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SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

OMB APPROVAL  
OMB Number: 3235-0123  
Expires: October 31, 2004  
Estimated average burden  
hours per response . . . 12.00

SEC FILE NUMBER  
8 - 26318

**ANNUAL AUDITED REPORT  
FORM X-17A-5  
PART III**

REC'D S.E.C.  
APR 25 2003  
603

**FACING PAGE**

Information Required of Brokers and Dealers Pursuant to Section 17 of the  
Securities Exchange Act of 1934 and Rule 17a-5 Thereunder

REPORT FOR THE PERIOD BEGINNING 01 / 01 / 02 AND ENDING 12 / 31 / 02  
MM/DD/YY MM/DD/YY

**A. REGISTRANT IDENTIFICATION**

NAME OF BROKER-DEALER:

Commerce Capital Markets, Inc.

OFFICIAL USE ONLY

FIRM ID. NO.

ADDRESS OF PRINCIPAL PLACE OF BUSINESS: (Do not use P.O. Box No.)

2005 Market Street - Suite 200

Philadelphia

(No. and Street)  
Pennsylvania

19103

(City)

(State)

(Zip Code)

NAME AND TELEPHONE NUMBER OF PERSON TO CONTACT IN REGARD TO THIS REPORT

Terrence J. Malloy, Chief Financial Officer

(215) 282-4400

(Area Code - Telephone No.)

**B. ACCOUNTANT IDENTIFICATION**

INDEPENDENT PUBLIC ACCOUNTANT whose opinion is contained in this Report\*

Ernst & Young LLP

2001 Market Street

(Name - of individual, state last, first, middle name)

Philadelphia

Pennsylvania

19103

(Address)

(City)

(State)

(Zip Code)

CHECK ONE:

- Certified Public Accountant
- Public Accountant
- Accountant not resident in United States or any of its possessions.

**PROCESSED**  
MAY 01 2003

THOMSON  
FINANCIAL

FOR OFFICIAL USE ONLY

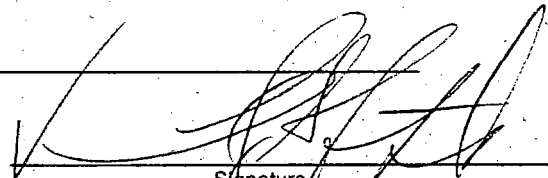
\*Claims for exemption from the requirement that the annual report be covered by the opinion of an independent public accountant must be supported by a statement of facts and circumstances relied on as the basis for the exemption. See section 240.17a-5(e)(2).

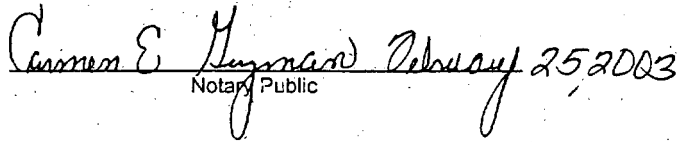
**OATH OR AFFIRMATION**

I, Vincent J. Stafford, swear (or affirm) that, to the best of my knowledge and belief the accompanying financial statements and supporting schedules pertaining to the firm of Commerce Capital Markets, Inc., as of December 31, 2002, are true and correct. I further swear (or affirm) that neither the company nor any partner, proprietor, principal officer or director has any proprietary interest in any account classified solely as that of a customer, except as follows:

\_\_\_\_\_  
\_\_\_\_\_

Notarial Seal  
Carmen E. Guzman, Notary Public  
Philadelphia, Philadelphia County  
My Commission Expires Feb. 26, 2005  
Member, Pennsylvania Association of Notaries

  
\_\_\_\_\_  
Signature  
**EVP / Chief Executive Officer**  
\_\_\_\_\_  
Title

  
\_\_\_\_\_  
Notary Public

- This report\*\* contains (check all applicable boxes):
- (a) Facing page.
  - (b) Statement of Financial Condition.
  - (c) Statement of Income (Loss).
  - (d) Statement of Changes in Financial Condition.
  - (e) Statement of Changes in Stockholders' Equity or Partners' or Sole Proprietor's Capital.
  - (f) Statement of Changes in Liabilities Subordinated to Claims or Creditors.
  - (g) Computation of Net Capital.
  - (h) Computation for Determination of Reserve Requirements Pursuant to Rule 15c3-3.
  - (i) Information Relating to the Possession or control Requirements Under Rule 15c3-3.
  - (j) A Reconciliation, including appropriate explanation, of the Computation of Net Capital Under Rule 15c3-1 and the Computation for Determination of the Reserve Requirements Under Exhibit A or Rule 15c3-3.
  - (k) A Reconciliation between the audited and unaudited Statements of Financial Condition with respect to methods of consolidation.
  - (l) An Oath or Affirmation.
  - (m) A copy of the SIPC Supplemental Report.
  - (n) A report describing any material inadequacies found to exist or found to have existed since the date of the previous audit.

\*\*For conditions of confidential treatment of certain portions of this filing, see section 240.17a-5(e)(3).

COMMERCE CAPITAL MARKETS, INC.

Statement of Financial Condition

December 31, 2002 with Report of Independent Auditors

Commerce Capital Markets, Inc.

Statement of Financial Condition

December 31, 2002

**Contents**

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## Report of Independent Auditors

The Board of Directors  
Commerce Capital Markets, Inc.

We have audited the accompanying statement of financial condition of Commerce Capital Markets, Inc. (the Company) as of December 31, 2002. This financial statement is the responsibility of the Company's management. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. 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 audit provides a reasonable basis for our opinion.

In our opinion, the statement of financial condition referred to above presents fairly, in all material respects, the financial position of Commerce Capital Markets, Inc. at December 31, 2002, in conformity with accounting principles generally accepted in the United States.

*Ernst + Young LLP*

February 14, 2003

Commerce Capital Markets, Inc.

Statement of Financial Condition

December 31, 2002

**Assets**

|   |                       |
|---|-----------------------|
| Cash  | \$ 4,067,992          |
| Cash segregated in compliance with federal and other regulations  | 100,000               |
| Receivable from customers   | 219,381               |
| Receivable from brokers and dealers   | 4,276,983             |
| Securities owned (at market value)  | 326,479,155           |
| Prepaid expenses  | 330,440               |
| Good faith deposits   | 414,280               |
| Accrued income receivable   | 897,732               |
| Accrued interest receivable   | 2,449,360             |
| Furniture, equipment, and leasehold improvements, at cost (net of accumulated depreciation and amortization of \$2,246,579) | 3,099,085             |
| Other assets  | 324,544               |
| Total assets  | <u>\$ 342,658,952</u> |

**Liabilities and stockholder's equity**

Liabilities:

|                                |                   |
|--------------------------------|-------------------|
| Payable to brokers and dealers | \$ 15,379,021     |
| Payable to customers           | 494,385           |
| Accrued expenses               | 4,522,650         |
| Other liabilities              | 2,093,176         |
| Total liabilities              | <u>22,489,232</u> |

Stockholder's equity:

|  |                       |
|--|-----------------------|
| Common stock—authorized 10,000 shares; issued 4,684 shares, no par or stated value | 259,559               |
| Additional capital   | 292,390,095           |
| Retained earnings  | 27,520,066            |
| Total stockholder's equity   | <u>320,169,720</u>    |
| Total liabilities and stockholder's equity   | <u>\$ 342,658,952</u> |

*See accompanying notes.*

# Commerce Capital Markets, Inc.

## Notes to Statement of Financial Condition

December 31, 2002

### 1. Organization

Commerce Capital Markets, Inc. (the Company), an operating subsidiary of Commerce Bank, N.A. (CBNA), is a registered broker-dealer in securities under the Securities Exchange Act of 1934 and is a member of the National Association of Securities Dealers, Inc. CBNA is a wholly-owned subsidiary of Commerce Bancorp, Inc. (Bancorp), a multibank holding company headquartered in Cherry Hill, New Jersey.

The Company primarily underwrites and trades in state and municipal securities. The Company also provides corporate and municipal finance services, including private placements and financial advisory services for its customers and the customers of the Parent. The Company also acts as agent for affiliates of the Parent and others in certain securities transactions.

### 2. Significant Accounting Policies

Significant accounting policies are summarized as follows:

#### Securities Transactions

Security transactions are accounted for on a trade-date basis with the resulting receivables and payables classified as amounts due to or from pending transactions.

Securities owned consist primarily of state and municipal obligations which are valued at fair value. The fair value of securities owned is based primarily on quoted market prices, dealer quotes, and prices obtained from independent third parties.

#### Income Taxes

The Company is included in the consolidated federal income tax return filed by Bancorp. In accordance with the tax allocation policy of the consolidated group, the Company determines its federal income tax liability on a separate-return basis and makes the required tax payments to Bancorp.

Deferred income taxes have been provided for the effects of temporary differences between financial reporting and tax bases of assets and liabilities and have been measured using the enacted marginal tax rates and laws that are currently in effect. The deferred tax liability is recorded in other liabilities on the Statement of Financial Condition.

## Commerce Capital Markets, Inc.

### Notes to Statement of Financial Condition (continued)

#### 2. Significant Accounting Policies (continued)

##### Furniture, Equipment, and Leasehold Improvements

All furniture, equipment, and leasehold improvements are recorded at cost and are depreciated on a straight-line basis over the estimated useful lives of the assets. Leasehold improvements are amortized using the straight-line method over the shorter of the lease term or useful life.

##### Financial Instruments

Short-term receivables are recorded at contracted amounts approximating fair value.

Derivative financial instruments used to offset the market risk associated with trading instruments include futures and options and are carried at market value which is based on quoted market prices. Fair values of option contracts and futures transactions, as well as cash maintained in a related brokerage account, are recorded as receivable from and payable to brokers and dealers.

##### Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates.

#### 3. Receivable from and Payable to Brokers and Dealers

Amounts receivable from and payable to brokers and dealers at December 31, 2002, consist of the following:

|                                      | Receivable          | Payable              |
|--------------------------------------|---------------------|----------------------|
| Securities failed-to-deliver/receive | \$ 1,056,183        | \$ —                 |
| Unsettled trades                     | —                   | 14,999,117           |
| Derivative financial instruments     | 3,220,800           | —                    |
| Other                                | —                   | 379,904              |
|                                      | <u>\$ 4,276,983</u> | <u>\$ 15,379,021</u> |



## Commerce Capital Markets, Inc.

### Notes to Statement of Financial Condition (continued)

#### 4. Receivable from and Payable to Customers

Accounts receivable from and payable to customers include amounts due on cash transactions. Securities owned by customers are held as collateral for receivables. Such collateral is not reflected in the financial statements.

The Company clears certain of its customer transactions through another broker-dealer on a fully disclosed basis.

#### 5. Securities Owned

At December 31, 2002, securities owned by the Company are comprised of the following:

|                           | <u>Fair Value</u>     |
|---------------------------|-----------------------|
| State and municipal bonds | \$ 289,523,200        |
| State and municipal notes | 36,955,955            |
|                           | <u>\$ 326,479,155</u> |

#### 6. Short-Term Bank Loan

The Company has a \$10 million line of credit with Deutsche Bank used to facilitate the securities settlement process. This loan is a demand obligation and bears interest at the federal funds rate plus 75 basis points. There were no borrowings outstanding against this line of credit at December 31, 2002.

#### 7. Net Capital Requirements

Pursuant to the Uniform Net Capital Rule (Rule 15c3-1) of the Securities and Exchange Commission, the Company is required to maintain minimum net capital, as defined under such provisions. The rule requires it maintain minimum net capital equal to the greater of \$250,000 or 6-2/3% of aggregate indebtedness, as defined. At December 31, 2002, the Company's net capital was \$58,505,243 which was \$58,022,221 in excess of net capital requirements. The Company's ratio of aggregate indebtedness to net capital was .12 to 1.

## Commerce Capital Markets, Inc.

### Notes to Statement of Financial Condition (continued)

#### 8. Lease Commitments

The Company leases two branch offices under noncancelable operating leases expiring at various dates through 2003.

The Company leases its main office space from Bancorp. Minimum rental commitments associated with this lease are included in the table below.

At December 31, 2002, minimum rental commitments under all noncancelable leases were as follows:

| <u>Year ended December 31</u> | <u>Total</u>        | <u>Bancorp</u>      | <u>Third Party</u> |
|-------------------------------|---------------------|---------------------|--------------------|
| 2003                          | \$ 515,000          | \$ 425,000          | \$ 90,000          |
| 2004                          | 458,000             | 458,000             | --                 |
| 2005                          | 464,000             | 464,000             | --                 |
| 2006                          | 464,000             | 464,000             | --                 |
| 2007                          | 77,000              | 77,000              | --                 |
| Thereafter                    | --                  | --                  | --                 |
| Total                         | <u>\$ 1,978,000</u> | <u>\$ 1,888,000</u> | <u>\$ 90,000</u>   |

#### 9. Derivative Financial Instruments and Concentrations of Credit Risk

As part of its broker-dealer activities, the Company maintains an inventory of securities for distribution to its customers in order to meet those customers' needs. In order to reduce the exposure to market risk relating to the inventory, the Company buys and sells a variety of derivative financial instruments including futures and option contracts. Market risk includes changes in interest rates or value fluctuations in the underlying financial instruments. The Company's hedging strategy is to offset the market risk associated with its inventory through the buying and selling of futures and option contracts. The Company regularly sells financial future contracts not yet purchased (short sales) to offset the market risk associated in the inventory. Short positions may expose the Company to market risk in the event prices increase as the Company may be obligated to acquire the future contracts at prevailing market prices. The Company uses notional (contract) amounts to measure derivative activity. Notional amounts are not included on the statement of financial condition, as those amounts are not actually paid or

Commerce Capital Markets, Inc.

Notes to Statement of Financial Condition (continued)

**9. Derivative Financial Instruments and Concentrations of Credit Risk (continued)**

received at settlement. The following table reflects the open commitments for futures and options and the associated unrealized gains (losses) as of December 31, 2002:

| Commitments                | Net Contracts               |    | Notional Amount |                  | Unrealized<br>Gain (Loss) |
|----------------------------|-----------------------------|----|-----------------|------------------|---------------------------|
|                            | Outstanding<br>Long/(Short) |    | Long            | (Short)          |                           |
| Municipal bond futures     | 365                         | \$ | 36,500,000      | \$ -             | \$ 278,561                |
| Treasury bond futures      | (600)                       |    | 10,000,000      | (70,000,000)     | (2,537,224)               |
| Treasury bond put options  | (450)                       |    | 45,000,000      | -                | (22,919)                  |
| Treasury bond call options | (1,050)                     |    | -               | (105,000,000)    | (1,341,966)               |
| Total commitments          | (1,735)                     | \$ | 91,500,000      | \$ (175,000,000) | \$ (3,623,548)            |

The average notional amount for futures and options contracts for the year ended December 31, 2002 was \$106.7 million.

The notional amounts of derivative financial instruments do not represent the potential risk from counterparty nonperformance. Transactions in derivative financial instruments are conducted through regulated exchanges, which guarantee performance of counterparties, and settle in cash on a daily basis. The Company believes these factors minimize credit risk.

The Company's business involves the participation in underwriting activities primarily with public entities in and contiguous to the Commonwealth of Pennsylvania. As part of this activity, the Company executes commitments to acquire securities and execute security sale transactions with customers. The Company is exposed to market risk if the value of the securities which the Company has committed to underwrite declines before the closing of the transaction. Credit risk is eliminated at a transaction closing at which time funds are exchanged for the underwritten securities.

## Commerce Capital Markets, Inc.

### Notes to Statement of Financial Condition (continued)

#### **9. Derivative Financial Instruments and Concentration of Credit Risk (continued)**

The Company is involved in investment banking and trading services to underwrite, sell, and make a market in high yield securities. High yield securities have been defined as debt securities which are nonrated or those rated by Standard and Poor's as BB+ and Moody's as BB or lower (or equivalent ratings for other instruments). These activities expose the Company to higher degrees of credit risk than that associated with investment-grade securities. As of December 31, 2002, the Company held nonrated securities with a combined market value of approximately \$78.7 million.

#### **10. Related Party Transactions**

Cash segregated in compliance with federal and other regulations was \$100,000 at December 31, 2002. Cash on deposit with the Parent was \$3,092,277 at December 31, 2002.

The financial condition may have been significantly different had the Company been autonomous.