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COMMERCIAL BANKSHARES INC

Form 10-Q

May 13, 2002

U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended March 31, 2002

Commission File Number 00-22246

COMMERCIAL BANKSHARES, INC.

(Exact name of Registrant as specified in its charter)

FLORIDA

65-0050176

(State or other jurisdiction of
incorporation or organization)

(IRS Employer
Identification No.)

1550 S.W. 57th Avenue, Miami, Florida

33144

(Address of principal executive offices)

(Zip Code)

(305) 267-1200

(Registrant's Telephone Number, including area code)

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

Yes No

CLASS

OUTSTANDING AT May 13, 2002

COMMON STOCK, \$.08 PAR VALUE

3,616,252 SHARES

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TABLE OF CONTENTS

PART I	Item 1.	Financial Statements	1
	Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	7
	Item 3.	Quantitative and Qualitative Disclosures About Market Risk	9
PART II	Item 6.	Exhibits and Reports on Form 8-K	11

PART I - FINANCIAL INFORMATION

ITEM I - FINANCIAL STATEMENTS

COMMERCIAL BANKSHARES, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED BALANCE SHEETS
March 31, 2002 and December 31, 2001
(Dollars in thousands, except share data)

	3/31/2002	12/31/2001
	-----	-----
Assets:	(Unaudited)	
Cash and due from banks	\$ 21,145	\$ 21,420
Federal funds sold	42,200	46,780
	-----	-----
Total cash and cash equivalents	63,345	68,200
Investment securities available for sale, at fair value (cost of \$121,690 in 2002 and \$106,126 in 2001)	124,940	111,138
Investment securities held to maturity, at cost (fair value of \$43,309 in 2002 and \$25,332 in 2001)	43,088	24,664
Loans, net	345,735	346,251
Premises and equipment, net	12,584	12,554
Accrued interest receivable	3,081	2,790
Goodwill, net	253	253
Other assets	3,799	3,078
	-----	-----
Total assets	\$596,825	\$568,928
	=====	=====
Liabilities and stockholders' equity:		
Deposits:		
Demand	\$ 94,937	\$ 94,453
Interest-bearing checking	64,918	65,630
Money market accounts	52,174	51,958
Savings	26,200	24,896
Time	241,529	225,569

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Total deposits	479,758	462,506
Securities sold under agreements to repurchase	61,919	53,436
Accrued interest payable	606	633
Accounts payable and accrued liabilities	3,596	2,228
Total liabilities	545,879	518,803
Stockholders' equity:		
Common stock, \$.08 par value, 6,250,000 Authorized shares, 3,969,429 issued (3,962,440 in 2001)	316	316
Additional paid-in capital	44,138	44,041
Retained earnings	11,015	9,786
Accumulated other comprehensive income	2,214	2,686
Treasury stock, 353,921 shares (352,571 in 2001), at cost	(6,737)	(6,704)
Total stockholders' equity	50,946	50,125
Total liabilities and stockholders' equity	\$596,825	\$568,928

The accompanying notes are an integral part of these condensed consolidated financial statements

COMMERCIAL BANKSHARES, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
For the three months ended March 31, 2002 and 2001
(Dollars in thousands, except share data)
(Unaudited)

	2002	2001
Interest income:		
Interest and fees on loans	\$6,413	\$6,501
Interest on investment securities	2,174	2,636
Interest on federal funds sold	149	282
Total interest income	8,736	9,419
Interest expense:		
Interest on deposits	2,675	3,892
Interest on securities sold under agreements to repurchase	226	635
Total interest expense	2,901	4,527
Net interest income	5,835	4,892
Provision for loan losses	75	75

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Net interest income after provision	5,760	4,817
	-----	-----
Non-interest income:		
Service charges on deposit accounts	667	637
Other fees and service charges	141	123
Securities gains	40	-
	-----	-----
Total non-interest income	848	760
	-----	-----
Non-interest expense:		
Salaries and employee benefits	2,358	2,088
Occupancy	299	297
Data processing	313	241
Furniture and equipment	175	188
Insurance	80	53
Stationery and supplies	65	74
Telephone and fax	56	55
Administrative service charges	54	54
Amortization	-	41
Other	335	214
	-----	-----
Total non-interest expense	3,735	3,305
	-----	-----
Income before income taxes	2,873	2,272
Provision for income taxes	849	636
	-----	-----
Net income	\$2,024	\$1,636
	-----	-----
Earnings per common and common equivalent share:		
Basic	\$.56	\$.45
Diluted	\$.54	\$.44
Weighted average number of shares and common equivalent shares:		
Basic	3,612,581	3,602,311
Diluted	3,766,992	3,691,908

The accompanying notes are an integral part of these condensed consolidated financial statements

COMMERCIAL BANKSHARES, INC. AND SUBSIDIARY
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 For the three months ended March 31, 2002 and 2001
 (In thousands)
 (Unaudited)

	Three months ended	
	March 31,	
	2002	2001
	----	----
Net income	\$2,024	\$1,636
Other comprehensive income(loss), net of tax:		
Unrealized holding gains(losses) arising		

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during the period	(447)	1,064
Reclassification adjustment for gains realized in net income	(25)	-
Cumulative effect of a change in accounting principle	-	114
	-----	-----
Other comprehensive income(loss)	(472)	1,178
	-----	-----
Comprehensive income	\$1,552	\$2,814
	=====	=====

The accompanying notes are an integral part of these condensed consolidated financial statements

COMMERCIAL BANKSHARES, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
For the three months ended March 31, 2002 and 2001
(In thousands)
(Unaudited)

	2002	2001
	----	----
Cash flows from operating activities:		
Net income	\$ 2,024	\$ 1,636
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	75	75
Depreciation, amortization and accretion, net	192	229
Gain on sale of investment securities	(40)	-
Gain on sale of premises and equipment	(1)	-
Change in accrued interest receivable	(291)	304
Change in other assets	(721)	1,023
Change in accounts payable and accrued liabilities	1,610	(94)
Change in accrued interest payable	(27)	(38)
	-----	-----
Net cash provided by operating activities	2,821	3,135
	-----	-----
Cash flows from investing activities:		
Proceeds from maturities of investment securities held to maturity	2,522	1,318
Proceeds from maturities and sales of investment securities available for sale	10,041	31,605
Purchases of investment securities held to maturity	(21,287)	-
Purchases of investment securities available for sale	(24,259)	(16,723)
Net (increase) decrease in loans	441	(22,374)
Purchases of premises and equipment	(176)	(78)

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Sales of premises and equipment	1	-
	-----	-----
Net cash used in investing activities	(32,717)	(6,252)
	-----	-----
Cash flows from financing activities:		
Net change in deposits	17,252	19,358
Net change in securities sold under agreements to repurchase	8,483	2,819
Dividends paid	(758)	(720)
Proceeds from issuance of stock	97	38
Purchase of treasury stock	(33)	(4)
	-----	-----
Net cash provided by financing activities	25,041	21,491
	-----	-----
Increase (decrease) in cash and cash equivalents	(4,855)	18,374
Cash and cash equivalents at beginning of period	68,200	35,015
	-----	-----
Cash and cash equivalents at end of period	\$63,345	\$53,389
	=====	=====
Supplemental disclosures:		
Interest paid (net of amounts credited to deposit accounts)	\$ 440	\$ 715
	=====	=====
Income taxes paid	\$ 160	\$ 132
	=====	=====

The accompanying notes are an integral part of these condensed consolidated financial statements

COMMERCIAL BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. INTERIM FINANCIAL STATEMENTS

The accompanying unaudited condensed consolidated financial statements, which are for interim periods, do not include all disclosures provided in the annual consolidated financial statements. These financial statements and the footnotes thereto should be read in conjunction with the annual consolidated financial statements for the years ended December 31, 2001, 2000, and 1999 for Commercial Bankshares, Inc. (the "Company").

All material intercompany balances and transactions have been eliminated.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments necessary for a fair presentation of the financial statements. Those adjustments are of a normal recurring nature. The results of operations for the three month period ended March

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31, 2002, are not necessarily indicative of the results to be expected for the full year.

2. PER SHARE DATA

Earnings per share have been computed by dividing net income by the weighted average number of common shares (basic earnings per share) and by the weighted average number of common shares plus dilutive common share equivalents outstanding (diluted earnings per share). Common stock equivalents include the effect of all outstanding stock options, using the treasury stock method.

The following tables reconcile the weighted average shares used to calculate basic and diluted earnings per share (in thousands, except per share amounts):

Three Months Ended March 31, 2002			Three Months Ended March 31, 2001		
Income (Numerator)	Shares (Denominator)	Per-Share Amount	Income (Numerator)	Shares (Denominator)	Per-Share Amount
Basic EPS					
\$2,024	3,613	\$.56	\$1,636	3,602	\$.45
Effect of Dilutive Options					
-	154	(.02)	-	90	(.01)
Diluted EPS					
\$2,024	3,767	\$.54	\$1,636	3,692	\$.44
=====	=====	=====	=====	=====	=====

3. NEW ACCOUNTING PRONOUNCEMENTS

SFAS NO. 142: "Goodwill and Other Intangible Assets"

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets." This statement addresses how intangible assets that are acquired individually or with a group of other assets (but not those acquired in a business combination) should be accounted for in financial statements upon their acquisition. This statement also addresses how goodwill and other intangible assets should be accounted for after they have been initially recognized in the financial statements. Except for goodwill and intangible assets acquired after June 30, 2001, which are immediately subject to its provision, SFAS No. 142 is effective starting with fiscal years beginning after December 15, 2001.

The provisions of SFAS No. 142 no longer allow the amortization of goodwill, and certain intangible assets that have indefinite useful lives, and requires that impairment of goodwill on those assets be tested annually. In addition, SFAS No. 142 requires the following additional disclosures for goodwill and other intangible assets:

- Changes in the carrying amount of goodwill from period-to-

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- period;
- The carrying amount of goodwill by major intangible assets class, and
- The estimated intangible amortization for the next five years

The Company adopted SFAS No. 142 effective January 1, 2002. The Company did not incur impairment losses for goodwill resulting from a transitional impairment test. The Company expects that the elimination of goodwill amortization will positively impact pre-tax net income by approximately \$160,000 in 2002.

SFAS No. 144: "Accounting for the Impairment or Disposal of Long-Lived Assets"

In October 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS No. 144 is effective for fiscal years beginning after December 15, 2001 and was written to provide a single model for the disposal of long-lived assets. SFAS No. 144 supersedes SFAS No. 121 "Accounting for Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of" and the accounting and reporting provision of Accounting principles Board Opinion No. 30, "Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions." The Company adopted the provision of SFAS No. 144 effective January 1, 2002. The implementation of this statement has not had a material effect on the Company's financial position, results of operations or cash flows.

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

RESULTS OF OPERATIONS

The Company's net income reported for the quarter ended March 31, 2002, was \$2.02 million, a 23% increase over the quarter ended March 31, 2001 of \$1.64 million. Basic and diluted earnings per share were \$.56 and \$.54, respectively, for the first quarter of 2002, as compared to \$.45 and \$.44, respectively, for the first quarter of 2001.

The Company's first quarter tax-equivalent net interest income increased to \$6.11 million, from \$5.14 million in the corresponding quarter in 2001. The increase is due primarily to an increase in average earning assets of \$50 million and to a higher yielding asset mix in 2002. The net interest margin for the quarter ended March 31, 2002 was 4.58%. This compares to 4.25% for the quarter ended March 31, 2001. The net interest margin has been calculated on a tax-equivalent basis, which includes an adjustment for interest on tax-exempt securities.

Non-interest income for the first quarter of 2002 increased by \$88,000, or 12%, from the corresponding period of 2001. The increase for the first quarter of 2002 is primarily due to an

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increase in account activity charges of \$29,000 and a gain on sale of investments of \$40,000.

Salaries and employee benefits expense increased by \$270,000, or 13%, for the first quarter of 2002, from the corresponding period of 2001. The increase is attributable to normal payroll increases and increased benefit costs.

Data processing expense increased by \$72,000, or 30%, for the first quarter of 2002, as compared to the corresponding period in 2001. The increase is attributable to an increase in the number of accounts processed and to an increase in rates from the Company's service provider.

Company management continually reviews and evaluates the allowance for loan losses. In evaluating the adequacy of the allowance for loan losses, management considers the results of its methodology, along with other factors such as the amount of non-performing loans and the economic conditions affecting the Company's markets and customers. The allowance for loan losses was approximately \$4.66 million at March 31, 2002, as compared with \$4.64 million at December 31, 2001. For the three months ended March 31, 2002, the allowance for loan losses was increased by the provision for loan losses of \$75,000, and decreased by approximately \$61,000 in net charge-offs. For the three months ended March 31, 2001, the allowance was increased with a provision for loan losses of \$75,000 and decreased by approximately \$6,000 in net charge-offs. The allowance as a percentage of total loans has increased to 1.33% at March 31, 2002, from 1.32% at December 31, 2001. Based on the nature of the loan portfolio and prevailing economic factors, management believes that the current level of the allowance for loan losses is sufficient to absorb losses in the loan portfolio.

Approximately \$215 million, or 61% of total loans, was secured by nonresidential real estate, and \$74.7 million, or 21% of total loans, was secured by residential real estate as of March 31, 2002. Virtually all loans are within the Company's markets in Miami-Dade and Broward counties.

The Company had no non-accrual loans at March 31, 2002.

LIQUIDITY AND CAPITAL RESOURCES

The objective of liquidity management is to maintain cash flow requirements to meet immediate and ongoing future needs for loan demand, deposit withdrawals, maturing liabilities, and expenses. In evaluating actual and anticipated needs, management seeks to obtain funds at the most economical cost. Management believes that the level of liquidity is sufficient to meet future funding requirements.

For banks, liquidity represents the ability to meet both loan commitments and withdrawals of deposited funds. Funds to meet these needs can be obtained by converting liquid assets to cash or by attracting new deposits or other sources of funding. Many factors affect a bank's ability to meet liquidity needs. Commercial Bank of Florida's (the Bank) principal sources of funds are deposits, repurchase agreements, payments on loans,

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maturities and sales of investments. As an additional source of funds, the Bank has credit availability with the Federal Home Loan Bank amounting to \$89 million, and Federal Funds purchased lines available at correspondent banks amounting to \$13 million as of March 31, 2002.

The Bank's primary use of funds is to originate loans and purchase investment securities. The Bank purchased \$45.5 million of investment securities during the first three months of 2002. Funding for the above came primarily from increases in deposits of \$17.3 million, increases in securities sold under agreements to repurchase of \$8.5 million and increases from proceeds from maturities and sales of investment securities of \$12.6 million.

In accordance with risk-based capital guidelines issued by the Federal Reserve Board, the Company and the Bank are each required to maintain a minimum ratio of total capital to risk weighted assets of 8%. Additionally, all bank holding companies and member banks must maintain "core" or "Tier 1" capital of at least 3% of total assets ("leverage ratio"). Member banks operating at or near the 3% capital level are expected to have well diversified risks, including no undue interest rate risk exposure, excellent control systems, good earnings, high asset quality, high liquidity, and well managed on- and off-balance sheet activities, and in general be considered strong banking organizations with a composite 1 rating under the CAMELS rating system of banks. For all but the most highly rated banks meeting the above conditions, the minimum leverage ratio is to be 3% plus an additional 100 to 200 basis points. The Tier 1 Capital, Total Capital, and Leverage Ratios of the Company were 12.11%, 13.61%, and 8.08%, respectively, as of March 31, 2002.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

ASSET/LIABILITY MANAGEMENT AND INTEREST RATE RISK

Changes in interest rates can substantially impact the Company's long-term profitability and current income. An important part of management's efforts to maintain long-term profitability is the management of interest rate risk. The goal is to maximize net interest income within acceptable levels of interest rate risk and liquidity. Interest rate exposure is managed by monitoring the relationship between interest-earning assets and interest-bearing liabilities, focusing on the size, maturity or repricing date, rate of return and degree of risk. The Asset/Liability Management Committee of the Bank oversees the interest rate risk management and reviews the Bank's asset/liability structure on a quarterly basis.

The Bank uses interest rate sensitivity, or GAP analysis to monitor the amount and timing of balances exposed to changes in interest rates. The GAP analysis is not relied upon solely to determine future reactions to interest rate changes because it is presented at one point in time and could change significantly from day-to-day. Other methods such as simulation analysis are utilized in evaluating the Bank's interest rate risk position. The table presented below shows the Bank's GAP analysis at March

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31, 2002.

INTEREST RATE SENSITIVITY ANALYSIS
(Dollars in Thousands)

	Term to Repricing				Total
	90 Days or Less	91-181 Days	182-365 Days	Over 1 Year & Non-rate Sensitive	
Interest-earning assets:					
Federal funds sold	\$42,200	\$ -	\$ -	\$ -	\$ 42,200
Investment securities	21,254	11,413	28,118	104,204	164,989
Gross loans (excluding non-accrual)	81,287	31,676	62,690	175,411	351,064
Total interest-earning assets	\$144,741	\$43,089	\$90,808	\$279,615	\$558,253
Interest-bearing liabilities:					
Interest-bearing checking	\$ -	\$ -	\$ -	\$ 64,918	\$ 64,918
Money market	-	13,044	13,044	26,086	52,174
Savings	-	-	-	26,200	26,200
Time deposits	79,545	57,225	63,102	41,657	241,529
Borrowed funds	63,553	-	-	-	63,553
Total interest-bearing liabilities	\$143,098	\$70,269	\$76,146	\$158,861	\$448,374
Interest sensitivity gap	\$ 1,643	(\$27,180)	\$14,662	\$120,754	\$109,879
Cumulative gap	\$ 1,643	(\$25,537)	(\$10,875)	\$109,879	
Cumulative ratio of interest-earning assets to interest-bearing liabilities	101%	88%	96%	125%	
Cumulative gap as a percentage of total interest-earning assets	0.3%	(4.6%)	(1.9%)	19.7%	

Management's assumptions reflect the Bank's estimate of the anticipated repricing sensitivity of non-maturity deposit products. Interest-bearing checking and savings accounts have been allocated to the "over 1 year" category, and money market accounts 25% to the "91-181 days" category, 25% to the "182-365 days" category, and 50% to the "over 1 year" category.

The Bank uses simulation analysis to quantify the effects of various immediate parallel shifts in interest rates on net interest income over the next 12 month period. Such a "rate shock" analysis requires key assumptions which are inherently uncertain, such as deposit sensitivity, cash flows from investments and loans, reinvestment options, management's capital

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plans, market conditions, and the timing, magnitude and frequency of interest rate changes. As a result, the simulation is only a best-estimate and cannot accurately predict the impact of the future interest rate changes on net income. As of March 31, 2002, the Bank's simulation analysis projects an increase to net interest income of 5.25%, assuming an immediate parallel shift downward in interest rates by 200 basis points. If rates rise by 200 basis points, the simulation analysis projects net interest income would decrease by 4.22%. These projected levels are within the Bank's policy limits.

PART II - OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

All exhibits are omitted because they are not applicable.

(b) Reports on Form 8-K. No report on Form 8-K was filed During the quarter ended March 31, 2002.

SIGNATURES

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

Commercial Bankshares, Inc.

(Registrant)

/s/ Barbara E. Reed

Senior Vice President &
Chief Financial Officer

Date: May 13, 2002
