enterprises, corporate debt securities and state and municipal securities. The fair value of Level 2 securities was determined using quoted prices of securities with similar characteristics or pricing models based on observable market data inputs, primarily interest rates, spreads and prepayment information. Securities classified as Level 3, of which the substantial majority are auction-rate securities (ARS), represent securities in less liquid markets requiring significant management assumptions when determining fair value. Due to the lack of a robust secondary auction-rate securities market with active fair value indicators, fair value at September 30, 2011, December 31, 2010 and September 30, 2010 was determined using an income approach based on a discounted cash flow model utilizing two significant assumptions: discount rate (including a liquidity risk premium) and workout period. The discount rate was calculated using credit spreads of the underlying collateral or similar securities plus a liquidity risk premium. The liquidity risk premium was based on observed industry auction-rate securities valuations by third parties and incorporated the rate at which the various types of similar ARS had been redeemed or sold since acquisition in 2008. The workout period was based on an assessment of publicly available information on efforts to re-establish functioning markets for these securities and the Corporation s redemption experience. As of September 30, 2011, approximately 64 percent of the aggregate ARS par value had been redeemed or sold since acquisition at or above carrying value.

Loans

The Corporation does not record loans at fair value on a recurring basis. However, periodically, the Corporation records nonrecurring adjustments to the carrying value of loans based on fair value measurements. Loans for which it is probable that payment of interest or principal will not be made in accordance with the contractual terms of the original loan agreement are considered impaired. Impaired loans are reported as nonrecurring fair value measurements when an allowance is established based on the fair value of collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Corporation classifies the impaired loan as nonrecurring Level 2. When management determines that the fair value of the collateral requires additional adjustments, either as a result of non-current appraisal value or when there is no observable market price, the Corporation classifies the impaired loan as nonrecurring Level 3.

Business loans consist of commercial, real estate construction, commercial mortgage, lease financing and international loans. The estimated fair value for variable rate business loans that reprice frequently is based on carrying values adjusted for estimated credit losses and other adjustments that would be expected to be made by a market participant in an active market. The fair value for other business loans and retail loans are estimated using a discounted cash flow model that employs interest rates currently offered on the loans, adjusted by an amount for estimated credit losses and other adjustments that would be expected to be made by a market participant in an active market. The rates take into account the expected yield curve, as well as an adjustment for prepayment risk, when applicable.

Customers liability on acceptances outstanding and acceptances outstanding

The carrying amount of these instruments approximates the estimated fair value, due to their short-term nature.

Derivative assets and derivative liabilities

Derivative instruments held or issued for risk management or customer-initiated activities are traded in over-the-counter markets where quoted market prices are not readily available. Fair value for over-the-counter derivative instruments is measured using internally developed models that use primarily market observable inputs, such as yield curves and option volatilities. Included in the fair value of over-the-counter derivative instruments are credit valuation adjustments reflecting counterparty credit risk and credit risk of the Corporation. These adjustments are determined by applying a credit spread for the counterparty or the Corporation, as appropriate, to the total expected exposure of the derivative after considering collateral and other master netting arrangements. These adjustments, which are considered Level 3 inputs, are based on estimates of current credit spreads to evaluate the likelihood of default. The Corporation assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative

Notes to Consolidated Financial Statements (unaudited)

Comerica Incorporated and Subsidiaries

NOTE 3 FAIR VALUE MEASUREMENTS (continued)

positions and determined that the credit valuation adjustments were not significant to the overall valuation of its derivatives. As a result, the Corporation classified its over-the-counter derivative valuations in Level 2 of the fair value hierarchy. Examples of Level 2 derivative instruments are interest rate swaps and energy derivative and foreign exchange contracts.

The Corporation also holds a portfolio of warrants for generally nonmarketable equity securities. These warrants are primarily from high technology, non-public companies obtained as part of the loan origination process. Warrants which contain a net exercise provision or a non-contingent put right embedded in the warrant agreement are accounted for as derivatives and recorded at fair value using a Black-Scholes valuation model with five inputs: risk-free rate, expected life, volatility, exercise price, and the per share market value of the underlying company. The Corporation classifies warrants accounted for as derivatives as recurring Level 3.

The Corporation holds a derivative contract associated with the 2008 sale of its remaining ownership of Visa Inc. (Visa) Class B shares. Under the terms of the derivative contract, the Corporation will compensate the counterparty primarily for dilutive adjustments made to the conversion factor of the Visa Class B to Class A shares based on the ultimate outcome of litigation involving Visa. Conversely, the Corporation will be compensated by the counterparty for any increase in the conversion factor from anti-dilutive adjustments. The fair value of the derivative contract was based on unobservable inputs consisting of management s estimate of the litigation outcome, timing of litigation settlements and payments related to the derivative. The Corporation classifies the derivative liability as recurring Level 3.

Nonmarketable equity securities

The Corporation has a portfolio of indirect private equity and venture capital investments. These funds generally cannot be redeemed and the majority are not readily marketable. Distributions from these funds are received by the Corporation as a result of the liquidation of underlying investments of the funds and/or as income distributions. It is estimated that the underlying assets of the funds will be liquidated over a period of up to 15 years. The value of these investments is at risk to changes in equity markets, general economic conditions and a variety of other factors. The investments are accounted for on the cost or equity method and are individually reviewed for impairment on a quarterly basis by comparing the carrying value to the estimated fair value. These investments may be carried at fair value on a nonrecurring basis when they are deemed to be impaired and written down to fair value. For such investments, fair value measurement guidance permits the use of net asset value, provided the net asset value is calculated by the fund in compliance with fair value measurement guidance applicable to investment companies. Where there is not a readily determinable fair value, the Corporation estimates fair value for indirect private equity and venture capital investments based on the Corporation s percentage ownership in the net asset value of the entire fund, as reported by the fund, after indication that the fund adheres to applicable fair value measurement guidance. For those funds where the net asset value is not reported by the fund, the Corporation derives the fair value of the fund by estimating the fair value of each underlying investment in the fund. In addition to using qualitative information about each underlying investment, as provided by the fund, the Corporation gives consideration to information pertinent to the specific nature of the debt or equity investment, such as relevant market conditions, offering prices, operating results, financial conditions, exit strategy and other qualitative information, as available. The lack of an independent source to validate fair value estimates, including the impact of future capital calls and transfer restrictions, is an inherent limitation in the valuation process. Commitments to fund additional investments in nonmarketable equity securities recorded at fair value on a nonrecurring basis were insignificant at September 30, 2011 and $1 million at December 31, 2010.

The Corporation also holds restricted equity investments, primarily Federal Home Loan Bank (FHLB) and Federal Reserve Bank (FRB) stock. Restricted equity securities are not readily marketable and are recorded at cost (par value) and evaluated for impairment based on the ultimate recoverability of the par value. No significant observable market data for these instruments is available. The Corporation considers the profitability and asset quality of the issuer, dividend payment history and recent redemption experience, when determining the ultimate recoverability of the par value. The Corporation s investment in FHLB stock totaled $95 million and $128 million at September 30, 2011 and December 31, 2010, respectively, and its investment in FRB stock totaled $59 million at both September 30, 2011 and December 31, 2010. The Corporation believes its investments in FHLB and FRB stock are recoverable at par.

The Corporation classifies nonmarketable equity securities subjected to nonrecurring fair value adjustments as Level 3.

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Notes to Consolidated Financial Statements (unaudited)

Comerica Incorporated and Subsidiaries

NOTE 3 FAIR VALUE MEASUREMENTS (continued)

Other real estate

Other real estate is included in accrued income and other assets on the consolidated balance sheets and includes primarily foreclosed property. Foreclosed property is initially recorded at fair value, less costs to sell, at the date of foreclosure, establishing a new cost basis. Subsequently, foreclosed property is carried at the lower of cost or fair value, less costs to sell. Other real estate may be carried at fair value on a nonrecurring basis when fair value is less than cost. Fair value is based upon independent market prices, appraised value or management s estimate of the value. Foreclosed property carried at fair value based on an observable market price or a current appraised value is classified by the Corporation as nonrecurring Level 2. When management determines that the fair value of the foreclosed property requires additional adjustments, either as a result of a non-current appraisal or when there is no observable market price, the Corporation classifies the foreclosed property as nonrecurring Level 3.

Loan servicing rights

Loan servicing rights, included in accrued income and other assets on the consolidated balance sheets, are subject to impairment testing. A valuation model is used for impairment testing, which utilizes a discounted cash flow analysis using interest rates and prepayment speed assumptions currently quoted for comparable instruments and a discount rate determined by management. If the valuation model reflects a value less than the carrying value, loan servicing rights are adjusted to fair value through a valuation allowance as determined by the model. As such, the Corporation classifies loan servicing rights subjected to nonrecurring fair value adjustments as Level 3.

Deposit liabilities

The estimated fair value of checking, savings and certain money market deposit accounts is represented by the amounts payable on demand. The estimated fair value of term deposits is calculated by discounting the scheduled cash flows using the period-end rates offered on these instruments.

Short-term borrowings

The carrying amount of federal funds purchased, securities sold under agreements to repurchase and other short-term borrowings approximates the estimated fair value.

Medium- and long-term debt

The carrying value of variable-rate FHLB advances approximates the estimated fair value. The estimated fair value of the Corporation s remaining variable- and fixed-rate medium- and long-term debt is based on quoted market values. If quoted market values are not available, the estimated fair value is based on the market values of debt with similar characteristics.

Credit-related financial instruments

The estimated fair value of unused commitments to extend credit and standby and commercial letters of credit is represented by the estimated cost to terminate or otherwise settle the obligations with the counterparties. This amount is approximated by the fees currently charged to enter into similar arrangements, considering the remaining terms of the agreements and any changes in the credit quality of counterparties since the agreements were executed. This estimate of fair value does not take into account the significant value of the customer relationships and the future earnings potential involved in such arrangements as the Corporation does not believe that it would be practicable to estimate a representational fair value for these items.

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Comerica Incorporated and Subsidiaries

NOTE 3 FAIR VALUE MEASUREMENTS (continued)

Assets and Liabilities Recorded at Fair Value on a Recurring Basis

The following tables present the recorded amount of assets and liabilities measured at fair value on a recurring basis as of September 30, 2011 and December 31, 2010.

(in millions)	Total	Level 1	Level 2	Level 3
September 30, 2011				
Trading securities:				
Deferred compensation plan assets	$ 86	$ 86	$	$
State and municipal securities	18		17	1
Total trading securities	104	86	17	1
Investment securities available-for-sale:				
U.S. Treasury and other U.S. government agency securities	20	20		
Residential mortgage-backed securities (a)	9,135		9,135	
State and municipal securities (b)	23			23
Corporate debt securities:				
Auction-rate debt securities	1			1
Other corporate debt securities	45		45	
Equity and other non-debt securities:				
Auction-rate preferred securities	409			409
Money market and other mutual funds	99	99		
Total investment securities available-for-sale	9,732	119	9,180	433
Derivative assets:				
Interest rate contracts	633		633	
Energy derivative contracts	97		97	
Foreign exchange contracts	85		85	
Warrants	5			5
Total derivative assets	820		815	5
Total assets at fair value	$ 10,656	$ 205	$ 10,012	$ 439
Derivative liabilities:				
Interest rate contracts	$ 274	$	$ 274	$
Energy derivative contracts	97		97	
Foreign exchange contracts	68		68	
Other	1			1
Total derivative liabilities	440		439	1

Deferred compensation plan liabilities	86	86		
Total liabilities at fair value	$ 526	$ 86	$ 439	$ 1

(a) Residential mortgage-backed securities issued and/or guaranteed by U.S. government agencies or U.S. government-sponsored enterprises.
(b) Primarily auction-rate securities.

Notes to Consolidated Financial Statements (unaudited)

Comerica Incorporated and Subsidiaries

NOTE 3 FAIR VALUE MEASUREMENTS (continued)

(in millions)	Total	Level 1	Level 2	Level 3
December 31, 2010				
Trading securities:				
Deferred compensation plan assets	$ 86	$ 86	$	$
Residential mortgage-backed securities (a)	7		7	
Other government-sponsored enterprise securities	1		1	
State and municipal securities	19		19	
Corporate debt securities	4		4	
Other securities	1			1
Total trading securities	118	86	31	1
Investment securities available-for-sale:				
U.S. Treasury and other U.S. government agency securities	131	131		
Residential mortgage-backed securities (a)	6,709		6,709	
State and municipal securities (b)	39			39
Corporate debt securities:				
Auction-rate debt securities	1			1
Other corporate debt securities	26		25	1
Equity and other non-debt securities:				
Auction-rate preferred securities	570			570
Money market and other mutual funds	84	84		
Total investment securities available-for-sale	7,560	215	6,734	611
Derivative assets:				
Interest rate contracts	542		542	
Energy derivative contracts	103		103	
Foreign exchange contracts	51		51	
Warrants	7			7
Total derivative assets	703		696	7
Total assets at fair value	$ 8,381	$ 301	$ 7,461	$ 619
Derivative liabilities:				
Interest rate contracts	$ 249	$	$ 249	$
Energy derivative contracts	103		103	
Foreign exchange contracts	48		48	
Other	1			1
Total derivative liabilities	401		400	1
Deferred compensation plan liabilities	86	86		
Total liabilities at fair value	$ 487	$ 86	$ 400	$ 1

(a) Residential mortgage-backed securities issued and/or guaranteed by U.S. government agencies or U.S. government-sponsored enterprises.
(b) Primarily auction-rate securities.

There were no transfers of assets or liabilities recorded at fair value on a recurring basis into or out of Level 1, Level 2 and Level 3 fair value measurements during the three- and nine-month periods ended September 30, 2011 and 2010.

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Comerica Incorporated and Subsidiaries

NOTE 3 FAIR VALUE MEASUREMENTS (continued)

The following table summarizes the changes in Level 3 assets and liabilities measured at fair value on a recurring basis for the three- and nine-month periods ended September 30, 2011 and 2010.

		Net Realized/Unrealized Gains (Losses)						
		Recorded in Earnings		Recorded in Other Comprehensive Income				
(in millions)	Balance at Beginning of Period	Realized	Unrealized	(Pre-tax)	Purchases	Sales	Settlements	Balance at End of Period
Three months ended September 30, 2011								
Trading securities:								
State and municipal securities	$ 2	$	$	$	$ 1	$ (2)	$	$ 1
Investment securities available-for-sale:								
State and municipal securities (a)	26					(3)		23
Auction-rate debt securities	1							1
Other corporate debt securities	1						(1)	
Auction-rate preferred securities	437	2		8		(38)		409
Total investment securities available-for-sale	465	2		8		(41)	(1)	433
Derivative assets:								
Warrants	8	3	(1)			(5)		5
Derivative liabilities:								
Other	1	(1)					(1)	1
Three months ended September 30, 2010								
Trading securities:								
State and municipal securities	$ 3	$	$	$	$	$ (3)	$	$
Investment securities available-for-sale:								
State and municipal securities (a)	42	(1)				(3)		38
Auction-rate debt securities	52	1		2		(55)		
Other corporate debt securities	1							1
Auction-rate preferred securities	609	1		(11)		(15)		584
Total investment securities available-for-sale	704	1		(9)		(73)		623
Derivative assets:								
Warrants	7		(2)		1			6
Derivative liabilities:								
Other	2		(1)					3
Nine months ended September 30, 2011								
Trading securities:								
State and municipal securities	$	$	$	$	$ 3	$ (2)	$	$ 1

Other securities	1				(1)		
Total trading securities	1			3	(3)		1
Investment securities available-for-sale:							
State and municipal securities (a)	39				(16)		23
Auction-rate debt securities	1						1
Other corporate debt securities	1					(1)	
Auction-rate preferred securities	570	9	5		(175)		409