

FIFTH THIRD BANCORP  
Form 10-Q  
August 03, 2006  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

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**FORM 10-Q**

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

**For the Quarterly Period Ended June 30, 2006**

**Commission File Number 0-8076**

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**FIFTH THIRD BANCORP**

(Exact name of Registrant as specified in its charter)

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**Ohio**  
(State or other jurisdiction of  
incorporation or organization)

**31-0854434**  
(I.R.S. Employer

Identification Number)

**Fifth Third Center**

**Cincinnati, Ohio 45263**

(Address of principal executive offices)

**Registrant's telephone number, including area code: (513) 534-5300**

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

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

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐

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

There were 557,894,188 shares of the Registrant's Common Stock, without par value, outstanding as of June 30, 2006.

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This report may contain forward-looking statements about the Registrant and/or the company as combined with acquired entities within the meaning of Sections 27A of the Securities Act of 1933, as amended, and Rule 175 promulgated thereunder, and 21E of the Securities Exchange Act of 1934, as amended, and Rule 3b-6 promulgated thereunder, that involve inherent risks and uncertainties. This report may contain certain forward-looking statements with respect to the financial condition, results of operations, plans, objectives, future performance and business of the Registrant and/or the combined company including statements preceded by, followed by or that include the words or phrases such as "believes," "expects," "anticipates," "plans," "trend," "objective," "continue," "remain" or similar expressions or future or conditional verbs such as "should," "could," "might," "can," "may" or similar expressions. There are a number of important factors that could cause future results to differ materially from historical performance and these forward-looking statements. Factors that might cause such a difference include, but are not limited to: (1) competitive pressures among depository institutions increase significantly; (2) changes in the interest rate environment reduce interest margins; (3) prepayment speeds, loan origination and sale volumes, charge-offs and loan loss provisions; (4) general economic conditions, either national or in the states in which the Registrant, one or more acquired entities and/or the combined company do business, are less favorable than expected; (5) political developments, wars or other hostilities may disrupt or increase volatility in securities markets or other economic conditions; (6) changes and trends in the securities markets; (7) legislative or regulatory changes or actions, or significant litigation, adversely affect the Registrant, one or more acquired entities and/or the combined company or the businesses in which the Registrant, one or more acquired entities and/or the combined company are engaged; (8) difficulties in combining the operations of acquired entities and (9) the impact of reputational risk created by the developments discussed above on such matters as business generation and retention, funding and liquidity. Additional information concerning factors that could cause actual results to differ materially from those expressed or implied in the forward-looking statements is available in the Registrant's Annual Report on Form 10-K for the year ended December 31, 2005, filed with the United States Securities and Exchange Commission (SEC). Copies of this filing are available at no cost on the SEC's Web site at [www.sec.gov](http://www.sec.gov) or on the Registrant's Web site at [www.53.com](http://www.53.com). The Registrant undertakes no obligation to release revisions to these forward-looking statements or

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reflect events or circumstances after the date of this report.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (Item 2)**

The following is management's discussion and analysis of certain significant factors that have affected Fifth Third Bancorp's (the Registrant or Fifth Third) financial condition and results of operations during the periods included in the Condensed Consolidated Financial Statements, which are a part of this filing. Reference to the Registrant incorporates the parent holding company and all consolidated subsidiaries.

**TABLE 1: Selected Financial Data**

| (\$ in millions, except per share data)                                                                | For the three months ended June 30, |         |                | For the six months ended June 30, |           |                |
|--------------------------------------------------------------------------------------------------------|-------------------------------------|---------|----------------|-----------------------------------|-----------|----------------|
|                                                                                                        | 2006                                | 2005    | Percent Change | 2006                              | 2005      | Percent Change |
| <b>Income Statement Data</b>                                                                           |                                     |         |                |                                   |           |                |
| Net interest income (a)                                                                                | \$ 716                              | 758     | (5)%           | \$ 1,434                          | 1,517     | (5)%           |
| Noninterest income                                                                                     | 655                                 | 635     | 3              | 1,272                             | 1,242     | 2              |
| Total revenue (a)                                                                                      | 1,371                               | 1,393   | (2)            | 2,706                             | 2,759     | (2)            |
| Provision for loan and lease losses                                                                    | 71                                  | 60      | 18             | 149                               | 127       | 17             |
| Noninterest expense                                                                                    | 759                                 | 728     | 4              | 1,490                             | 1,432     | 4              |
| Net income                                                                                             | 382                                 | 417     | (8)            | 746                               | 822       | (9)            |
| <b>Common Share Data</b>                                                                               |                                     |         |                |                                   |           |                |
| Earnings per share, basic                                                                              | \$ .69                              | .75     | (8)%           | \$ 1.34                           | 1.48      | (9)%           |
| Earnings per share, diluted                                                                            | .69                                 | .75     | (8)            | 1.34                              | 1.47      | (9)            |
| Cash dividends per common share                                                                        | .40                                 | .35     | 14             | .78                               | .70       | 11             |
| Book value per share                                                                                   | 17.13                               | 16.82   | 2              |                                   |           |                |
| Dividend payout ratio                                                                                  | 58.0%                               | 46.7    | 24             | 58.2%                             | 47.6      | 22             |
| <b>Financial Ratios</b>                                                                                |                                     |         |                |                                   |           |                |
| Return on average assets                                                                               | 1.45%                               | 1.63    | (11)%          | 1.43%                             | 1.63      | (12)%          |
| Return on average equity                                                                               | 16.0                                | 18.1    | (12)           | 15.7                              | 18.1      | (13)           |
| Average equity as a percent of average assets                                                          | 9.09                                | 8.98    | 1              | 9.13                              | 9.00      | 4              |
| Tangible equity                                                                                        | 6.92                                | 6.89    |                |                                   |           |                |
| Net interest margin (a)                                                                                | 3.01                                | 3.29    | (9)            | 3.04                              | 3.33      | (9)            |
| Efficiency (a)                                                                                         | 55.3                                | 52.2    | 6              | 55.0                              | 51.9      | 6              |
| <b>Credit Quality</b>                                                                                  |                                     |         |                |                                   |           |                |
| Net losses charged off                                                                                 | \$ 67                               | 55      | 22%            | \$ 140                            | 118       | 18%            |
| Net losses charged off as a percent of average loans and leases                                        | .37%                                | .34     | 9              | .40%                              | .37       | 8              |
| Allowance for loan and lease losses as a percent of loans and leases                                   | 1.04                                | 1.09    | (5)            |                                   |           |                |
| Allowance for credit losses as a percent of loans and leases (b)                                       | 1.14                                | 1.20    | (5)            |                                   |           |                |
| Nonperforming assets as a percent of loans, leases and other assets, including other real estate owned | .49                                 | .51     | (4)            |                                   |           |                |
| <b>Average Balances</b>                                                                                |                                     |         |                |                                   |           |                |
| Loans and leases, including held for sale                                                              | \$ 73,093                           | 66,762  | 9%             | \$ 72,367                         | \$ 65,924 | 10%            |
| Total securities and other short-term investments                                                      | 22,439                              | 25,716  | (13)           | 22,677                            | 25,916    | (12)           |
| Total assets                                                                                           | 105,741                             | 102,765 | 3              | 105,241                           | 101,891   | 3              |
| Transaction deposits                                                                                   | 49,282                              | 47,624  | 3              | 49,116                            | 47,603    | 3              |
| Core deposits                                                                                          | 59,731                              | 55,910  | 7              | 59,217                            | 55,641    | 6              |
| Wholesale funding                                                                                      | 32,903                              | 34,274  | (4)            | 33,013                            | 33,820    | (2)            |
| Shareholders' equity                                                                                   | 9,607                               | 9,224   | 4              | 9,604                             | 9,166     | 5              |

**Regulatory Capital Ratios**

|                          |              |       |     |
|--------------------------|--------------|-------|-----|
| Tier I capital           | <b>8.52%</b> | 8.48  | %   |
| Total risk-based capital | <b>10.45</b> | 10.80 | (3) |
| Tier I leverage          | <b>8.38</b>  | 7.76  | 8   |

(a) Amounts presented on a fully taxable equivalent basis.

(b) The allowance for credit losses is the sum of the allowance for loan and lease losses and the reserve for unfunded commitments.

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### **Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

#### **OVERVIEW**

This overview of management's discussion and analysis highlights selected information in the financial results of the Registrant and may not contain all of the information that is important to you. For a more complete understanding of trends, events, commitments, uncertainties, liquidity, capital resources and critical accounting policies and estimates, you should carefully read this entire document. Each of these items could have an impact on the Registrant's financial condition and results of operations.

The Registrant is a diversified financial services company headquartered in Cincinnati, Ohio. At June 30, 2006, the Registrant had \$106.1 billion in assets, operated 19 affiliates with 1,138 full-service Banking Centers including 116 Bank Mart® locations open seven days a week inside select grocery stores and 2,034 Jeanie® ATMs in Ohio, Kentucky, Indiana, Michigan, Illinois, Florida, Tennessee, West Virginia, Pennsylvania and Missouri. The Registrant reports on five business segments: Commercial Banking, Branch Banking, Consumer Lending, Investment Advisors and Fifth Third Processing Solutions ( FTPS ). During the first quarter of 2006, the Registrant began separating its Retail line of business into the Branch Banking and Consumer Lending business segments. All prior year information has been updated to reflect this presentation.

The Registrant believes that banking is first and foremost a relationship business where the strength of the competition and challenges for growth can vary in every market. Its affiliate operating model provides a competitive advantage by keeping the decisions close to the customer and by emphasizing individual relationships. Through its affiliate operating model, individual managers, from the banking center to the executive level, are given the opportunity to tailor financial solutions for their customers.

The Registrant's revenues are fairly evenly dependent on net interest income and noninterest income. For the three months ended June 30, 2006, net interest income, on a fully taxable equivalent ( FTE ) basis, and noninterest income provided 52% and 48% of total revenue, respectively. Therefore, changes in interest rates, credit quality, economic trends and the capital markets are primary factors that drive the performance of the Registrant. As discussed later in the Risk Management section, risk identification, measurement, monitoring, control and reporting are important to the management of risk and to the financial performance and capital strength of the Registrant.

The Registrant continues to focus on funding growth in loans and leases with growth in core deposits, which includes demand deposits, interest checking, savings, money market and other time deposits. When core deposit growth does not meet the growth in loans and leases, the Registrant has utilized cash flows from the securities portfolio as well as wholesale funding, which includes certificates \$100,000 and over, foreign office deposits, federal funds purchased, short-term bank notes, other short-term borrowings and long-term debt.

Net interest income, which continues to be the Registrant's largest revenue source, is the difference between interest income earned on assets, such as loans, leases and securities, and interest expense paid on liabilities, such as deposits and borrowings. Net interest income is affected by the general level of interest rates, the relative level of short- and long-term interest rates, changes in interest rates and changes in the amount and composition of interest-earning assets and interest-bearing liabilities. Generally, the rates of interest the Registrant earns on its assets and owes on its liabilities are established for a period of time. The change in market interest rates over time exposes the Registrant to interest rate risk through potential adverse changes to net interest income and financial position. The Registrant manages this risk by continually analyzing and adjusting the composition of its assets and liabilities based on their payment streams and interest rates, the timing of their maturities and their sensitivity to changes in market interest rates. Additionally, in the ordinary course of business, the Registrant enters into certain derivative transactions as part of its overall strategy to manage its interest rate and prepayment risks.

The Registrant is also exposed to the risk of losses on its loan and lease portfolio as a result of changing expected cash flows caused by loan defaults and inadequate collateral, among other factors.

Noninterest income is derived primarily from electronic funds transfer ( EFT ) and merchant transaction processing fees, card interchange, fiduciary and investment management fees, banking fees and service charges and mortgage banking revenue.

Net interest income, net interest margin, net interest rate spread and the efficiency ratio are presented in Management's Discussion and Analysis of Financial Condition and Results of Operations on an FTE basis. The FTE basis adjusts for the tax-favored status of income from certain loans and securities held by the Registrant that are not taxable for federal income tax purposes. The Registrant believes this presentation to be the preferred industry measurement of net interest income as it provides a relevant comparison between taxable and non-taxable amounts.

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The Registrant's net income was \$382 million in the second quarter of 2006, an eight percent decrease compared to \$417 million for the same period last year. Earnings per diluted share were \$.69 for the second quarter, an eight percent decrease from \$.75 for the same period last year. The Registrant's quarterly dividend increased to \$.40 per common share from \$.35 in the second quarter of 2005, an increase of 14%.

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### **Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

Net interest income (FTE) decreased five percent compared to the same period last year. Net interest margin decreased to 3.01% in the second quarter of 2006 from 3.29% in the same period last year and from 3.08% in the first quarter of 2006 largely due to the rise in short-term interest rates and the corresponding impact on the cost of certain wholesale funding categories, the impact of the primarily fixed-rate securities portfolio and mix shifts within the core deposit base. Noninterest income increased three percent over the same period last year with strong growth in electronic payment processing revenue and corporate banking revenue offset by an \$8 million decline in operating lease revenue as a result of the year-over-year runoff from the consumer automobile lease portfolio and a \$5 million, or 10%, decline in mortgage banking revenue due to lower gains on loan sales. Despite a 25% increase in volume-related bankcard expenditures and a nine percent increase in occupancy expense related to the addition of de-novo banking centers, noninterest expense increased only four percent over the same quarter last year as the Registrant continues to realize cost savings from expense control initiatives.

Credit quality metrics remained stable during the second quarter of 2006. Net charge-offs as a percent of average loans and leases were .37% in the second quarter of 2006 compared to .42% in the first quarter of 2006 and .34% in the second quarter of 2005. At June 30, 2006, nonperforming assets as a percent of loans and leases were down to .49% from .51% at March 31, 2006 and June 30, 2005.

The Registrant's capital ratios exceed the well-capitalized guidelines as defined by the Board of Governors of the Federal Reserve System (FRB). As of June 30, 2006, the Tier I capital ratio was 8.52% and the total risk-based capital ratio was 10.45%.

The Registrant continues to invest in the geographic areas that offer the best growth prospects, as it believes this investment is the most cost efficient method of expansion within its largest affiliate markets. During the first six months of 2006, the Registrant opened 25 new banking centers that did not involve the relocation or consolidation of existing facilities, with plans to add a total of 50 net banking centers (excluding relocations and consolidations) in key markets for the full-year 2006.

### **RECENT ACCOUNTING STANDARDS**

Note 2 of the Notes to Condensed Consolidated Financial Statements provides a complete discussion of the new accounting standards adopted by the Registrant during 2006 and 2005 and the expected impact of accounting standards issued but not yet required to be adopted.

### **CRITICAL ACCOUNTING POLICIES**

#### **Allowance for Loan and Lease Losses**

The Registrant maintains an allowance to absorb probable loan and lease losses inherent in the portfolio. The allowance is maintained at a level the Registrant considers to be adequate and is based on ongoing quarterly assessments and evaluations of the collectibility and historical loss experience of loans and leases. Credit losses are charged and recoveries are credited to the allowance. Provisions for loan and lease losses are based on the Registrant's review of the historical credit loss experience and such factors that, in management's judgment, deserve consideration under existing economic conditions in estimating probable credit losses. In determining the appropriate level of the allowance, the Registrant estimates losses using a range derived from base and conservative estimates. The Registrant's strategy for credit risk management includes a combination of conservative exposure limits significantly below legal lending limits and conservative underwriting, documentation and collections standards. The strategy also emphasizes diversification on a geographic, industry and customer level, regular credit examinations and quarterly management reviews of large credit exposures and loans experiencing deterioration of credit quality.

Larger commercial loans that exhibit probable or observed credit weakness are subject to individual review. Where appropriate, allowances are allocated to individual loans based on management's estimate of the borrower's ability to repay the loan given the availability of collateral, other sources of cash flow and legal options available to the Registrant. The review of individual loans includes those loans that are impaired as provided in SFAS No. 114, Accounting by Creditors for Impairment of a Loan. Any allowances for impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the underlying collateral. The Registrant evaluates the collectibility of both principal and interest when assessing the need for loss accrual. Historical loss rates are applied to other commercial loans not subject to specific allowance allocations. The loss rates are derived from a migration analysis, which tracks the net charge-off experience sustained on loans according to their internal risk grade. The risk grading system currently utilized for allowance analysis purposes encompasses 10 categories. The Registrant also maintains a dual risk rating system that provides for 13 probability of default grade categories and an additional six grade categories for estimating actual losses given an event of default. The probability of default and estimated loss given default evaluations are not separated in the 10-grade risk rating system. The Registrant is in the process of completing significant

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validation and testing of the dual risk rating system prior to implementation for allowance analysis purposes. The dual risk rating system is expected to be consistent with Basel II requirements and will allow for more precision in the analysis of commercial credit risk.

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### **Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

Homogenous loans and leases, such as consumer installment, residential mortgage and automobile leases are not individually risk graded. Rather, standard credit scoring systems and delinquency monitoring are used to assess credit risks. Allowances are established for each pool of loans based on the expected net charge-offs for one year. Loss rates are based on the average net charge-off history by loan category.

Historical loss rates for commercial and consumer loans may be adjusted for significant factors that, in management's judgment, reflect the impact of any current conditions on loss recognition. Factors that management considers in the analysis include the effects of the national and local economies, trends in the nature and volume of loans (delinquencies, charge-offs and nonaccrual loans), changes in mix, credit score migration comparisons, asset quality trends, risk management and loan administration, changes in the internal lending policies and credit standards, collection practices and examination results from bank regulatory agencies and the Registrant's internal credit examiners.

Regardless of the extent of the evaluation of the previously discussed factors, certain inherent but undetected losses are probable within the loan and lease portfolios. An unallocated component to the allowance is maintained to recognize the imprecision in estimating and measuring loss when evaluating allowances for individual loans or pools of loans. Allowances on individual loans and historical loss rates are reviewed quarterly and adjusted as necessary based on changing borrower and/or collateral conditions and actual collection and charge-off experience.

Loans acquired by the Registrant through a purchase business combination are evaluated for possible credit impairment. Reduction to the carrying value of the acquired loans as a result of credit impairment is recorded as an adjustment to goodwill. The Registrant does not carry over the acquired company's allowance for loan and lease losses nor does the Registrant add to its existing allowance for the acquired loans as part of purchase accounting.

The Registrant's determination of the allowance for commercial loans is sensitive to the risk grade it assigns to these loans. In the event that 10% of commercial loans in each risk category would experience a downgrade of one risk category, the allowance for commercial loans would increase by approximately \$71 million at June 30, 2006. The Registrant's determination of the allowance for residential and retail loans is sensitive to changes in estimated loss rates. In the event that estimated loss rates would increase by 10%, the allowance for residential and retail loans would increase by approximately \$23 million at June 30, 2006. As several quantitative and qualitative factors are considered in determining the allowance for loan and lease losses, these sensitivity analyses do not necessarily reflect the nature and extent of future changes in the allowance for loan and lease losses. They are intended to provide insights into the impact of adverse changes in risk grades and inherent losses and do not imply any expectation of future deterioration in the risk rating or loss rates. Given current processes employed by the Registrant, management believes the risk grades and inherent loss rates currently assigned are appropriate.

The Registrant's primary market areas for lending are Ohio, Kentucky, Indiana, Michigan, Illinois, Florida, Tennessee, West Virginia, Pennsylvania and Missouri. When evaluating the adequacy of allowances, consideration is given to this regional geographic concentration and the closely associated effect changing economic conditions have on the Registrant's customers.

In the current year, the Registrant has not substantively changed any material aspect of its overall approach to determine its allowance for loan and lease losses. There have been no material changes in assumptions or estimation techniques as compared to prior periods that impacted the determination of the current period allowance for loan and lease losses. Based on the procedures discussed above, the Registrant is of the opinion that the allowance of \$753 million was adequate, but not excessive, to absorb estimated credit losses associated with the loan and lease portfolio at June 30, 2006.

### **Reserve for Unfunded Commitments**

The reserve for unfunded commitments is maintained at a level believed by management to be sufficient to absorb estimated probable losses related to unfunded credit facilities. The determination of the adequacy of the reserve is based upon an evaluation of the unfunded credit facilities, including an assessment of historical commitment utilization experience, credit risk grading and credit grade migration. Net adjustments to the reserve for unfunded commitments are included in other noninterest expense.

### **Taxes**

The Registrant estimates income tax expense based on amounts expected to be owed to the various tax jurisdictions in which the Registrant conducts business. On a quarterly basis, management assesses the reasonableness of its effective tax rate based upon its current estimate of the amount and components of net income, tax credits and the applicable statutory tax rates expected for the full year. The estimated income tax

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expense is recorded in the Condensed Consolidated Statements of Income.

Deferred income tax assets and liabilities are determined using the balance sheet method and are reported in accrued taxes, interest and expenses in the Condensed Consolidated Balance Sheets. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax basis of assets and liabilities and recognizes enacted changes in tax rates and laws. Deferred tax assets are recognized subject to management judgment that realization is more likely than not.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

Accrued taxes represent the net estimated amount due or to be received from taxing jurisdictions and are reported in accrued taxes, interest and expenses in the Condensed Consolidated Balance Sheets. The Registrant evaluates and assesses the relative risks and appropriate tax treatment of transactions and filing positions after considering statutes, regulations, judicial precedent and other information and maintains tax accruals consistent with its evaluation of these relative risks and merits. Changes to the estimate of accrued taxes occur periodically due to changes in tax rates, interpretations of tax laws, the status of examinations being conducted by taxing authorities and changes to statutory, judicial and regulatory guidance that impact the relative risks of tax positions. These changes, when they occur, can affect deferred taxes and accrued taxes as well as the current period's income tax expense and can be significant to the operating results of the Registrant. See Note 2 of the Notes to the Condensed Consolidated Financial Statements for discussion of the recently issued accounting statement, which clarifies the accounting for uncertainty in income taxes. As described in greater detail in Note 9 of the Notes to the Condensed Consolidated Financial Statements, the Internal Revenue Service is currently challenging the Registrant's tax treatment of certain leasing transactions.

**Valuation of Servicing Rights**

When the Registrant sells loans through either securitizations or individual loan sales in accordance with its investment policies, it often retains servicing rights. Servicing rights resulting from loan sales are amortized in proportion to and over the period of estimated net servicing revenues. Servicing rights are assessed for impairment monthly, based on fair value, with temporary impairment recognized through a valuation allowance and permanent impairment recognized through a write-off of the servicing asset and related valuation allowance. Key economic assumptions used in measuring any potential impairment of the servicing rights include the prepayment speeds of the underlying loans, the weighted-average life, the discount rate, the weighted-average coupon and the weighted-average default rate, as applicable. The primary risk of material changes to the value of the servicing rights resides in the potential volatility in the economic assumptions used, particularly the prepayment speeds.

The Registrant monitors risk and adjusts its valuation allowance as necessary to adequately reserve for any probable impairment in the portfolio. For purposes of measuring impairment, the servicing rights are stratified based on the financial asset type and interest rates. In addition, the Registrant obtains an independent third-party valuation of mortgage servicing rights (MSR) on a quarterly basis. Fees received for servicing loans owned by investors are based on a percentage of the outstanding monthly principal balance of such loans and are included in noninterest income as loan payments are received. Costs of servicing loans are charged to expense as incurred.

The change in the fair value of MSRs at June 30, 2006, due to immediate 10% and 20% adverse changes in the current prepayment assumption would be approximately \$22 million and \$42 million, respectively, and due to immediate 10% and 20% favorable changes in the current prepayment assumption would be approximately \$24 million and \$49 million, respectively. The change in the fair value of the MSR portfolio at June 30, 2006, due to immediate 10% and 20% adverse changes in the discount rate assumption would be approximately \$20 million and \$39 million, respectively, and due to immediate 10% and 20% favorable changes in the discount rate assumption would be approximately \$22 million and \$45 million, respectively. Sensitivity analysis related to other consumer and commercial servicing rights is not material to the Registrant's Condensed Consolidated Financial Statements. These sensitivities are hypothetical and should be used with caution. As the figures indicate, change in fair value based on a 10% and 20% variation in assumptions typically cannot be extrapolated because the relationship of the change in assumptions to change in fair value may not be linear. Also, the effect of variation in a particular assumption on the fair value of the retained interests is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another, which might magnify or counteract the sensitivities. Additionally, the effect of the Registrant's non-qualifying hedging strategy, which is maintained to lessen the impact of changes in value of the MSR portfolio, is excluded from the above analysis.

**STATEMENTS OF INCOME ANALYSIS****Net Interest Income**

The Registrant continues to face a challenging net interest income environment as a result of rising short-term interest rates. Net interest income (FTE) was \$716 million for the second quarter of 2006, a decline of \$2 million compared to the sequential quarter and a decline of \$42 million compared to the prior year quarter. In terms of mix between volume and yield, the impact of changes in interest rates on net interest income (FTE) was a year-over-year decrease of 11%. The decline also resulted in continued compression of net interest margin to 3.01% from 3.08% in the first quarter and 3.29% in the second quarter of 2005. The Registrant currently expects modest margin compression in the third quarter with future trends dependent on the timing of further short-term interest rate increases and the overall direction of the forward curve as well as overall deposit and loan growth trends.

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Contraction in the net interest margin occurred in the second quarter despite growth in average earning assets. Total average earning assets increased four percent on an annualized sequential basis and three percent over the second quarter of 2005. Margin compression was the result of a 13 basis points ( bp ) sequential and a 53 bp year-over-year decrease in net interest rate spread. The decrease in net interest spread was the result of higher funding costs and the yield curve continuing to be flat, the impact of the primarily fixed-rate security portfolio and a change in mix within core deposits. The average interest rate spread between the 3-month Treasury bill and the 10-year Treasury note compressed from 123 bp in the second quarter of 2005 to 24 bp in the second quarter of 2006, illustrating the relative pressure between shorter-term and longer-term funding costs and general security portfolio

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### **Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

re-investment opportunities. The decrease in net interest rate spread was partially offset by an increased benefit from free funding of 68 bp in the second quarter of 2006, up 6 bp from the first quarter of 2006 and 25 bp over the second quarter of 2005. The large increase in the benefit of free funding over the second quarter of 2005 was the result of higher funding costs and an improvement in the net free funding position of the Registrant, calculated as the total of noninterest-bearing liabilities and equity less noninterest-earning assets, which increased three percent to \$16.7 billion.

The growth in average loans and leases over the second quarter of 2005 outpaced core deposit growth for the same period by \$2.5 billion. The funding shortfall was more than offset by a \$3.5 billion reduction in the average available-for-sale securities portfolio, as the Registrant continues to use cash flows from its securities portfolio to reduce its reliance on wholesale funding. For the second quarter of 2006, wholesale funding represented 42% of interest-bearing liabilities, down from 45% for the same period in the prior year. In the current interest rate environment, the Registrant expects to continue to use cash flows from its securities portfolio during the remainder of 2006 to fund its loan and lease growth that is in excess of its core deposit growth.

The Registrant continues to emphasize its highly competitive daily rate deposit pricing strategy. As part of this strategy, the Registrant maintains competitive deposit rates in all of its affiliate markets and across all of its deposit products. Additionally, a migration of interest checking balances into money market, savings and time deposit accounts has continued. During the second quarter of 2006, interest checking balances were 37% of average interest-bearing core deposits and savings and money market combined to represent 40%, compared to 46% and 34%, respectively, in the second quarter of 2005.

The cost of interest-bearing core deposits was 3.12% in the second quarter of 2006, up from 2.88% in the first quarter of 2006 and 1.86% in the second quarter of 2005. Despite the increasing deposit rates, the relative cost advantage of interest-bearing core deposits compared to wholesale funding increased from 130 bp in the second quarter of 2005 and 162 bp in the first quarter of 2006 to 188 bp in the second quarter of 2006.

Interest income (FTE) from loans and leases increased \$291 million, or 31%, compared to the second quarter of 2005. The increase resulted from the growth in average loans and leases of nine percent for the second quarter of 2006 over the comparable period in 2005 as well as a 111 bp increase in average rates. The increase in average loans and leases included growth in commercial loans and leases of 11% and growth in average consumer loans and leases of seven percent compared to the second quarter of 2005.

Interest income (FTE) from investment securities and short-term investments decreased \$31 million to \$253 million for the second quarter of 2006 compared to the same period in 2005 due to the previously mentioned reduction of the investment securities portfolio. The average yield on taxable securities increased by only 10 bp as a result of 84% of the debt securities within the available-for-sale portfolio being fixed-rate securities and the relative stability in longer-term interest rates.

The interest expense on core deposits increased \$163 million, or 83%, in the second quarter of 2006 over the comparable period in 2005 due to increases in short-term interest rates and increasing average balances. Average interest-bearing core deposits increased \$4 billion, or nine percent, compared to the second quarter of 2005. The Registrant continues to focus on growing its core deposit balances in order to fund loan growth, improve the funding mix and improve net interest margin trends.

The interest expense on wholesale funding increased by \$139 million, or 52%, in the second quarter over the comparable period in 2005 due to increasing interest rates partially offset by a \$1.4 billion decrease in average balances. The cost of wholesale funding increased from 3.16% in the second quarter of 2005 to 5.00% in the second quarter of 2006 due to the increases in the short-end of the interest rate curve. Included within other short-term borrowings are the Registrant's customer repo sweep balances, which were \$2.7 billion and \$2.8 billion on an average basis for the three months ended June 30, 2006 and 2005, respectively.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****TABLE 2: Consolidated Average Balance Sheets and Analysis of Net Interest Income (FTE)**

| For the three months ended          | June 30, 2006      |                  |                           | June 30, 2005      |                  |                           | Attribution of Change<br>in Net Interest Income<br>(a) |      |       |
|-------------------------------------|--------------------|------------------|---------------------------|--------------------|------------------|---------------------------|--------------------------------------------------------|------|-------|
|                                     | Average<br>Balance | Revenue/<br>Cost | Average<br>Yield/<br>Rate | Average<br>Balance | Revenue/<br>Cost | Average<br>Yield/<br>Rate | Volume                                                 | Rate | Total |
| (\$ in millions)                    |                    |                  |                           |                    |                  |                           |                                                        |      |       |
| <b>Assets</b>                       |                    |                  |                           |                    |                  |                           |                                                        |      |       |
| Interest-earning assets:            |                    |                  |                           |                    |                  |                           |                                                        |      |       |
| Loans and leases (b):               |                    |                  |                           |                    |                  |                           |                                                        |      |       |
| Commercial loans                    | \$ 20,239          | \$ 363           | 7.19%                     | \$ 17,768          | \$ 248           | 5.60%                     | \$ 38                                                  | 77   | 115   |
| Commercial mortgage                 | 9,980              | 176              | 7.08                      | 9,042              | 136              | 6.01                      | 15                                                     | 25   | 40    |
| Commercial construction             | 5,840              | 111              | 7.67                      | 5,467              | 80               | 5.90                      | 6                                                      | 25   | 31    |
| Commercial leases                   | 3,729              | 47               | 5.03                      | 3,436              | 44               | 5.15                      | 4                                                      | (1)  | 3     |
| Subtotal commercial                 | 39,788             | 697              | 7.03                      | 35,713             | 508              | 5.71                      | 63                                                     | 126  | 189   |
| Residential mortgage                | 8,756              | 129              | 5.90                      | 8,453              | 115              | 5.45                      | 4                                                      | 10   | 14    |
| Residential construction            | 735                | 11               | 6.02                      | 576                | 8                | 5.36                      | 2                                                      | 1    | 3     |
| Other consumer loans                | 22,430             | 377              | 6.75                      | 20,169             | 287              | 5.71                      | 34                                                     | 56   | 90    |
| Consumer leases                     | 1,384              | 16               | 4.70                      | 1,851              | 21               | 4.52                      | (5)                                                    |      | (5)   |
| Subtotal consumer                   | 33,305             | 533              | 6.42                      | 31,049             | 431              | 5.56                      | 35                                                     | 67   | 102   |
| Total loans and leases              | 73,093             | 1,230            | 6.75                      | 66,762             | 939              | 5.64                      | 98                                                     | 193  | 291   |
| Securities:                         |                    |                  |                           |                    |                  |                           |                                                        |      |       |
| Taxable                             | 21,642             | 239              | 4.43                      | 24,771             | 268              | 4.33                      | (35)                                                   | 6    | (29)  |
| Exempt from income taxes (b)        | 616                | 11               | 7.33                      | 815                | 15               | 7.29                      | (4)                                                    |      | (4)   |
| Other short-term investments        | 181                | 3                | 5.60                      | 130                | 1                | 3.28                      | 1                                                      | 1    | 2     |
| Total interest-earning assets       | 95,532             | 1,483            | 6.23                      | 92,478             | 1,223            | 5.30                      | 60                                                     | 200  | 260   |
| Cash and due from banks             | 2,564              |                  |                           | 2,822              |                  |                           |                                                        |      |       |
| Other assets                        | 8,393              |                  |                           | 8,182              |                  |                           |                                                        |      |       |
| Allowance for loan and lease losses | (748)              |                  |                           | (717)              |                  |                           |                                                        |      |       |
| Total assets                        | \$ 105,741         |                  |                           | \$ 102,765         |                  |                           |                                                        |      |       |
| <b>Liabilities</b>                  |                    |                  |                           |                    |                  |                           |                                                        |      |       |
| Interest-bearing liabilities:       |                    |                  |                           |                    |                  |                           |                                                        |      |       |
| Interest checking                   | \$ 17,025          | \$ 102           | 2.39%                     | \$ 19,267          | \$ 71            | 1.49%                     | \$ (9)                                                 | 40   | 31    |
| Savings                             | 12,064             | 87               | 2.90                      | 9,697              | 35               | 1.44                      | 10                                                     | 42   | 52    |
| Money market                        | 6,429              | 64               | 4.01                      | 4,755              | 28               | 2.37                      | 12                                                     | 24   | 36    |
| Other time deposits                 | 10,449             | 105              | 4.00                      | 8,286              | 61               | 2.93                      | 18                                                     | 26   | 44    |
| Certificates - \$100,000 and over   | 5,316              | 61               | 4.64                      | 3,946              | 29               | 2.92                      | 12                                                     | 20   | 32    |
| Foreign office deposits             | 4,382              | 52               | 4.77                      | 3,907              | 29               | 2.98                      | 4                                                      | 19   | 23    |
| Federal funds purchased             | 3,886              | 48               | 4.97                      | 3,952              | 29               | 2.97                      |                                                        | 19   | 19    |
| Short-term bank notes               |                    |                  |                           | 230                | 2                | 2.84                      | (1)                                                    | (1)  | (2)   |
| Other short-term borrowings         | 4,854              | 52               | 4.31                      | 5,190              | 34               | 2.63                      | (2)                                                    | 20   | 18    |
| Long-term debt                      | 14,465             | 196              | 5.45                      | 17,049             | 147              | 3.46                      | (25)                                                   | 74   | 49    |

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|                                                         |                   |              |             |            |       |       |      |      |     |
|---------------------------------------------------------|-------------------|--------------|-------------|------------|-------|-------|------|------|-----|
| Total interest-bearing liabilities                      | <b>78,870</b>     | <b>767</b>   | <b>3.90</b> | 76,279     | 465   | 2.44  | 19   | 283  | 302 |
| Demand deposits                                         | <b>13,764</b>     |              |             | 13,905     |       |       |      |      |     |
| Other liabilities                                       | <b>3,500</b>      |              |             | 3,357      |       |       |      |      |     |
| Total liabilities                                       | <b>96,134</b>     |              |             | 93,541     |       |       |      |      |     |
| Shareholders' equity                                    | <b>9,607</b>      |              |             | 9,224      |       |       |      |      |     |
| Total liabilities and shareholders' equity              | <b>\$ 105,741</b> |              |             | \$ 102,765 |       |       |      |      |     |
| Net interest income margin                              | <b>\$ 716</b>     | <b>3.01%</b> |             | \$ 758     | 3.29% | \$ 41 | (83) | (42) |     |
| Net interest rate spread                                |                   | <b>2.33</b>  |             |            | 2.86  |       |      |      |     |
| Interest-bearing liabilities to interest-earning assets |                   | <b>82.56</b> |             |            | 82.48 |       |      |      |     |

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- (a) Changes in interest not solely due to volume or yield/rate are allocated in proportion to the absolute dollar amount of change in volume and yield/rate.
- (b) The net taxable equivalent adjustment amounts included in the above table are \$6 million and \$8 million for the three months ended June 30, 2006 and 2005, respectively.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****TABLE 3: Consolidated Average Balance Sheets and Analysis of Net Interest Income (FTE)**

| For the six months ended            | June 30, 2006   |              |                    | June 30, 2005   |              |                    | Attribution of Change in Net Interest Income (a) |      |       |
|-------------------------------------|-----------------|--------------|--------------------|-----------------|--------------|--------------------|--------------------------------------------------|------|-------|
|                                     | Average Balance | Revenue/Cost | Average Yield/Rate | Average Balance | Revenue/Cost | Average Yield/Rate | Volume                                           | Rate | Total |
| (\$ in millions)                    |                 |              |                    |                 |              |                    |                                                  |      |       |
| <b>Assets</b>                       |                 |              |                    |                 |              |                    |                                                  |      |       |
| Interest-earning assets:            |                 |              |                    |                 |              |                    |                                                  |      |       |
| Loans and leases (b):               |                 |              |                    |                 |              |                    |                                                  |      |       |
| Commercial loans                    | \$ 19,852       | \$ 691       | 7.01%              | \$ 17,921       | \$ 481       | 5.42%              | \$ 57                                            | 153  | 210   |
| Commercial mortgage                 | 9,712           | 336          | 6.96               | 8,715           | 254          | 5.87               | 31                                               | 51   | 82    |
| Commercial construction             | 6,024           | 222          | 7.43               | 5,170           | 146          | 5.69               | 27                                               | 49   | 76    |
| Commercial leases                   | 3,708           | 93           | 5.08               | 3,414           | 88           | 5.18               | 7                                                | (2)  | 5     |
| Subtotal commercial                 | 39,296          | 1,342        | 6.88               | 35,220          | 969          | 5.55               | 122                                              | 251  | 373   |
| Residential mortgage                | 8,555           | 249          | 5.87               | 8,435           | 230          | 5.49               | 3                                                | 16   | 19    |
| Residential construction            | 720             | 21           | 5.94               | 522             | 14           | 5.30               | 5                                                | 2    | 7     |
| Other consumer loans                | 22,334          | 734          | 6.63               | 19,832          | 552          | 5.62               | 75                                               | 107  | 182   |
| Consumer leases                     | 1,462           | 35           | 4.87               | 1,915           | 44           | 4.66               | (11)                                             | 2    | (9)   |
| Subtotal consumer                   | 33,071          | 1,039        | 6.34               | 30,704          | 840          | 5.52               | 72                                               | 127  | 199   |
| Total loans and leases              | 72,367          | 2,381        | 6.63               | 65,924          | 1,809        | 5.53               | 194                                              | 378  | 572   |
| Securities:                         |                 |              |                    |                 |              |                    |                                                  |      |       |
| Taxable                             | 21,878          | 481          | 4.44               | 24,852          | 534          | 4.33               | (66)                                             | 13   | (53)  |
| Exempt from income taxes (b)        | 630             | 23           | 7.47               | 835             | 31           | 7.32               | (8)                                              |      | (8)   |
| Other short-term investments        | 169             | 4            | 5.31               | 229             | 2            | 2.06               | (1)                                              | 3    | 2     |
| Total interest-earning assets       | 95,044          | 2,889        | 6.13               | 91,840          | 2,376        | 5.22               | 119                                              | 394  | 513   |
| Cash and due from banks             | 2,616           |              |                    | 2,721           |              |                    |                                                  |      |       |
| Other assets                        | 8,327           |              |                    | 8,046           |              |                    |                                                  |      |       |
| Allowance for loan and lease losses | (746)           |              |                    | (716)           |              |                    |                                                  |      |       |
| Total assets                        | \$ 105,241      |              |                    | \$ 101,891      |              |                    |                                                  |      |       |
| <b>Liabilities</b>                  |                 |              |                    |                 |              |                    |                                                  |      |       |
| Interest-bearing liabilities:       |                 |              |                    |                 |              |                    |                                                  |      |       |
| Interest checking                   | \$ 17,312       | \$ 201       | 2.34%              | \$ 19,618       | \$ 134       | 1.38%              | \$ (17)                                          | 84   | 67    |
| Savings                             | 11,827          | 163          | 2.79               | 9,519           | 61           | 1.30               | 18                                               | 84   | 102   |
| Money market                        | 6,258           | 119          | 3.83               | 4,770           | 53           | 2.26               | 20                                               | 46   | 66    |
| Other time deposits                 | 10,101          | 194          | 3.87               | 8,038           | 113          | 2.83               | 33                                               | 48   | 81    |
| Certificates - \$100,000 and over   | 4,995           | 109          | 4.41               | 3,744           | 54           | 2.92               | 22                                               | 33   | 55    |
| Foreign office deposits             | 4,217           | 96           | 4.59               | 4,122           | 56           | 2.72               | 1                                                | 39   | 40    |
| Federal funds purchased             | 4,217           | 99           | 4.72               | 4,060           | 54           | 2.68               | 2                                                | 43   | 45    |
| Short-term bank notes               |                 |              |                    | 501             | 6            | 2.60               | (3)                                              | (3)  | (6)   |
| Other short-term borrowings         | 4,786           | 97           | 4.07               | 5,062           | 61           | 2.41               | (3)                                              | 39   | 36    |
| Long-term debt                      | 14,798          | 377          | 5.14               | 16,331          | 267          | 3.29               | (27)                                             | 137  | 110   |

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|                                                         |                   |              |             |            |       |       |       |      |     |
|---------------------------------------------------------|-------------------|--------------|-------------|------------|-------|-------|-------|------|-----|
| Total interest-bearing liabilities                      | <b>78,511</b>     | <b>1,455</b> | <b>3.74</b> | 75,765     | 859   | 2.29  | 46    | 550  | 596 |
| Demand deposits                                         | <b>13,719</b>     |              |             | 13,696     |       |       |       |      |     |
| Other liabilities                                       | <b>3,407</b>      |              |             | 3,264      |       |       |       |      |     |
| Total liabilities                                       | <b>95,637</b>     |              |             | 92,725     |       |       |       |      |     |
| Shareholders' equity                                    | <b>9,604</b>      |              |             | 9,166      |       |       |       |      |     |
| Total liabilities and shareholders' equity              | <b>\$ 105,241</b> |              |             | \$ 101,891 |       |       |       |      |     |
| Net interest income margin                              | <b>\$ 1,434</b>   | <b>3.04%</b> |             | \$ 1,517   | 3.33% | \$ 73 | (156) | (83) |     |
| Net interest rate spread                                |                   | <b>2.39</b>  |             |            | 2.93  |       |       |      |     |
| Interest-bearing liabilities to interest-earning assets |                   | <b>82.60</b> |             |            | 82.50 |       |       |      |     |

- 
- (a) Changes in interest not solely due to volume or yield/rate are allocated in proportion to the absolute dollar amount of change in volume and yield/rate.
- (b) The net taxable equivalent adjustment amounts included in the above table are \$13 million and \$17 million for the six months ended June 30, 2006 and 2005, respectively.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****Provision for Loan and Lease Losses**

The Registrant provides as an expense an amount for probable loan and lease losses within the loan portfolio that is based on the factors discussed in the Critical Accounting Policies section. The provision is recorded to bring the allowance for loan and lease losses to a level deemed appropriate by the Registrant. Actual credit losses on loans and leases are charged against the allowance for loan and lease losses. The amount of loans actually removed from the Condensed Consolidated Balance Sheets is referred to as charge-offs. Net charge-offs include current period charge-offs less recoveries in the current period on previously charged off assets.

The provision for loan and lease losses increased to \$71 million in the second quarter of 2006 compared to \$60 million in the same period last year. The increase is due to both the increase in net charge-offs from \$55 million in the second quarter of 2005 to \$67 million and increased loan growth in the second quarter of 2006. The allowance for loan and lease losses as a percent of loans and leases declined to 1.04% from 1.09% at June 30, 2005. Refer to the Credit Risk Management section for further information on the provision for loan and lease losses, net charge-offs and other factors considered by the Registrant in assessing the credit quality of the loan portfolio and the allowance for loan and lease losses.

**Noninterest Income**

For the three and six months ended June 30, 2006, noninterest income increased by three percent and two percent, respectively. The components of noninterest income for these periods are as follows:

**TABLE 4: Noninterest Income**

| (\$ in millions)                      | For the three months ended June 30, |      |                | For the six months ended June 30, |       |                |
|---------------------------------------|-------------------------------------|------|----------------|-----------------------------------|-------|----------------|
|                                       | 2006                                | 2005 | Percent Change | 2006                              | 2005  | Percent Change |
| Electronic payment processing revenue | \$ 211                              | 183  | 15%            | \$ 407                            | 354   | 15%            |
| Service charges on deposits           | 135                                 | 132  | 2              | 261                               | 253   | 3              |
| Mortgage banking net revenue          | 41                                  | 46   | (10)           | 88                                | 87    | 1              |
| Investment advisory revenue           | 96                                  | 92   | 5              | 187                               | 182   | 3              |
| Corporate banking revenue             | 82                                  | 74   | 10             | 157                               | 136   | 16             |
| Other noninterest income              | 76                                  | 93   | (19)           | 157                               | 200   | (23)           |
| Securities gains, net                 | 14                                  | 15   | (6)            | 15                                | 30    | (48)           |
| Total noninterest income              | \$ 655                              | 635  | 3%             | \$ 1,272                          | 1,242 | 2%             |

During the first quarter of 2006, the Registrant refined its presentation of noninterest income in order to provide more granularity around its revenue streams. The primary result of this refinement was the consolidation of the Registrant's interest rate derivative sales, international service fees, institutional sales and loan and lease syndication fees into a new income statement line item named corporate banking revenue. Corporate banking revenue increased to \$82 million in the second quarter of 2006, up 10% over the comparable period in 2005. The growth in corporate banking revenue was largely attributable to continued strong sales in international services and loan and lease related fees.

Electronic payment processing revenue increased \$28 million in the second quarter of 2006 compared to the same period last year. EFT revenue increased \$14 million, or 14%, to \$116 million, as a result of continued success in attracting financial institution customers as well as an \$8 million increase in issuer interchange. Merchant processing revenue increased 17%, to \$95 million, compared to the same period in 2005. Trends in the second quarter of 2006 are representative of continuing momentum in attracting new customer relationships moderated by slower growth in the level of retail sales transaction volumes. The Registrant continues to see significant opportunities to attract new retailers and financial institution customers. The Registrant handles electronic processing for over 117,000 merchant locations and 1,500 financial institutions worldwide, including The Kroger Co., Nordstrom, Inc., the Armed Forces Financial Network and, most recently, Linens n Things, Inc., Talbots, Uno Restaurant Holdings Corporation and Rollins, Inc. (wholly-owned subsidiaries include: Orkin, Inc., Western Pest Services and the Industrial Fumigant Company).

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Service charges on deposits increased two percent in the second quarter of 2006 compared to the same period last year. Commercial deposit revenue increased two percent while consumer deposit revenue increased three percent. Despite growth in the number of relationships and overall activity, commercial service charges were negatively impacted compared to the second quarter last year by a 43% increase in earnings credits on commercial customer demand deposit accounts due to the higher interest rate environment. Net new consumer deposit account production increased by over 50% through the first half of 2006 compared to the same period last year. Growth in the number of customer deposit account relationships has improved consumer deposit revenue and deposit generation continues to be a primary focus of the Registrant.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

Mortgage banking net revenue decreased to \$41 million in the second quarter of 2006 from \$46 million in the same period last year. Mortgage originations were \$2.6 billion in the second quarter of 2006 and 2005. The components of mortgage banking net revenue for the three and six months ended June 30, 2006 and 2005 are as follows:

**TABLE 5: Components of Mortgage Banking Net Revenue**

| (\$ in millions)                                                                                                   | For the three months<br>ended June 30, |      | For the six months<br>ended June 30, |      |
|--------------------------------------------------------------------------------------------------------------------|----------------------------------------|------|--------------------------------------|------|
|                                                                                                                    | 2006                                   | 2005 | 2006                                 | 2005 |
| Origination fees and gains (losses) on loan sales                                                                  | \$ 27                                  | 38   | 48                                   | 61   |
| Servicing revenue:                                                                                                 |                                        |      |                                      |      |
| Servicing fees                                                                                                     | 30                                     | 27   | 59                                   | 52   |
| Servicing rights amortization                                                                                      | (17)                                   | (16) | (31)                                 | (33) |
| Net valuation adjustments on servicing rights and free-standing derivatives entered into to economically hedge MSR | 1                                      | (3)  | 12                                   | 7    |
| Net servicing revenue                                                                                              | 14                                     | 8    | 40                                   | 26   |
| Mortgage banking net revenue                                                                                       | \$ 41                                  | 46   | 88                                   | 87   |

Mortgage net servicing revenue increased by \$6 million as compared to the same period last year. Net servicing revenue is comprised of gross servicing fees and amortization as well as valuation adjustments on mortgage servicing rights and mark-to-market adjustments on both settled and outstanding free-standing derivative financial instruments. The Registrant's total residential mortgage loans serviced at June 30, 2006 and 2005 were \$35.8 billion and \$32.3 billion, respectively, with \$27.1 billion and \$24.5 billion, respectively, of residential mortgage loans serviced for others.

Net valuation adjustments on servicing rights and free-standing derivatives were affected by the general rise in longer-term interest rates in the second quarter of 2006 and the corresponding general decrease in prepayment speeds, which led to the reversal of \$6 million in temporary impairment on the MSR portfolio in the second quarter as compared to a recognition of \$21 million in temporary impairment during the second quarter of 2005. Servicing rights are deemed impaired when a borrower's loan rate is distinctly higher than prevailing rates. Impairment on servicing rights is reversed when the prevailing rates return to a level commensurate with the borrower's loan rate. The Registrant recognized a net loss of \$5 million and net gain of \$18 million in the second quarter of 2006 and 2005, respectively, related to changes in fair value and settlement of free-standing derivatives purchased to economically hedge the MSR portfolio.

The Registrant maintains a non-qualifying hedging strategy to manage a portion of the risk associated with changes in impairment on the MSR portfolio. In the second quarter of 2006, the Registrant primarily used principal only swaps, interest rate swaps and swaptions to hedge the economic risk of the MSR portfolio as they were deemed to be the best available instruments for several reasons. Principal only swaps hedge the mortgage-LIBOR spread because they appreciate in value as a result of tightening spreads. They also provide prepayment protection by increasing in value when prepayment speeds increase, as opposed to MSRs that lose value in a faster prepayment environment. Receive fixed/pay floating interest rate swaps and swaptions increase in value when interest rates do not increase as quickly as expected. As of June 30, 2006 and 2005, the Registrant held a combination of free-standing derivatives, including principal only swaps, swaptions and interest rate swaps with a net negative fair value of \$3 million and a net positive fair value of \$11 million, respectively, on outstanding notional amounts of \$9 billion and \$3.7 billion, respectively. In addition to the derivative positions used to economically hedge the MSR portfolio, the Registrant began to acquire various securities (primarily principal only strips) during 2005 and 2006 as a component of its non-qualifying hedging strategy. Principal only strips increase in value as prepayment speeds increase, thus providing an economic hedge for the MSR portfolio. As of June 30, 2006, the Registrant's available-for-sale securities portfolio included \$240 million of securities related to the non-qualifying hedging strategy.

Investment advisory revenues increased by \$4 million, or five percent, in the second quarter of 2006 compared to the same period last year. The increase in revenue was primarily related to improved securities and brokerage income and private client revenues. The Registrant continues to focus its sales efforts on integrating services across business lines and working closely with retail and commercial team members to take

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advantage of a diverse and expanding customer base. The Registrant is one of the largest money managers in the Midwest and as of June 30, 2006 had over \$203 billion in assets under care and \$31 billion in assets under management.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

The major components of other noninterest income are as follows:

**TABLE 6: Components of Other Noninterest Income**

| (\$ in millions)                 | For the three months<br>ended June 30, |      | For the six months<br>ended June 30, |      |
|----------------------------------|----------------------------------------|------|--------------------------------------|------|
|                                  | 2006                                   | 2005 | 2006                                 | 2005 |
| Cardholder fees                  | \$ 11                                  | 11   | 23                                   | 22   |
| Consumer loan and lease fees     | 13                                     | 15   | 24                                   | 28   |
| Operating lease income           | 7                                      | 15   | 15                                   | 35   |
| Bank owned life insurance income | 22                                     | 22   | 43                                   | 45   |
| Insurance income                 | 7                                      | 7    | 14                                   | 12   |
| Other                            | 16                                     | 23   | 38                                   | 58   |
| Total other noninterest income   | \$ 76                                  | 93   | 157                                  | 200  |

Other noninterest income decreased by 19% in the second quarter of 2006 compared to the same period last year. The decrease was primarily attributable to the continued runoff in the operating lease portfolio. Consumer operating lease revenues result from the consolidation of a special purpose entity in 2003 that was formed for the purpose of the sale and subsequent leaseback of leased automobiles. The consolidation was the result of the Registrant's adoption of FASB Interpretation No. 46. Declines in operating lease revenues will continue throughout 2006, however to a lesser extent, as automobile leases continue to mature and are partially offset by originations of commercial operating leases.

**Noninterest Expense**

During the second quarter, the Registrant continued to invest in the expansion of the retail distribution network and in the information technology infrastructure. Operating expense levels are often measured using the efficiency ratio (noninterest expense divided by the sum of net interest income (FTE) and noninterest income), which was 55.3% and 52.2% for the second quarter of 2006 and 2005, respectively. The Registrant continues to focus on efficiency initiatives as part of its core emphasis on operating leverage and views its recent investments as its platform for future growth and increasing expense efficiency.

With the continued focus on expense control, the Registrant expects growth in noninterest expenses to be consistent with recent trends. Cost savings initiatives will continue to be somewhat mitigated by investments in certain high opportunity markets, as evidenced by the 25 net new banking centers added in the first half and the 25 net new banking centers expected to be added in the second half of 2006.

The major components of noninterest expense are as follows:

**TABLE 7: Noninterest Expense**

| (\$ in millions)               | For the three months<br>ended June 30, |      | Percent<br>Change | For the six months<br>ended June 30, |      | Percent<br>Change |
|--------------------------------|----------------------------------------|------|-------------------|--------------------------------------|------|-------------------|
|                                | 2006                                   | 2005 |                   | 2006                                 | 2005 |                   |
| Salaries, wages and incentives | \$ 303                                 | 295  | 3%                | \$ 586                               | 561  | 5%                |
| Employee benefits              | 69                                     | 67   | 4                 | 156                                  | 148  | 5                 |
| Equipment expense              | 29                                     | 25   | 16                | 56                                   | 50   | 12                |
| Net occupancy expense          | 59                                     | 54   | 9                 | 118                                  | 108  | 9                 |
| Other noninterest expense      | 299                                    | 287  | 4                 | 574                                  | 565  | 1                 |

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|                           |    |            |     |    |    |              |       |    |
|---------------------------|----|------------|-----|----|----|--------------|-------|----|
| Total noninterest expense | \$ | <b>759</b> | 728 | 4% | \$ | <b>1,490</b> | 1,432 | 4% |
|---------------------------|----|------------|-----|----|----|--------------|-------|----|

Total noninterest expense increased four percent in the second quarter of 2006 compared to the same period last year. The increase in expenses is primarily due to the recognition of approximately \$9 million of incremental expense related to the adoption of SFAS No. 123 (R) and the April 2006 issuance of stock-based awards to retirement-eligible employees, increases in bankcard volume-related costs and the increase in occupancy expenses offset by a decrease in operating lease expense. Net occupancy expenses increased nine percent in the second quarter of 2006 over the same period last year primarily due to the addition of 61 net new banking centers since June 30, 2005.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

The major components of other noninterest expense are as follows:

**TABLE 8: Components of Other Noninterest Expense**

| (\$ in millions)                      | For the three months ended June 30, |      | For the six months ended June 30, |      |
|---------------------------------------|-------------------------------------|------|-----------------------------------|------|
|                                       | 2006                                | 2005 | 2006                              | 2005 |
| Marketing and communications          | \$ 32                               | 31   | 65                                | 61   |
| Postal and courier                    | 12                                  | 12   | 25                                | 24   |
| Bankcard                              | 79                                  | 63   | 148                               | 126  |
| Loan and lease                        | 20                                  | 23   | 41                                | 39   |
| Travel                                | 14                                  | 14   | 25                                | 27   |
| Information technology and operations | 27                                  | 25   | 51                                | 52   |
| Operating lease                       | 4                                   | 10   | 10                                | 26   |
| Other                                 | 111                                 | 109  | 209                               | 210  |
| Total other noninterest expense       | \$ 299                              | 287  | 574                               | 565  |

Total other noninterest expense increased by \$12 million from the second quarter of 2005 primarily due to increases in bankcard expenses. Bankcard expense increased 25% compared to last year due to an increase in the number of merchant and retail customers as well as continued organic growth in debit and credit card usage. The decrease in operating lease expense is attributable to the continued runoff in the operating lease portfolio. The remaining expense captions continue to be well-controlled.

**Applicable Income Taxes**

The Registrant's income before income taxes, applicable income tax expense and effective tax rate for each of the periods are as follows:

**TABLE 9: Applicable Income Taxes**

| (\$ in millions)                                 | For the three months ended June 30, |      | For the six months ended June 30, |       |
|--------------------------------------------------|-------------------------------------|------|-----------------------------------|-------|
|                                                  | 2006                                | 2005 | 2006                              | 2005  |
| Income before income taxes and cumulative effect | \$ 535                              | 597  | 1,054                             | 1,183 |
| Applicable income taxes                          | 153                                 | 180  | 312                               | 361   |
| Effective tax rate                               | 28.5%                               | 30.1 | 29.6                              | 30.5  |

Applicable income tax expense for all periods include the benefit from tax-exempt income, tax-advantaged investments and general business tax credits, partially offset by the effect of nondeductible expenses. Income tax expense for the second quarter of 2006 includes the favorable resolution of certain tax examinations and statute expirations.

**Cumulative Effect of Change in Accounting Principle**

In the first quarter of 2006, the Registrant recognized a benefit of approximately \$4 million, net of \$2 million of tax, related to the adoption of SFAS No. 123 (Revised 2004). The benefit recognized relates to the Registrant's estimate of forfeiture experience to be realized for all unvested stock-based awards outstanding.

**BUSINESS SEGMENT REVIEW**

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The Registrant reports on five business segments: Commercial Banking, Branch Banking, Consumer Lending, Investment Advisors and Processing Solutions. During the first quarter of 2006, the Registrant began reporting its Retail line of business as two business segments, Branch Banking and Consumer Lending. All prior year information has been updated to reflect this presentation. Further detailed financial information on each business segment is included in Note 14 of the Notes to the Condensed Consolidated Financial Statements.

Results of the Registrant's business segments are presented based on its management structure and management accounting practices. The structure and practices are specific to the Registrant; therefore, the financial results of the Registrant's business segments are not necessarily comparable with similar information for other financial institutions. The Registrant refines its methodologies from time to time as management accounting practices are improved and businesses change. Revisions to the Registrant's methodologies are applied on a retroactive basis.

The Registrant manages interest rate risk centrally at the corporate level by employing a funds transfer pricing (FTP) methodology. This methodology insulates the business segments from interest rate risk, enabling them to focus on servicing customers through loan originations and deposit taking. The FTP system assigns charge and credit rates to classes of assets and liabilities, respectively, based on expected duration. The Registrant has not changed the conceptual application of FTP during 2005 or 2006. The net impact of the FTP methodology is included in Other/Eliminations.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

The financial results of the business segments include allocations for shared services and headquarters expenses. Even with these allocations, the financial results are not necessarily indicative of the business segments' financial condition and results of operations as if they were to exist as independent entities. Additionally, the business segments form synergies by taking advantage of cross-sell opportunities and when funding operations by accessing the capital markets as a collective unit. Net income by business segment is summarized as follows:

**TABLE 10: Business Segment Results**

| (\$ in millions)     | For the three months<br>ended June 30, |      | For the six months<br>ended June 30, |       |
|----------------------|----------------------------------------|------|--------------------------------------|-------|
|                      | 2006                                   | 2005 | 2006                                 | 2005  |
| Commercial Banking   | \$ 202                                 | 193  | 396                                  | 372   |
| Branch Banking       | 240                                    | 205  | 464                                  | 394   |
| Consumer Lending     | 37                                     | 54   | 80                                   | 102   |
| Investment Advisors  | 40                                     | 31   | 74                                   | 56    |
| Processing Solutions | 50                                     | 32   | 80                                   | 67    |
| Other/Eliminations   | (187)                                  | (98) | (348)                                | (169) |
| Net income           | \$ 382                                 | 417  | 746                                  | 822   |

*Commercial Banking*

Commercial Banking provides a comprehensive range of financial services and products to large and middle-market businesses, governments and professional customers. In addition to the traditional lending and depository offerings, Commercial Banking products and services include, among others, cash management, foreign exchange and international trade finance, derivatives and capital markets services, asset-based lending, real estate finance, public finance, commercial leasing and syndicated finance. The table below contains selected financial data for the Commercial Banking segment.

**TABLE 11: Commercial Banking Selected Financial Data**

| (\$ in millions)                    | For the three months<br>ended June 30, |      | For the six<br>months<br>ended June 30, |      |
|-------------------------------------|----------------------------------------|------|-----------------------------------------|------|
|                                     | 2006                                   | 2005 | 2006                                    | 2005 |
| <b>Income Statement Data</b>        |                                        |      |                                         |      |
| Net interest income (FTE)           | \$ 380                                 | 352  | 755                                     | 695  |
| Provision for loan and lease losses | 31                                     | 23   | 67                                      | 52   |
| Noninterest income:                 |                                        |      |                                         |      |
| Corporate banking revenue           | 78                                     | 73   | 150                                     | 132  |
| Service charges on deposits         | 38                                     | 38   | 77                                      | 76   |
| Other noninterest income            | 12                                     | 15   | 24                                      | 30   |
| Noninterest expense:                |                                        |      |                                         |      |
| Salaries, incentives and benefits   | 60                                     | 59   | 121                                     | 114  |
| Other noninterest expenses          | 129                                    | 117  | 253                                     | 227  |
| Income before taxes                 | 288                                    | 279  | 565                                     | 540  |
| Applicable income taxes (a)         | 86                                     | 86   | 169                                     | 168  |
| Net income                          | \$ 202                                 | 193  | 396                                     | 372  |

**Average Balance Sheet Data**

|                                            |           |        |        |        |
|--------------------------------------------|-----------|--------|--------|--------|
| Commercial loans                           | \$ 33,377 | 30,026 | 32,924 | 29,677 |
| Demand deposits                            | 5,994     | 6,160  | 6,087  | 6,187  |
| Interest checking                          | 3,762     | 2,913  | 3,844  | 2,826  |
| Savings and money market                   | 5,238     | 4,686  | 5,335  | 4,589  |
| Certificates over \$100,000 and other time | 1,537     | 1,074  | 1,473  | 1,004  |

(a) Includes taxable-equivalent adjustments of \$3 million for the three months ended June 30, 2006 and 2005 and \$7 million and \$6 million for the six months ended June 30, 2006 and 2005, respectively.

Net income increased \$9 million, or four percent, compared to the second quarter of 2005 largely as a result of loan and deposit growth. Average commercial loans and leases increased 11% to \$33.4 billion over the second quarter of 2005, with growth occurring in all loan categories.

Despite average demand deposits declining modestly from the prior year second quarter, average core deposits increased nine percent to \$15.0 billion in the second quarter of 2006 from \$13.8 billion in 2005. The increase in average core deposits and loans and the related net FTP impact led to a \$28 million increase in net interest income compared to the same period last year.

Noninterest income increased modestly compared to the same quarter last year as fee captions displayed mixed results. Overall, corporate banking revenue increased \$5 million, or seven percent, largely due to growth in nearly all sub-captions. Noninterest expense increased \$13 million, or eight percent, compared to the second quarter of 2005 as continued strong production volumes contributed to increases in loan and bankcard related expense and other noninterest expense.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)***Branch Banking*

Branch Banking provides a full range of deposit and loan and lease products to individuals and small businesses through 1,138 banking centers. Branch Banking offers depository and loan products, such as checking and savings accounts, home equity lines of credit, credit cards and loans for automobile and other personal financing needs, as well as products designed to meet the specific needs of small businesses, including cash management services. The table below contains selected financial data for the Branch Banking segment.

**TABLE 12: Branch Banking Selected Financial Data**

| (\$ in millions)                     | For the three months<br>ended June 30, |        | For the six<br>months<br>ended June 30, |        |
|--------------------------------------|----------------------------------------|--------|-----------------------------------------|--------|
|                                      | 2006                                   | 2005   | 2006                                    | 2005   |
| <b>Income Statement Data</b>         |                                        |        |                                         |        |
| Net interest income                  | \$ 476                                 | 416    | 928                                     | 809    |
| Provision for loan and lease losses  | 26                                     | 23     | 48                                      | 43     |
| Noninterest income:                  |                                        |        |                                         |        |
| Electronic payment processing        | 49                                     | 41     | 93                                      | 77     |
| Service charges on deposits          | 93                                     | 91     | 178                                     | 171    |
| Investment advisory income           | 23                                     | 22     | 46                                      | 43     |
| Other noninterest income             | 29                                     | 31     | 56                                      | 56     |
| Noninterest expense:                 |                                        |        |                                         |        |
| Salaries, incentives and benefits    | 117                                    | 115    | 232                                     | 227    |
| Net occupancy and equipment expenses | 38                                     | 34     | 74                                      | 65     |
| Other noninterest expenses           | 118                                    | 112    | 230                                     | 214    |
| Income before taxes                  | 371                                    | 317    | 717                                     | 607    |
| Applicable income taxes              | 131                                    | 112    | 253                                     | 213    |
| Net income                           | \$ 240                                 | 205    | 464                                     | 394    |
| <b>Average Balance Sheet Data</b>    |                                        |        |                                         |        |
| Consumer loans                       | \$ 11,274                              | 10,529 | 11,257                                  | 10,389 |
| Commercial loans                     | 4,308                                  | 3,947  | 4,300                                   | 3,838  |
| Demand deposits                      | 5,677                                  | 5,718  | 5,642                                   | 5,595  |
| Interest checking                    | 10,915                                 | 14,052 | 11,180                                  | 14,406 |
| Savings and money market             | 11,612                                 | 8,618  | 11,270                                  | 8,538  |
| Time deposits                        | 12,751                                 | 9,908  | 12,203                                  | 9,668  |

Net income increased \$35 million, or 17%, compared to the second quarter of 2005 as growth in average loans and leases and deposits led to a 15% increase in net interest income. Average loans and leases increased eight percent compared to the second quarter of 2005 and total deposits increased seven percent over the second quarter of 2005 with double-digit increases in savings, money market and consumer time deposits mitigated by a 22% decrease in interest checking. As a result of the growth in average loans, core deposits and the related net FTP impact, net interest income increased \$60 million compared to the same period last year.

Noninterest income increased \$9 million, or five percent, from the second quarter of 2005 as Branch Banking continues to realize results from its cross-sell initiatives. Increases in nearly every caption were led by electronic payment processing revenue, which increased \$8 million, or 20%.

Noninterest expense increased by four percent compared to the second quarter of 2005 as costs were contained despite the effect from the Registrant's continued de-novo banking center growth strategy. Net occupancy and equipment expenses increased 13% as a result of the continued opening of new banking centers. Since the second quarter of 2005, 61 net new banking centers were opened. The Registrant continues

to position itself for sustained long-term growth through new banking center additions in key markets.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)***Consumer Lending*

Consumer Lending includes the Registrant's mortgage and home equity lending activities and other indirect lending activities. Mortgage and home equity lending activities include the origination, retention and servicing of mortgage and home equity loans or lines of credit, sales and securitizations of those loans or pools of loans or lines of credit and all associated hedging activities. Other indirect lending activities include loans to consumers through auto dealers and federal and private student education loans. The table below contains selected financial data for the Consumer Lending segment.

**TABLE 13: Consumer Lending Selected Financial Data**

| (\$ in millions)                    | For the three months<br>ended June 30, |      | For the six<br>months<br>ended June 30, |      |
|-------------------------------------|----------------------------------------|------|-----------------------------------------|------|
|                                     | 2006                                   | 2005 | 2006                                    | 2005 |
| <b>Income Statement Data</b>        |                                        |      |                                         |      |
| Net interest income                 | \$ 99                                  | 107  | 198                                     | 211  |
| Provision for loan and lease losses | 23                                     | 14   | 51                                      | 41   |
| Noninterest income:                 |                                        |      |                                         |      |
| Mortgage banking net revenue        | 39                                     | 43   | 85                                      | 82   |
| Other noninterest income            | 21                                     | 33   | 47                                      | 72   |
| Noninterest expense:                |                                        |      |                                         |      |
| Salaries, incentives and benefits   | 28                                     | 24   | 56                                      | 47   |
| Other noninterest expenses          | 51                                     | 62   | 101                                     | 119  |
| Income before taxes                 | 57                                     | 83   | 122                                     | 158  |
| Applicable income taxes             | 20                                     | 29   | 42                                      | 56   |
| Net income                          | \$ 37                                  | 54   | 80                                      | 102  |

**Average Balance Sheet Data**

|                |           |        |        |        |
|----------------|-----------|--------|--------|--------|
| Consumer loans | \$ 20,321 | 18,825 | 20,108 | 18,599 |
|----------------|-----------|--------|--------|--------|

Net income decreased \$17 million, or 31%, compared to the second quarter of 2005 largely due to the effects of the flattening yield curve. Compared to the second quarter of 2005, net interest income decreased \$8 million, or seven percent, despite average loans and leases increasing eight percent, due to a 31 bp decline in the spread between loans yields and the related FTP charge as a result of the increasing competitive nature in this segment.

The Registrant had mortgage originations of \$2.6 billion for the three months ended June 30, 2006 and 2005. Despite the stable origination volume, mortgage banking net revenue declined \$4 million due to lower gains on sales. Decreases in other noninterest income and expense were largely a result of the runoff of the consumer automobile lease portfolio as operating lease income and expense decreased from the second quarter of 2005 by \$11 million and \$8 million, respectively.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)***Investment Advisors*

Investment Advisors provides a full range of investment alternatives for individuals, companies and not-for-profit organizations. The Registrant's primary services include trust, asset management, retirement plans and custody. Fifth Third Securities, Inc., an indirect wholly-owned subsidiary of the Registrant, offers full-service retail brokerage services to individual clients and broker dealer services to the institutional marketplace. Fifth Third Asset Management, Inc., an indirect wholly-owned subsidiary of the Registrant, provides asset management services and also advises the Registrant's proprietary family of mutual funds, Fifth Third Funds.\* The table below contains selected financial data for the Investment Advisors segment.

**TABLE 14: Investment Advisors Selected Financial Data**

| (\$ in millions)                    | For the three months ended June 30, |       | For the six months ended June 30, |       |
|-------------------------------------|-------------------------------------|-------|-----------------------------------|-------|
|                                     | 2006                                | 2005  | 2006                              | 2005  |
| <b>Income Statement Data</b>        |                                     |       |                                   |       |
| Net interest income                 | \$ 59                               | 47    | 113                               | 92    |
| Provision for loan and lease losses | 1                                   | 1     | 3                                 | 3     |
| Noninterest income:                 |                                     |       |                                   |       |
| Investment advisory income          | 97                                  | 92    | 188                               | 183   |
| Other noninterest income            | 4                                   | 4     | 9                                 | 7     |
| Noninterest expense:                |                                     |       |                                   |       |
| Salaries, incentives and benefits   | 42                                  | 41    | 85                                | 84    |
| Other noninterest expenses          | 55                                  | 53    | 107                               | 108   |
| Income before taxes                 | 62                                  | 48    | 115                               | 87    |
| Applicable income taxes             | 22                                  | 17    | 41                                | 31    |
| Net income                          | \$ 40                               | 31    | 74                                | 56    |
| <b>Average Balance Sheet Data</b>   |                                     |       |                                   |       |
| Loans and leases                    | \$ 3,072                            | 2,592 | 3,058                             | 2,541 |
| Core deposits                       | 4,658                               | 3,978 | 4,398                             | 4,062 |

Net income increased \$9 million, or 30%, in the second quarter of 2006 compared to the same period last year. This increase was the result of a 27% improvement in net interest income due to loan and deposit growth and the related FTP impact. Average loans and leases increased to \$3.1 billion, a 19% increase from the second quarter last year while core deposits increased 17% to \$4.7 billion. Noninterest income increased \$5 million, or five percent, with retail brokerage and private client services both posting increases of \$2 million. Noninterest expense increased four percent compared to the same period last year primarily related to an increase in incentive compensation from improved performance in retail brokerage.

**\* FIFTH THIRD FUNDS® PERFORMANCE DISCLOSURE**

Fifth Third Funds investments are: **NOT INSURED BY THE FDIC** or any other government agency, are not deposits or obligations of, or guaranteed by, any bank, the distributor or of the Funds any of their respective affiliates, and involve investment risks, including the possible loss of the principal amount invested. An investor should consider the fund's investment objectives, risks and charges and expenses carefully before investing or sending money. The Funds' prospectus contains this and other important information about the Funds. To obtain a prospectus or any other information about Fifth Third Funds, please call 1-800-282-5706 or visit [www.53.com](http://www.53.com). Please read the prospectus carefully before investing. Fifth Third Funds are distributed by Fifth Third Funds Distributor, Inc., 3435 Stelzer Road, Columbus, Ohio 43219.



**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)***Processing Solutions*

Fifth Third Processing Solutions provides electronic funds transfer, debit, credit and merchant transaction processing, operates the Jeanie® ATM network and provides other data processing services to affiliated and unaffiliated customers. The table below contains selected financial data for the Processing Solutions segment.

**TABLE 15: Processing Solutions Selected Financial Data**

| (\$ in millions)                    | For the three months<br>ended June 30, |      | For the six months<br>ended June 30, |      |
|-------------------------------------|----------------------------------------|------|--------------------------------------|------|
|                                     | 2006                                   | 2005 | 2006                                 | 2005 |
| <b>Income Statement Data</b>        |                                        |      |                                      |      |
| Net interest income                 | \$ 9                                   | 9    | 18                                   | 17   |
| Provision for loan and lease losses | 2                                      | 3    | 4                                    | 5    |
| Noninterest income:                 |                                        |      |                                      |      |
| Merchant processing                 | 97                                     | 82   | 184                                  | 161  |
| EFT processing                      | 73                                     | 67   | 143                                  | 127  |
| Other noninterest income            | 28                                     | 3    | 33                                   | 19   |
| Noninterest expense:                |                                        |      |                                      |      |
| Salaries, incentives and benefits   | 18                                     | 13   | 36                                   | 27   |
| Processing costs                    | 89                                     | 74   | 172                                  | 147  |
| Other noninterest expenses          | 21                                     | 22   | 41                                   | 41   |
| Income before taxes                 | 77                                     | 49   | 125                                  | 104  |
| Applicable income taxes             | 27                                     | 17   | 45                                   | 37   |
| Net income                          | \$ 50                                  | 32   | 80                                   | 67   |

Net income increased \$18 million, or 58%, compared to the second quarter of 2005. Merchant and EFT revenues increased by 18% and 10%, respectively, primarily due to new customer additions and related increased volume. Other noninterest income increased \$25 million primarily due to a \$24 million gain from the MasterCard Incorporated redemption of a portion of the common shares held by the Registrant. The strong increase in noninterest income was mitigated by a 17% increase in noninterest expense, which increased due to headcount additions, investment in information technology and processing costs. The 20% increase in processing costs resulted primarily from volume-related costs as merchant transactions processed increased 19% over the second quarter of 2005. The Registrant continues to see significant opportunities to attract new financial institution customers and retailers within this business segment.

*Other/Eliminations*

Other/Eliminations includes the unallocated portion of the investment portfolio, certain wholesale funding, unassigned equity and certain support activities and other items not attributed to the business segments.

The results of Other/Eliminations were primarily impacted by the decrease in interest income from investment securities and the increased cost of wholesale funding. Interest income from the securities portfolio decreased \$33 million from the second quarter of 2005 due to the continued runoff of the securities portfolio in 2005 and 2006. Interest expense on wholesale funding increased \$139 million from the second quarter of 2005. This increase in interest expense resulted from the increase in the average interest rate on wholesale funding, which rose from 3.16% in the second quarter of 2005 to 5.00% in the second quarter of 2006.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****BALANCE SHEET ANALYSIS****Loans**

The table below summarizes the end of period total loans and leases, which includes loans held for sale, by major category:

**TABLE 16: Components of Total Loans and Leases (including held for sale)**

| (\$ in millions)                         | June 30, 2006<br>Balance | Percent<br>of Total | December 31, 2005<br>Balance | Percent<br>of Total | June 30, 2005<br>Balance | Percent<br>of Total |
|------------------------------------------|--------------------------|---------------------|------------------------------|---------------------|--------------------------|---------------------|
| <b>Commercial:</b>                       |                          |                     |                              |                     |                          |                     |
| Commercial loans                         | \$ 20,618                | 29%                 | \$ 19,299                    | 27%                 | \$ 18,017                | 27%                 |
| Commercial mortgage                      | 9,792                    | 13                  | 9,188                        | 13                  | 9,091                    | 14                  |
| Commercial construction                  | 5,950                    | 8                   | 6,342                        | 9                   | 5,590                    | 8                   |
| Commercial leases                        | 3,740                    | 5                   | 3,698                        | 5                   | 3,537                    | 5                   |
| <b>Total commercial loans and leases</b> | <b>40,100</b>            | <b>55</b>           | <b>38,527</b>                | <b>54</b>           | <b>36,235</b>            | <b>54</b>           |
| <b>Consumer:</b>                         |                          |                     |                              |                     |                          |                     |
| Residential mortgage                     | 8,780                    | 12                  | 8,296                        | 12                  | 7,808                    | 12                  |
| Residential construction                 | 748                      | 1                   | 695                          | 1                   | 611                      | 1                   |
| Credit card                              | 945                      | 1                   | 866                          | 1                   | 749                      | 1                   |
| Home equity                              | 12,277                   | 16                  | 12,000                       | 17                  | 11,521                   | 17                  |
| Other consumer loans                     | 9,360                    | 13                  | 9,250                        | 13                  | 8,343                    | 12                  |
| Consumer leases                          | 1,298                    | 2                   | 1,595                        | 2                   | 1,812                    | 3                   |
| <b>Total consumer loans and leases</b>   | <b>33,408</b>            | <b>45</b>           | <b>32,702</b>                | <b>46</b>           | <b>30,844</b>            | <b>46</b>           |
| <b>Total loans and leases</b>            | <b>\$ 73,508</b>         | <b>100%</b>         | <b>\$ 71,229</b>             | <b>100%</b>         | <b>\$ 67,079</b>         | <b>100%</b>         |

Total loans and leases increased 10% over the second quarter of 2005. Total commercial loans and leases increased \$3.9 billion, or 11%, compared to June 30, 2005. The increase in commercial loans and leases was primarily driven by strong growth in commercial and industrial loans which increased 14% over the second quarter 2005. The mix of commercial loans was essentially unchanged from prior periods.

Total consumer loans and leases increased \$2.6 billion, or eight percent, compared to June 30, 2005, as a result of double-digit growth in residential construction, residential mortgage, credit card and other consumer loans. The Registrant is continuing to devote significant focus on producing retail loan originations given the attractive yields available in these products. Consumer lease balances decreased 19% from December 31, 2005 and 28% compared to June 30, 2005 largely resulting from continued competition from captive finance companies offering promotional lease rates. Excluding consumer leases, consumer loans increased 11% over June 30, 2005.

The table below summarizes the average total loans and leases by major category:

**TABLE 17: Components of Average Total Loans and Leases (including held for sale)**

| (\$ in millions) | June 30, 2006<br>Balance | December 31, 2005<br>Balance | June 30, 2005<br>Balance |
|------------------|--------------------------|------------------------------|--------------------------|
|------------------|--------------------------|------------------------------|--------------------------|

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|                                                            | Percent<br>of Total |      | Percent<br>of Total |      | Percent<br>of Total |      |
|------------------------------------------------------------|---------------------|------|---------------------|------|---------------------|------|
| Commercial:                                                |                     |      |                     |      |                     |      |
| Commercial loans                                           | \$ 20,239           | 27%  | \$ 18,909           | 27%  | \$ 17,768           | 26%  |
| Commercial mortgage                                        | 9,980               | 14   | 9,159               | 13   | 9,042               | 14   |
| Commercial construction                                    | 5,840               | 8    | 6,051               | 9    | 5,467               | 8    |
| Commercial leases                                          | 3,729               | 5    | 3,611               | 5    | 3,436               | 5    |
|                                                            |                     |      |                     |      |                     |      |
| Total commercial loans and leases                          | 39,788              | 54   | 37,730              | 54   | 35,713              | 53   |
| Consumer:                                                  |                     |      |                     |      |                     |      |
| Residential mortgage                                       | 8,756               | 12   | 8,444               | 12   | 8,453               | 13   |
| Residential construction                                   | 735                 | 1    | 673                 | 1    | 576                 | 1    |
| Credit card                                                | 897                 | 1    | 825                 | 1    | 755                 | 1    |
| Home equity                                                | 12,193              | 17   | 11,884              | 17   | 11,325              | 17   |
| Other consumer loans                                       | 9,340               | 13   | 9,251               | 13   | 8,089               | 12   |
| Consumer leases                                            | 1,384               | 2    | 1,682               | 2    | 1,851               | 3    |
|                                                            |                     |      |                     |      |                     |      |
| Total consumer loans and leases                            | 33,305              | 46   | 32,759              | 46   | 31,049              | 47   |
|                                                            |                     |      |                     |      |                     |      |
| Total loans and leases                                     | \$ 73,093           | 100% | \$ 70,489           | 100% | \$ 66,762           | 100% |
|                                                            |                     |      |                     |      |                     |      |
| Total portfolio loans and leases (excluding held for sale) | \$ 72,209           |      | \$ 69,218           |      | \$ 65,649           |      |

## **Table of Contents**

### **Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

With strong growth in each category, average commercial loans and leases increased \$4.1 billion, or 11%, compared to the second quarter of 2005. The Registrant experienced double-digit growth in more than half of its affiliates, including 18% growth in the Florida markets and 21% growth in the Chicago market.

On an average basis, consumer loans and leases increased \$2.3 billion, or seven percent, compared to the second quarter of 2005, highlighted by 39% growth in the Florida markets and strong growth in the Tennessee and Chicago affiliates. The growth in average consumer loans and leases was a result of strong growth in each category mitigated by decreases in consumer leases.

### **Investment Securities**

Total investment securities were \$20.9 billion, \$22.4 billion and \$25.0 billion at June 30, 2006, December 31, 2005 and June 30, 2005, respectively. During the second quarter of 2006, increasing interest rates across the yield curve resulted in an increase in the net unrealized loss on the available-for-sale securities portfolio from \$851 million at March 31, 2006 to \$1.0 billion at June 30, 2006. Securities are classified as available-for-sale when, in management's judgment, they may be sold in response to or in anticipation of changes in market conditions. The Registrant maintains its intent and ability to hold these securities to the earlier of the recovery of the losses or maturity. At June 30, 2006, 93% of the unrealized losses in the available-for-sale security portfolio were comprised of securities issued by U.S. Treasury and Government agencies, U.S. Government sponsored agencies and states and political subdivisions as well as agency mortgage-backed securities. The Registrant believes the price movements in these securities were the result of the movement in market interest rates, particularly given the negligible inherent credit risk for these securities.

In the second quarter of 2006, the Registrant continued its efforts to reduce the level of available-for-sale securities on the balance sheet. On an amortized cost basis, period end available-for-sale securities decreased \$1.2 billion since December 31, 2005 and \$3.4 billion since June 30, 2005. At June 30, 2006, available-for-sale securities have decreased to 22% of interest-earning assets, compared to 24% and 27% at December 31, 2005 and June 30, 2005, respectively. At June 30, 2006, 16% of the debt securities in the available-for-sale portfolio were adjustable-rate instruments, compared to 17% at December 31, 2005 and 19% at June 30, 2005. The estimated weighted-average life of the debt securities in the available-for-sale portfolio was 4.8 years at June 30, 2006 compared to 4.3 years at December 31, 2005 and 3.7 years at June 30, 2005. The increase in the weighted-average life results from lower prepayment expectations due to rising interest rates.

Information presented in the following table is on a weighted-average life basis anticipating future prepayments. Yield information is presented on an FTE basis and is computed utilizing historical cost balances. Maturity and yield calculations for the total available-for-sale portfolio exclude equity securities that have no stated yield or maturity.

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****TABLE 18: Characteristics of Available-for-Sale and Other Securities**

| As of June 30, 2006 (\$ in millions)                  | Amortized Cost | Fair Value | Weighted-Average Life<br>(in years) | Weighted-Average Yield |
|-------------------------------------------------------|----------------|------------|-------------------------------------|------------------------|
| U.S. Treasury and Government agencies:                |                |            |                                     |                        |
| Average life of one year or less                      | \$ 2           | \$ 2       | 0.3                                 | 2.93%                  |
| Average life 1 - 5 years                              |                |            |                                     |                        |
| Average life 5 - 10 years                             | 499            | 459        | 6.9                                 | 3.71                   |
| Average life greater than 10 years                    | 4              | 4          | 12.7                                | 6.05                   |
| Total                                                 | 505            | 465        | 6.9                                 | 3.72                   |
| U.S. Government sponsored agencies:                   |                |            |                                     |                        |
| Average life of one year or less                      | 116            | 115        | 0.1                                 | 4.43                   |
| Average life 1 - 5 years                              | 1,348          | 1,288      | 2.9                                 | 3.81                   |
| Average life 5 - 10 years                             | 352            | 321        | 6.4                                 | 4.07                   |
| Average life greater than 10 years                    |                |            |                                     |                        |
| Total                                                 | 1,816          | 1,724      | 3.4                                 | 3.90                   |
| Obligations of states and political subdivisions (a): |                |            |                                     |                        |
| Average life of one year or less                      | 51             | 51         | 0.5                                 | 7.78                   |
| Average life 1 - 5 years                              | 319            | 325        | 3.3                                 | 7.47                   |
| Average life 5 - 10 years                             | 240            | 245        | 6.4                                 | 7.15(b)                |
| Average life greater than 10 years                    | 40             | 40         | 11.9                                | 6.90(b)                |
| Total                                                 | 650            | 661        | 4.7                                 | 7.37                   |
| Agency mortgage-backed securities:                    |                |            |                                     |                        |
| Average life of one year or less                      | 40             | 40         | 0.6                                 | 6.31                   |
| Average life 1 - 5 years                              | 9,752          | 9,256      | 3.7                                 | 4.33                   |
| Average life 5 - 10 years                             | 5,373          | 5,043      | 6.9                                 | 4.88                   |
| Average life greater than 10 years                    | 81             | 74         | 10.7                                | 4.79                   |
| Total                                                 | 15,246         | 14,413     | 4.9                                 | 4.53                   |
| Other bonds, notes and debentures (c):                |                |            |                                     |                        |
| Average life of one year or less                      | 23             | 23         | 0.5                                 | 4.41                   |
| Average life 1 - 5 years                              | 1,031          | 1,001      | 3.2                                 | 4.87                   |
| Average life 5 - 10 years                             | 1,070          | 1,031      | 7.7                                 | 5.13                   |
| Average life greater than 10 years                    | 16             | 15         | 22.2                                | 3.71                   |
| Total                                                 | 2,140          | 2,070      | 5.6                                 | 4.98                   |
| Other securities (d)                                  | 1,019          | 1,012      |                                     |                        |
| Total available-for-sale and other securities         | \$ 21,376      | \$ 20,345  | 4.8                                 | 4.58%                  |

(a) Taxable-equivalent yield adjustments included in above table are 2.58%, 2.48%, 2.39%, 2.30% and 2.45% for securities with an average life of one year or less, 1-5 years, 5-10 years, greater than 10 years and in total, respectively.

(b) Weighted-average yield excludes \$17 million and \$35 million of securities with an average life of 5-10 years and greater than 10 years, respectively, related to qualified zone academy bonds whose yields are realized through income tax credits. The weighted-average effective yield of these instruments is 6.77%.

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- (c) Other bonds, notes and debentures consist of non-agency mortgage backed securities, certain other asset backed securities (primarily automobile and commercial loan backed securities) and corporate bond securities.
- (d) Other securities consist of FHLB and Federal Reserve Bank restricted stock holdings that are carried at cost, Federal Home Loan Mortgage Corporation ( FHLMC ) preferred stock holdings, certain mutual fund holdings and equity security holdings.

**TABLE 19: Components of Investment Securities (amortized cost basis)**

|                                                  | June 30,  | December 31, | June 30, |
|--------------------------------------------------|-----------|--------------|----------|
| (\$ in millions)                                 | 2006      | 2005         | 2005     |
| Available-for-sale and other:                    |           |              |          |
| U.S. Treasury and Government agencies            | \$ 505    | 506          | 504      |
| U.S. Government sponsored agencies               | 1,816     | 2,034        | 2,406    |
| Obligations of states and political subdivisions | 650       | 657          | 787      |
| Agency mortgage-backed securities                | 15,246    | 16,127       | 17,280   |
| Other bonds, notes and debentures                | 2,140     | 2,119        | 2,838    |
| Other securities                                 | 1,019     | 1,090        | 999      |
| Total available-for-sale and other securities    | \$ 21,376 | 22,533       | 24,814   |
| Held-to-maturity:                                |           |              |          |
| Obligations of states and political subdivisions | \$ 347    | 378          | 295      |
| Other bonds, notes and debentures                | 11        | 11           | 12       |
| Total held-to-maturity                           | \$ 358    | 389          | 307      |

**Table of Contents****Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****Deposits**

The table below summarizes the end of period total deposits by major category:

**TABLE 20: Deposits**

| (\$ in millions)                  | June 30, 2006 |                  | December 31, 2005 |                  | June 30, 2005 |                  |
|-----------------------------------|---------------|------------------|-------------------|------------------|---------------|------------------|
|                                   | Balance       | Percent of Total | Balance           | Percent of Total | Balance       | Percent of Total |
| Demand                            | \$ 14,078     | 20%              | \$ 14,609         | 22%              | \$ 14,393     | 23%              |
| Interest checking                 | 16,788        | 24               | 18,282            | 27               | 18,811        | 30               |
| Savings                           | 12,061        | 17               | 11,276            | 17               | 9,653         | 15               |
| Money market                      | 6,505         | 9                | 6,129             | 9                | 4,732         | 7                |
| Other time                        | 10,627        | 15               | 9,313             | 14               | 8,513         | 14               |
| Certificates - \$100,000 and over | 5,691         | 8                | 4,343             | 6                | 3,986         | 6                |
| Foreign office                    | 4,773         | 7                | 3,482             | 5                | 3,089         | 5                |
| Total deposits                    | \$ 70,523     | 100%             | \$ 67,434         | 100%             | \$ 63,177     | 100%             |

Deposit balances represent an important source of funding and revenue growth opportunity. The Registrant is continuing to focus on transaction account deposit growth in its retail and commercial franchises by enhancing its product offering and providing competitive rates. The Registrant's goal is to continue to grow the core deposit component of its funding profile. At June 30, 2006, core deposits represented 57% of the Registrant's asset funding base, compared to 54% at June 30, 2005.

Total deposits increased 12% compared to June 30, 2005 primarily attributable to 25% or greater growth in savings, money market and other time deposits, mitigated by an 11% decrease in interest checking. The Registrant continues to realize a mix shift as customers move from lower-yield transaction accounts to higher-yield time deposits. Overall, transaction deposits increased four percent compared to the second quarter of 2005. The Registrant experienced double-digit transaction account deposit growth in the Detroit, Evansville, Indianapolis, Lexington, Louisville, Orlando and Tampa affiliates.

Foreign office deposits represent U.S. dollar denominated deposits of the Registrant's foreign branch located in the Cayman Islands. The Registrant utilizes these deposit balances as a method to fund earning asset growth.

The table below summarizes the average total deposits by major category:

**TABLE 21: Average Deposits**

| (\$ in millions)                  | June 30, 2006 |                  | December 31, 2005 |                  | June 30, 2005 |                  |
|-----------------------------------|---------------|------------------|-------------------|------------------|---------------|------------------|
|                                   | Balance       | Percent of Total | Balance           | Percent of Total | Balance       | Percent of Total |
| Demand                            | \$ 13,764     | 20%              | \$ 14,099         | 21%              | \$ 13,905     | 22%              |
| Interest checking                 | 17,025        | 25               | 17,828            | 26               | 19,267        | 31               |
| Savings                           | 12,064        | 17               | 11,036            | 17               | 9,697         | 15               |
| Money market                      | 6,429         | 9                | 5,974             | 9                | 4,755         | 7                |
| Other time                        | 10,449        | 15               | 9,143             | 14               | 8,286         | 13               |
| Certificates - \$100,000 and over | 5,316         | 8                | 4,354             | 7                | 3,946         | 6                |
| Foreign office                    | 4,382         | 6                | 3,703             | 6                | 3,907         | 6                |

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|                |                  |             |           |      |           |      |
|----------------|------------------|-------------|-----------|------|-----------|------|
| Total deposits | <b>\$ 69,429</b> | <b>100%</b> | \$ 66,137 | 100% | \$ 63,763 | 100% |
|----------------|------------------|-------------|-----------|------|-----------|------|

## Borrowings

Total short-term borrowings were \$7.8 billion at June 30, 2006 compared to \$9.6 billion at December 31, 2005 and \$9.5 billion at June 30, 2005. Long-term debt decreased five percent and 17% compared to December 31, 2005 and June 30, 2005, respectively. The Registrant continues to explore additional alternatives regarding the level and cost of various other sources of funding. Refer to the Liquidity Risk Management section for discussion on the Registrant's liquidity management.

**TABLE 22: Borrowings**

| (\$ in millions)            | June 30,<br>2006 | December 31,<br>2005 | June 30,<br>2005 |
|-----------------------------|------------------|----------------------|------------------|
| Federal funds purchased     | <b>\$ 2,493</b>  | 5,323                | 4,523            |
| Other short-term borrowings | <b>5,275</b>     | 4,246                | 4,972            |
| Long-term debt              | <b>14,502</b>    | 15,227               | 17,494           |
| Total borrowings            | <b>\$ 22,270</b> | 24,796               | 26,989           |

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### **Quantitative and Qualitative Disclosure about Market Risk (Item 3)**

#### **RISK MANAGEMENT OVERVIEW**

Managing risk is an essential component of successfully operating a financial services company. The Registrant's risk management function is responsible for the identification, measurement, monitoring, control and reporting of risk and avoidance of those risks that are inconsistent with the Registrant's risk profile. The Enterprise Risk Management division, led by the Registrant's Chief Risk Officer, ensures consistency in the Registrant's approach to managing and monitoring risk within the structure of the Registrant's affiliate operating model. The risks faced by the Registrant include, but are not limited to, credit, market, operational and regulatory compliance. In addition, the Internal Audit division provides an independent assessment of the Registrant's internal control structure and related systems and processes. The Enterprise Risk Management division includes the following key functions:

Risk Policy - ensures consistency in the approach to risk management as the Registrant's clearinghouse for credit, market and operational risk policies, procedures and guidelines;

Operational Risk Management - responsible for the risk self-assessment process, the change control evaluation process, fraud prevention and detection, and root cause analysis and corrective action plans relating to identified operational losses;

Insurance Risk Management - responsible for all property, casualty and liability insurance policies including the claims administration process for the Registrant;

Capital Markets Risk Management - responsible for establishing and monitoring proprietary trading limits, monitoring liquidity and interest rate risk and utilizing value at risk and earnings at risk models;

Credit Risk Review - responsible for evaluating the sufficiency of underwriting, documentation and approval processes for consumer and commercial credits;

Compliance Risk Management - responsible for oversight of compliance with all banking regulations;

Risk Strategies and Reporting - responsible for quantitative analytics and Board of Directors and senior management reporting on credit, market and operational risk metrics.

Designated risk managers have been assigned to the business lines reporting jointly to the senior executives within the division or affiliate and to the Enterprise Risk Management division. Affiliate risk management is handled by regional risk managers who are responsible for multiple affiliates and who report jointly to affiliate presidents and the Enterprise Risk Management division.

Risk management oversight and governance is provided by the Risk and Compliance Committee of the Board of Directors and through multiple management committees whose membership includes a broad cross-section of line of business, affiliate and support representatives. The Risk and Compliance Committee of the Board of Directors consists of three outside directors and has the responsibility for the oversight of credit, market, operational, regulatory compliance and strategic risk management activities for the Registrant, as well as for the Registrant's overall aggregate risk profile. The Risk and Compliance Committee has approved the formation of key management governance committees that are responsible for evaluating risks and controls. These committees include the Market Risk Committee, the Credit Risk Committee and the Operational Risk Committee. There are also new products and initiatives processes applicable to every line of business to ensure an appropriate standard readiness assessment is performed before launching a new product or initiative. Significant risk policies approved by the management governance committees are also reviewed and approved by the Board of Directors' Risk and Compliance Committee.

## CREDIT RISK MANAGEMENT

The objective of the Registrant's credit risk management strategy is to quantify and manage credit risk exposure on an aggregate portfolio basis, as well as to limit the risk of loss resulting from an individual customer default. The Registrant's credit risk management strategy is based on three core principles: conservatism, diversification and monitoring. The Registrant believes that effective credit risk management begins with conservative lending practices. These practices include conservative exposure and counterparty limits and conservative underwriting, documentation and collection standards. The Registrant's credit risk management strategy also emphasizes diversification on a geographic, industry and customer level, regular credit examinations and monthly management reviews of large credit exposures and credits experiencing deterioration of credit quality. Lending officers with the authority to extend credit are delegated specific authority amounts, the utilization of which is closely monitored. Lending activities are largely decentralized, while the Enterprise Risk Management division manages the policy process centrally. The Credit Risk Review function, within the Enterprise Risk Management division, provides objective assessments of the quality of underwriting and documentation, the accuracy of risk grades and the charge-off and reserve analysis process.

The Registrant's credit review process and overall assessment of required allowances is based on quarterly assessments of the probable estimated losses inherent in the loan and lease portfolio. The Registrant uses these assessments to promptly identify potential problem loans or leases within the portfolio, maintain an adequate allowance and take any necessary charge-offs. In addition to the individual review of larger commercial loans that exhibit probable or observed credit weakness, the commercial credit review process includes the use of two risk grading systems. The risk grading system currently utilized for allowance analysis purposes encompasses 10 categories. The Registrant also maintains a dual risk grading system that provides for 13 probability of default grade categories and an additional six grade categories for estimating actual losses given an event of default. The probability of default and estimated loss given default evaluations are not separated in the 10-grade risk rating system. The Registrant is in the process of completing significant validation and testing of the dual risk rating system prior to implementation for

**Table of Contents****Quantitative and Qualitative Disclosure about Market Risk (continued)**

allowance analysis purposes. The dual risk rating system is consistent with Basel II expectations and allows for more precision in the analysis of commercial credit risk. Scoring systems and delinquency monitoring are used to assess the credit risk in the Registrant's homogenous consumer loan portfolios.

**Portfolio Diversity**

The Registrant's credit risk management strategy includes minimizing concentrations of risk through diversification. The following table provides breakouts of the commercial loan and lease portfolio, including held for sale, by major industry classification, by loan size and by state, illustrating the diversity and granularity of the Registrant's portfolio.

**TABLE 23: Commercial Loan and Lease Portfolio (a)**

| As of June 30 (\$ in millions)   | Outstanding | 2006<br>Exposure | Nonaccrual | Outstanding | 2005<br>Exposure | Nonaccrual |
|----------------------------------|-------------|------------------|------------|-------------|------------------|------------|
| By industry:                     |             |                  |            |             |                  |            |
| Real estate                      | \$ 10,029   | 12,433           | 31         | 8,957       | 10,826           | 29         |
| Construction                     | 5,403       | 8,961            | 42         | 4,538       | 7,232            | 49         |
| Manufacturing                    | 4,805       | 10,507           | 33         | 4,311       | 9,366            | 38         |
| Retail trade                     | 3,701       | 6,244            | 11         | 3,298       | 5,466            | 18         |
| Transportation and warehousing   | 1,945       | 2,280            | 6          | 1,512       | 1,797            | 7          |
| Business services                | 1,927       | 3,536            | 10         | 1,892       | 3,413            | 23         |
| Wholesale trade                  | 1,906       | 3,574            | 15         | 1,787       | 3,272            | 8          |
| Healthcare                       | 1,702       | 2,967            | 8          | 1,545       | 2,682            | 6          |
| Individuals                      | 1,629       | 2,157            | 12         | 1,871       | 2,393            | 10         |
| Financial services and insurance | 1,173       | 3,853            | 4          | 961         | 2,810            | 1          |
| Other services                   | 968         | 1,323            | 15         | 899         | 1,214            | 7          |
| Other                            | 958         | 1,425            | 4          | 745         | 1,114            |            |
| Accommodation and food           | 896         | 1,318            | 10         | 1,015       | 1,438            | 8          |
| Public administration            | 815         | 992              |            | 812         | 951              |            |
| Communication and information    | 617         | 1,234            | 3          | 530         | 1,146            | 1          |
| Agribusiness                     | 576         | 803              | 1          | 537         | 825              | 4          |
| Entertainment and recreation     | 539         | 761              | 1          | 502         | 696              | 3          |
| Utilities                        | 296         | 1,082            |            | 275         | 812              |            |
| Mining                           | 215         | 408              | 3          | 248         | 417              |            |
| Total                            | \$ 40,100   | 65,858           | 209        | 36,235      | 57,870           | 212        |
| By loan size:                    |             |                  |            |             |                  |            |
| Less than \$200,000              | 5%          | 4                | 16         | 6           | 4                | 19         |
| \$200,000 to \$1 million         | 18          | 13               | 30         | 20          | 15               | 39         |
| \$1 million to \$5 million       | 32          | 27               | 40         | 35          | 30               | 32         |
| \$5 million to \$10 million      | 18          | 16               | 14         | 17          | 16               | 10         |
| \$10 million to \$25 million     | 20          | 24               |            | 17          | 23               |            |
| Greater than \$25 million        | 7           | 16               |            | 5           | 12               |            |
| Total                            | 100%        | 100              | 100        | 100         | 100              | 100        |
| By state:                        |             |                  |            |             |                  |            |
| Ohio                             | 24%         | 28               | 36         | 28          | 31               | 35         |
| Michigan                         | 22          | 20               | 20         | 23          | 21               | 26         |

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|                  |      |     |     |     |     |     |
|------------------|------|-----|-----|-----|-----|-----|
| Indiana          | 10   | 9   | 18  | 10  | 10  | 10  |
| Illinois         | 10   | 10  | 11  | 10  | 10  | 11  |
| Florida          | 10   | 9   | 6   | 9   | 8   | 3   |
| Kentucky         | 6    | 6   | 6   | 6   | 6   | 7   |
| Tennessee        | 3    | 3   | 2   | 2   | 2   | 3   |
| Pennsylvania     | 1    | 2   |     | 1   | 1   |     |
| West Virginia    | 1    |     |     |     |     | 1   |
| Out-of-footprint | 13   | 13  | 1   | 11  | 11  | 4   |
| Total            | 100% | 100 | 100 | 100 | 100 | 100 |

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(a) *Outstanding reflects total commercial customer loan and lease balances, including held for sale and net of unearned income, and exposure reflects total commercial customer lending commitments.*

**Table of Contents****Quantitative and Qualitative Disclosure about Market Risk (continued)**

The commercial portfolio is further characterized by 87% of outstanding balances and exposures concentrated within the Registrant's primary market areas of Ohio, Kentucky, Indiana, Michigan, Illinois, Florida, Tennessee, West Virginia and Pennsylvania. Exclusive of a national large-ticket leasing business, the commercial portfolio is characterized by 91% of exposures and 94% of outstanding balances concentrated within these nine states. The mortgage and construction segments of the commercial portfolio are characterized by 97% of exposures and outstanding balances concentrated within these nine states.

**Analysis of Nonperforming Assets**

Nonperforming assets include: (i) nonaccrual loans and leases on which ultimate collectibility of the full amount of the principal and/or interest is uncertain; (ii) loans and leases that have been renegotiated to provide for a reduction or deferral of interest or principal because of deterioration in the financial position of the borrower and (iii) other assets, including other real estate owned and repossessed equipment. Loans are placed on nonaccrual status when the principal or interest is past due 90 days or more (unless the loan is both well secured and in process of collection) and payment of the full principal and/or interest under the contractual terms of the loan are not expected. Additionally, loans are placed on nonaccrual status upon deterioration of the financial condition of the borrower. When a loan is placed on nonaccrual status, the accrual of interest, amortization of loan premium, accretion of loan discount and amortization or accretion of deferred net loan fees or costs are discontinued. Commercial loans on nonaccrual status are reviewed for impairment at least quarterly. If the principal or a portion of principal is deemed a loss, the loss amount is charged off to the allowance for loan and lease losses.

Total nonperforming assets were \$358 million at June 30, 2006, compared to \$361 million at December 31, 2005 and \$340 million at June 30, 2005. Nonperforming assets as a percent of total loans, leases and other assets, including other real estate owned was .49% as of June 30, 2006 compared to .52% as of December 31, 2005 and .51% as of June 30, 2005. Commercial nonaccrual credits as a percent of loans decreased since the second quarter of 2005, from .59% to .52%. Consumer nonaccrual credits as a percent of loans increased slightly since the second quarter of 2005, from .20% to .22%. Overall, nonaccrual credits continue to represent a small portion of the portfolio at just .38% as of June 30, 2006, compared to .41% as of June 30, 2005. Total loans and leases 90 days past due have increased from \$129 million as of June 30, 2005 to \$191 million as of June 30, 2006, with the increase driven primarily from the commercial component.

**TABLE 24: Summary of Nonperforming Assets and Delinquent Loans**

| (\$ in millions)                                | June 30,<br>2006 | December 31,<br>2005 | June 30,<br>2005 |
|-------------------------------------------------|------------------|----------------------|------------------|
| Commercial loans and leases                     | \$ 129           | 145                  | 132              |
| Commercial mortgages                            | 62               | 51                   | 56               |
| Commercial construction                         | 18               | 31                   | 24               |
| Residential mortgage and construction           | 34               | 30                   | 25               |
| Consumer loans and leases                       | 38               | 37                   | 36               |
| Total nonaccrual loans and leases               | 281              | 294                  | 273              |
| Renegotiated loans and leases                   |                  |                      | 1                |
| Other assets, including other real estate owned | 77               | 67                   | 66               |
| Total nonperforming assets                      | \$ 358           | 361                  | 340              |
| Commercial loans and leases                     | \$ 50            | 21                   | 24               |
| Commercial mortgages                            | 16               | 8                    | 7                |
| Commercial construction                         | 6                | 6                    | 3                |
| Credit card receivables                         | 13               | 10                   | 10               |
| Residential mortgage and construction (a)       | 58               | 53                   | 44               |
| Consumer loans and leases                       | 48               | 57                   | 41               |
| Total 90 days past due loans and leases         | \$ 191           | 155                  | 129              |

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|                                                                                                              |             |     |     |
|--------------------------------------------------------------------------------------------------------------|-------------|-----|-----|
| Nonperforming assets as a percent of total loans, leases and other assets, including other real estate owned | <b>.49%</b> | .52 | .51 |
| Allowance for loan and lease losses as a percent of total nonperforming assets                               | <b>210</b>  | 206 | 212 |

(a) *Information for all periods presented excludes advances made pursuant to servicing agreements to Government National Mortgage Association ( GNMA ) mortgage pools whose repayments are insured by the Federal Housing Administration or guaranteed by the Department of Veterans Affairs. These advances were \$10 million as of June 30, 2006 and \$13 million as of December 31, 2005 and June 30, 2005.*

**Table of Contents****Quantitative and Qualitative Disclosure about Market Risk (continued)****Analysis of Net Loan Charge-offs**

The table below provides a summary of credit loss experience and net charge-offs as a percentage of average loans and leases outstanding by loan category:

**TABLE 25: Summary of Credit Loss Experience**

|                                                                                     | For the three months   |       | For the six months     |       |
|-------------------------------------------------------------------------------------|------------------------|-------|------------------------|-------|
|                                                                                     | ended June 30,<br>2006 | 2005  | ended June 30,<br>2006 | 2005  |
| (\$ in millions)                                                                    |                        |       |                        |       |
| Losses charged off:                                                                 |                        |       |                        |       |
| Commercial loans                                                                    | \$ (31)                | (24)  | (66)                   | (41)  |
| Commercial mortgage loans                                                           | (5)                    | (3)   | (8)                    | (5)   |
| Construction loans                                                                  | (3)                    |       | (3)                    | (1)   |
| Commercial lease financing                                                          | (2)                    |       | (2)                    | (9)   |
| Residential mortgage loans                                                          | (6)                    | (5)   | (10)                   | (9)   |
| Consumer loans                                                                      | (46)                   | (40)  | (96)                   | (82)  |
| Consumer lease financing                                                            | (3)                    | (4)   | (8)                    | (9)   |
| Total losses                                                                        | (96)                   | (76)  | (193)                  | (156) |
| Recoveries of losses previously charged off:                                        |                        |       |                        |       |
| Commercial loans                                                                    | 9                      | 6     | 12                     | 9     |
| Commercial mortgage loans                                                           | 1                      | 1     | 1                      | 3     |
| Construction loans                                                                  |                        |       |                        | 1     |
| Commercial lease financing                                                          | 1                      | 1     | 3                      | 1     |
| Residential mortgage loans                                                          |                        |       |                        |       |
| Consumer loans                                                                      | 16                     | 12    | 31                     | 22    |
| Consumer lease financing                                                            | 2                      | 1     | 6                      | 2     |
| Total recoveries                                                                    | 29                     | 21    | 53                     | 38    |
| Net losses charged off:                                                             |                        |       |                        |       |
| Commercial loans                                                                    | (22)                   | (18)  | (54)                   | (32)  |
| Commercial mortgage loans                                                           | (4)                    | (2)   | (7)                    | (2)   |
| Construction loans                                                                  | (3)                    |       | (3)                    |       |
| Commercial lease financing                                                          | (1)                    | 1     | 1                      | (8)   |
| Residential mortgage loans                                                          | (6)                    | (5)   | (10)                   | (9)   |
| Consumer loans                                                                      | (30)                   | (28)  | (65)                   | (60)  |
| Consumer lease financing                                                            | (1)                    | (3)   | (2)                    | (7)   |
| Total net losses charged off                                                        | \$ (67)                | (55)  | (140)                  | (118) |
| Net charge-offs as a percent of average loans and leases (excluding held for sale): |                        |       |                        |       |
| Commercial loans                                                                    | .44%                   | .41   | .54                    | .36   |
| Commercial mortgage loans                                                           | .18                    | .07   | .14                    | .05   |
| Construction loans                                                                  | .16                    | .02   | .08                    |       |
| Commercial lease financing                                                          | .03                    | (.03) | (.04)                  | .48   |
| Residential mortgage loans                                                          | .24                    | .24   | .26                    | .24   |
| Consumer loans                                                                      | .57                    | .56   | .60                    | .61   |
| Consumer lease financing                                                            | .30                    | .55   | .27                    | .79   |

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|                              |            |     |            |     |
|------------------------------|------------|-----|------------|-----|
| Total net losses charged off | <b>.37</b> | .34 | <b>.40</b> | .37 |
|------------------------------|------------|-----|------------|-----|

Net charge-offs as a percent of average loans and leases outstanding increased by 3 bp over the second quarter of 2005, to .37% for the second quarter of 2006, and decreased by 5 bp from last quarter. The increase in net charge-offs during the second quarter is partially a result of \$6 million in losses realized from the sale of approximately \$38 million in nonaccrual loans and leases during the quarter. The Registrant has experienced continued improvement in consumer lease financing net charge-off activity, with a decrease in the ratio of consumer lease financing net charge-offs to average consumer leases outstanding compared to the second quarter of 2005. The ratio of residential mortgage loan net charge-offs to average residential mortgage loans outstanding was stable compared to the second quarter of 2005.

**Table of Contents****Quantitative and Qualitative Disclosure about Market Risk (continued)****Allowance for Credit Losses**

The allowance for credit losses is comprised of the allowance for loan and lease losses and the reserve for unfunded commitments. The allowance for loan and lease losses provides coverage for probable losses in the loan and lease portfolio. The Registrant evaluates the allowance each quarter to determine its adequacy to cover inherent losses. In the current year, the Registrant has not substantively changed any material aspect to its overall approach in the determination of the allowance for loan and lease losses and there have been no material changes in assumptions or estimation techniques as compared to prior periods that impacted the determination of the current period allowance. The Registrant maintains a reserve for unfunded commitments to provide coverage for probable losses on credit facilities that have not been funded. The methodology used to determine the adequacy of the reserve for unfunded commitments is similar to the Registrant's methodology for determining the allowance for loan and lease losses. The provision for unfunded commitments is included in other noninterest expense on the Condensed Consolidated Statements of Income.

**TABLE 26: Changes in Allowance for Credit Losses**

| (\$ in millions)                     | For the three months   |      | For the six months     |       |
|--------------------------------------|------------------------|------|------------------------|-------|
|                                      | ended June 30,<br>2006 | 2005 | ended June 30,<br>2006 | 2005  |
| Allowance for loan and lease losses: |                        |      |                        |       |
| Beginning balance                    | \$ 749                 | 717  | 744                    | 713   |
| Net losses charged off               | (67)                   | (55) | (140)                  | (118) |
| Provision for loan and lease losses  | 71                     | 60   | 149                    | 127   |
| Ending balance                       | \$ 753                 | 722  | 753                    | 722   |
| Reserve for unfunded commitments:    |                        |      |                        |       |
| Beginning balance                    | \$ 69                  | 67   | 70                     | 72    |
| Provision for unfunded commitments   | 5                      | 4    | 4                      | (2)   |
| Acquisitions                         |                        |      |                        | 1     |
| Ending balance                       | \$ 74                  | 71   | 74                     | 71    |

The allowance for loan and lease losses at June 30, 2006 decreased to 1.04% of the total loan and lease portfolio compared to 1.09% at June 30, 2005 due to an overall improved assessment of inherent losses in the portfolio from the consideration of historical and anticipated loss rates.

**Residential Mortgage Portfolio**

Certain mortgage products have contractual features that may increase credit exposure to the Registrant in the event of a decline in housing prices. These types of mortgage products offered by the Registrant include high loan-to-value ( LTV ) ratios, multiple loans on the same collateral that when combined result in a high LTV ( 80/20 ) and interest-only loans. Table 27 provides the amount of these loans as a percent of the residential mortgage loans in the Registrant's portfolio and the delinquency rates of these loan products as of June 30, 2006 and 2005. Table 28 shows the Registrant's originations of these products for the three and six months ended June 30, 2006 and 2005. The Registrant does not currently originate mortgage loans that permit principal payment deferral or payments that are less than the accruing interest.

The Registrant also sells certain of these mortgage products in the secondary market with recourse. The outstanding balances and delinquency rates for these loans sold with recourse as of June 30, 2006 and 2005 were \$1.1 billion and 1.53% and \$614 million and 0.51%, respectively.

The Registrant manages credit risk in the mortgage portfolio through conservative underwriting and documentation standards and geographic and product diversification. The Registrant may also package and sell loans in the portfolio without recourse or may purchase mortgage

insurance for the loans sold in order to mitigate credit risk.

**TABLE 27: Residential Mortgage Outstandings**

| As of June 30 (\$ in millions)                  | 2006<br>Percent |          |                      | 2005<br>Percent |          |                      |
|-------------------------------------------------|-----------------|----------|----------------------|-----------------|----------|----------------------|
|                                                 | Balance         | of total | Delinquency<br>Ratio | Balance         | of total | Delinquency<br>Ratio |
| Greater than 80% LTV with no mortgage insurance | \$ 1,871        | 22%      | 3.23%                | \$ 2,267        | 29%      | 2.01%                |
| Interest-only                                   | 1,218           | 14       | .07                  | 636             | 8        |                      |
| Greater than 80% LTV and interest-only          | 554             | 6        | .39                  | 184             | 2        | 1.07                 |
| 80/20 loans                                     | 33              |          | .25                  | 123             | 2        |                      |

**Table of Contents****Quantitative and Qualitative Disclosure about Market Risk (continued)****TABLE 28: Residential Mortgage Originations**

|                                                 | 2006<br>Percent |          | 2005<br>Percent |          |
|-------------------------------------------------|-----------------|----------|-----------------|----------|
| (\$ in millions)                                | Balance         | of total | Balance         | of total |
| For the three months ended June 30:             |                 |          |                 |          |
| Greater than 80% LTV with no mortgage insurance | \$ 208          | 8%       | \$ 335          | 14%      |
| Interest-only                                   | 334             | 13       | 346             | 14       |
| Greater than 80% LTV and interest-only          | 52              | 2        | 118             | 5        |
| 80/20 loans                                     | 132             | 5        | 132             | 5        |
| For the six months ended June 30:               |                 |          |                 |          |
| Greater than 80% LTV with no mortgage insurance | 392             | 8        | 609             | 14       |
| Interest-only                                   | 614             | 13       | 591             | 13       |
| Greater than 80% LTV and interest-only          | 153             | 3        | 168             | 4        |
| 80/20 loans                                     | 232             | 5        | 211             | 5        |

**MARKET RISK MANAGEMENT**

Market risk arises from the potential for fluctuations in interest rates, foreign exchange rates and equity prices that may result in potential reduction in net income. Interest rate risk, a component of market risk, is the exposure to adverse changes in net interest income or financial position due to changes in interest rates. Management considers interest rate risk a prominent market risk in terms of its potential impact on earnings. Interest rate risk can occur for any one or more of the following reasons: (i) assets and liabilities may mature or reprice at different times; (ii) short-term and long-term market interest rates may change by different amounts or (iii) the remaining maturity of various assets or liabilities may shorten or lengthen as interest rates change. In addition to the direct impact of interest rate changes on net interest income, interest rates can indirectly impact earnings through their effect on loan demand, credit losses, mortgage origination fees, the value of servicing rights and other sources of the Registrant's earnings. Consistency of the Registrant's net interest income is largely dependent upon the effective management of interest rate risk.

**Net Interest Income Simulation Model**

The Registrant employs a variety of measurement techniques to identify and manage its interest rate risk, including the use of an earnings simulation model to analyze net interest income sensitivity to changing interest rates. The model is based on actual cash flows and repricing characteristics for all of the Registrant's financial instruments and incorporates market-based assumptions regarding the effect of changing interest rates on the prepayment rates of certain assets and liabilities. The model also includes senior management projections of the future volume and pricing of each of the product lines offered by the Registrant as well as other pertinent assumptions about the balance sheet. Actual results will differ from these simulated results due to timing, magnitude and frequency of interest rate changes as well as changes in market conditions and management strategies.

The Registrant's Asset Liability Risk Management Committee (ALCO), which includes senior management representatives and is accountable to the Risk and Compliance Committee of the Board of Directors, monitors and manages interest rate risk within Board approved policy limits. In addition to the risk management activities of ALCO, the Registrant has a Market Risk Management function as part of the Enterprise Risk Management Division that provides independent oversight of market risk activities. The Registrant's current interest rate risk policy limits are determined by measuring the anticipated change in net interest income over a 12-month and 24-month horizon assuming a 200 bp parallel increase or decrease in market interest rates. In accordance with the current policy, the rate movements occur over one year and are sustained thereafter.

The following table shows the Registrant's estimated earnings sensitivity profile on the asset and liability positions as of June 30, 2006:

**TABLE 29: Estimated Earnings Sensitivity Profile**

| Change in interest rates (bp) | Change in Net Interest Income (FTE) |           |
|-------------------------------|-------------------------------------|-----------|
|                               | 12 Months                           | 24 Months |
| + 200                         | (2.56)%                             | (5.57)    |
| + 100                         | (1.32)                              | (2.79)    |
| - 100                         | 1.65                                | 3.82      |
| - 200                         | 3.41                                | 5.51      |

**Table of Contents****Quantitative and Qualitative Disclosure about Market Risk (continued)****Market Value of Equity**

The Registrant also utilizes the market value of equity ( MVE ) as a measurement tool in managing interest rate sensitivity. Whereas net interest income simulation highlights exposures over a relatively short time horizon, the MVE analysis incorporates all cash flows over the estimated remaining life of all balance sheet and derivative positions. The MVE of the balance sheet, at a point in time, is defined as the discounted value of asset and derivative cash flows less the discounted value of liability cash flows. The sensitivity of MVE to changes in the level of interest rates is a measure of the longer-term repricing risk. In contrast to the net interest income simulation, which assumes interest rates will change over a period of time, MVE uses instantaneous changes in rates. MVE values only the current balance sheet and does not incorporate the growth assumptions that are used in the net interest income simulation model. As with the net interest income simulation model, assumptions about the timing and variability of balance sheet cash flows are critical in the MVE analysis. Particularly important are the assumptions driving prepayments and the expected changes in balances and pricing of the transaction deposit portfolios. The following table shows the Registrant's MVE sensitivity profile as of June 30, 2006:

**TABLE 30: Estimated MVE Sensitivity Profile**

| Change in Interest Rates (bp) | Change in MVE |        |
|-------------------------------|---------------|--------|
|                               | 2006          | 2005   |
| +100                          | (5.19)%       | (3.34) |
| -100                          | 4.91          | 1.61   |

While an instantaneous shift in interest rates is used in this analysis to provide an estimate of exposure, the Registrant believes that a gradual shift in interest rates would have a much more modest impact. Since MVE measures the discounted present value of cash flows over the estimated lives of instruments, the change in MVE does not directly correlate to the degree that earnings would be impacted over a shorter time horizon (i.e., the current fiscal year). Further, MVE does not take into account factors such as future balance sheet growth, changes in product mix, changes in yield curve relationships and changing product spreads that could mitigate the adverse impact of changes in interest rates. The net interest income simulation and MVE analyses do not necessarily include certain actions that management may undertake to manage this risk in response to anticipated changes in interest rates.

**Use of Derivatives to Manage Interest Rate Risk**

An integral component of the Registrant's interest rate risk management strategy is its use of derivative instruments to minimize significant unplanned fluctuations in earnings and cash flows caused by market volatility. Examples of derivative instruments that the Registrant may use as part of its interest rate risk management strategy include interest rate swaps, interest rate floors, interest rate caps, forward contracts, principal only swaps, options and swaptions.

As part of its overall risk management strategy relative to its mortgage banking activity, the Registrant enters into forward contracts accounted for as free-standing derivatives to economically hedge interest rate lock commitments that are also considered free-standing derivatives.

The Registrant also establishes derivative contracts with reputable third parties to economically hedge significant exposures assumed in commercial customer accommodation derivative contracts. Generally, these contracts have similar terms in order to protect the Registrant from the market volatility. Credit risks arise from the possible inability of counterparties to meet the terms of their contracts, which the Registrant minimizes through approvals, limits and monitoring procedures. The notional amount and fair values of these derivatives as of June 30, 2006 are included in Note 5 to the Condensed Consolidated Financial Statements.

**Portfolio Loans and Leases and Interest Rate Risk**

Although the Registrant's portfolio loans and leases contain both fixed and floating/adjustable rate loan and lease products, the rates of interest earned by the Registrant on the outstanding balances are generally established for a period of time. The interest rate sensitivity of loans and leases is directly related to the length of time the rate earned is established. The following table summarizes the expected principal cash flows of the Registrant's portfolio loans and leases as of June 30, 2006:

**TABLE 31: Portfolio Loan and Lease Principal Cash Flows**

|                                             | Less than | 1 5    | Greater than |        |
|---------------------------------------------|-----------|--------|--------------|--------|
| (\$ in millions)                            | 1 year    | years  | 5 years      | Total  |
| Commercial loans                            | \$ 11,917 | 7,294  | 1,407        | 20,618 |
| Commercial mortgage loans                   | 3,111     | 5,246  | 1,435        | 9,792  |
| Commercial construction loans               | 3,986     | 1,702  | 262          | 5,950  |
| Commercial lease financing                  | 1,061     | 1,812  | 867          | 3,740  |
| Residential mortgage and construction loans | 2,296     | 3,850  | 2,477        | 8,623  |
| Consumer loans                              | 5,895     | 11,887 | 4,774        | 22,556 |
| Consumer lease financing                    | 506       | 786    | 6            | 1,298  |
| Total                                       | \$ 28,772 | 32,577 | 11,228       | 72,577 |

**Table of Contents****Quantitative and Qualitative Disclosure about Market Risk (continued)**

Segregated by interest rate type, the following is a summary of expected principal cash flows occurring after one year as of June 30, 2006:

**TABLE 32: Portfolio Loan and Lease Principal Cash Flows Occurring After One Year**

| (\$ in millions)                            | Interest Rate<br>Floating or |            |
|---------------------------------------------|------------------------------|------------|
|                                             | Fixed                        | Adjustable |
| Commercial loans                            | \$ 2,610                     | 6,091      |
| Commercial mortgage loans                   | 2,310                        | 4,371      |
| Commercial construction loans               | 300                          | 1,664      |
| Commercial lease financing                  | 2,679                        |            |
| Residential mortgage and construction loans | 3,154                        | 3,173      |
| Consumer loans                              | 7,431                        | 9,230      |
| Consumer lease financing                    | 792                          |            |
| Total                                       | \$ 19,276                    | 24,529     |

**Mortgage Servicing Rights and Interest Rate Risk**

The net carrying amount of the MSR portfolio was \$483 million as of June 30, 2006. The Registrant maintains a non-qualifying hedging strategy relative to its mortgage banking activity, including consultation with an independent third-party specialist, in order to manage a portion of the risk associated with changes in value of its MSR portfolio as a result of changing interest rates. The value of servicing rights can fluctuate sharply depending on changes in interest rates and other factors. Generally, as interest rates decline and loans are prepaid to take advantage of refinancing, the total value of existing servicing rights declines because no further servicing fees are collected on repaid loans.

The increase in interest rates during the second quarter of 2006 and the resulting impact of changing prepayment speeds led to the recovery of \$6 million of temporary impairment in the MSR portfolio compared to the recognition of \$21 million in temporary impairment in the second quarter of 2005. See Note 4 of the Notes to the Condensed Consolidated Financial Statements for further discussion on servicing rights.

**Foreign Currency Risk**

The Registrant enters into foreign exchange derivative contracts to economically hedge certain foreign denominated loans. The derivatives are classified as free-standing instruments with the revaluation gain or loss being recorded within other noninterest income on the Condensed Consolidated Statements of Income. The balance of the Registrant's foreign denominated loans at June 30, 2006 was approximately \$149 million. The Registrant also enters into foreign exchange derivative contracts for the benefit of commercial customers involved in international trade to hedge their exposure to foreign currency fluctuations. The Registrant has several controls in place to ensure excessive risk is not being taken in providing this service to customers. These include an independent determination of currency volatility and credit equivalent exposure on these contracts, counterparty credit approvals and country limits.

**LIQUIDITY RISK MANAGEMENT**

The goal of liquidity management is to provide adequate funds to meet changes in loan and lease demand or unexpected deposit withdrawals. This goal is accomplished by maintaining liquid assets in the form of investment securities, maintaining sufficient unused borrowing capacity in the national money markets and delivering consistent growth in core deposits. The primary source of asset-driven liquidity is provided by debt securities in the available-for-sale securities portfolio. The estimated average life of the available-for-sale portfolio is 4.8 years at June 30, 2006, based on current prepayment expectations. Of the \$20.3 billion (fair value basis) of securities in the available-for-sale portfolio at June 30, 2006, \$3.3 billion in principal and interest is expected to be received in the next 12 months, and an additional \$3.2 billion in principal and interest is expected to be received in the next 13 to 24 months. In addition to the sale of available-for-sale securities, asset-driven liquidity is provided by the Registrant's ability to sell or securitize loan and lease assets. In order to reduce the exposure to interest rate fluctuations and to manage

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liquidity, the Registrant has developed securitization and sale procedures for several types of interest-sensitive assets. A majority of the long-term, fixed-rate single-family residential mortgage loans underwritten according to FHLMC or Federal National Mortgage Association ( FNMA ) guidelines are sold for cash upon origination. Periodically, additional assets such as jumbo fixed-rate residential mortgages, certain floating-rate short-term commercial loans, certain floating-rate home equity loans, certain auto loans and other consumer loans are also securitized, sold or transferred off-balance sheet. For the six months ended June 30, 2006 and 2005, a total of \$4.7 billion and \$4.9 billion, respectively, were sold, securitized or transferred off-balance sheet.

Additionally, the Registrant has a shelf registration in place with the Securities and Exchange Commission permitting ready access to the public debt markets. As of June 30, 2006, \$1.5 billion of debt or other securities were available for issuance under this shelf registration. Additionally, the Registrant also has \$14.6 billion of funding available for issuance through private offerings of debt securities pursuant to its bank note program. These sources, in addition to the Registrant's 9.09% average equity capital base, provide a stable funding base.

**Table of Contents****Quantitative and Qualitative Disclosure about Market Risk (continued)**

Core deposits have historically provided the Registrant with a sizeable source of relatively stable and low cost funds. The Registrant's average core deposits and shareholders' equity funded 66% of its average total assets during the second quarter of 2006. In addition to core deposit funding, the Registrant also accesses a variety of other short-term and long-term funding sources, which include the use of various regional Federal Home Loan Banks as a funding source. Management does not rely on any one source of liquidity and manages availability in response to changing balance sheet needs.

**CAPITAL MANAGEMENT**

The Registrant maintains a relatively high level of capital as a margin of safety for its depositors and shareholders. For the quarter ended June 30, 2006, average shareholders' equity was \$9.6 billion, which is up one percent and four percent compared to the quarters ended December 31, 2005 and June 30, 2005, respectively. Average shareholders' equity as a percentage of average assets for the three months ended June 30, 2006 was 9.09%. The FRB adopted quantitative measures that assign risk weightings to assets and off-balance sheet items and also define and set minimum regulatory capital requirements (risk-based capital ratios). The guidelines define well-capitalized ratios of Tier I, total risk-based capital and leverage as 6%, 10% and 5%, respectively. The Registrant exceeded these well-capitalized ratios at June 30, 2006 and 2005 and December 31, 2005. The Registrant expects to maintain these ratios above the well-capitalized levels throughout 2006.

**TABLE 33: Regulatory Capital**

|                            | June 30, | December 31, | June 30, |
|----------------------------|----------|--------------|----------|
| (\$ in millions)           | 2006     | 2005         | 2005     |
| Tier I capital             | \$ 8,670 | 8,209        | 7,783    |
| Total risk-based capital   | 10,617   | 10,240       | 9,914    |
| Risk-weighted assets       | 101,605  | 97,994       | 91,791   |
| Regulatory capital ratios: |          |              |          |
| Tier I capital             | 8.52%    | 8.38         | 8.48     |
| Total risk-based capital   | 10.45    | 10.45        | 10.80    |
| Tier I leverage            | 8.38     | 8.08         | 7.76     |

**Dividend Policy**

The Registrant's common stock dividend policy reflects its earnings outlook, desired payout ratios, the need to maintain adequate capital levels and alternative investment opportunities. The Registrant's quarterly dividend was \$.40 per share, an increase of five percent over the \$.38 per share declared in the first quarter of 2006 and an increase of 14% over the \$.35 per share declared in the second quarter of 2005.

**Stock Repurchase Program**

On January 18, 2005, the Registrant announced that its Board of Directors had authorized management to purchase 20 million shares of the Registrant's common stock through the open market or in any private transaction. The timing of the purchases and the exact number of shares to be purchased depends upon market conditions. The authorization does not include specific price targets or an expiration date. The Registrant's stock repurchase program is an important element of its capital planning activities and the Registrant views share repurchases as an effective means of delivering value to shareholders. The Registrant's second quarter of 2006 repurchases of common shares were as follows:

**TABLE 34: Share Repurchases**

| Period | Total Number of<br>Shares<br>Purchased (a) | Average<br>Price Paid<br>Per<br>Share | Total Number of Shares<br>Purchased as Part of<br>Publicly Announced Plans<br>or Programs | Maximum Number of |
|--------|--------------------------------------------|---------------------------------------|-------------------------------------------------------------------------------------------|-------------------|
|--------|--------------------------------------------|---------------------------------------|-------------------------------------------------------------------------------------------|-------------------|

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|               |                |        |          | Shares that May Yet<br>Be Purchased Under the Plans<br>or Programs |
|---------------|----------------|--------|----------|--------------------------------------------------------------------|
| April 1, 2006 | April 30, 2006 | 39,806 | \$ 38.43 | 17,846,953                                                         |
| May 1, 2006   | May 31, 2006   | 29,309 | 39.50    | 17,846,953                                                         |
| June 1, 2006  | June 30, 2006  | 26,372 | 37.83    | 17,846,953                                                         |
| Total         |                | 95,487 | \$ 38.59 | 17,846,953                                                         |

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(a) *The Registrant repurchased 39,806, 29,309 and 26,372 shares during April, May and June, respectively, in connection with various employee compensation plans. These purchases are not included against the maximum number of shares that may yet be purchased under the Board of Directors' authorization.*

**Table of Contents****Quantitative and Qualitative Disclosure about Market Risk (continued)****OFF-BALANCE SHEET ARRANGEMENTS**

The Registrant consolidates all of its majority-owned subsidiaries. Other entities, including certain joint ventures, in which there is greater than 20% ownership, but upon which the Registrant does not possess, nor can exert, significant influence or control, are accounted for by equity method accounting and not consolidated. Those entities in which there is less than 20% ownership are generally carried at the lower of cost or fair value.

The Registrant does not participate in any trading activities involving commodity contracts that are accounted for at fair value. In addition, the Registrant has no material contracts for which a lack of marketplace quotations necessitates the use of fair value estimation techniques. The Registrant's derivative product policy and investment policies provide a framework within which the Registrant and its affiliates may use certain authorized financial derivatives as a market risk management tool in meeting the Registrant's ALCO capital planning directives, to hedge changes in fair value of its largely fixed rate mortgage servicing rights portfolio or to provide qualifying commercial customers access to the derivative products market. These policies are reviewed and approved annually by the Audit Committee and the Risk and Compliance Committee of the Board of Directors.

Through June 30, 2006, the Registrant had transferred, subject to credit recourse, certain primarily floating-rate, short-term, investment grade commercial loans to an unconsolidated QSPE that is wholly owned by an independent third-party. The outstanding balance of such loans at June 30, 2006 was \$3.4 billion. These loans may be transferred back to the Registrant upon the occurrence of an event specified in the legal documents that established the QSPE. These events include borrower default on the loans transferred, bankruptcy preferences initiated against underlying borrowers and ineligible loans transferred by the Registrant to the QSPE. The maximum amount of credit risk in the event of nonperformance by the underlying borrowers is approximately equivalent to the total outstanding balance of \$3.4 billion at June 30, 2006. In addition, the Registrant's agreement to provide liquidity support to the QSPE increased to \$3.8 billion as of June 30, 2006. At June 30, 2006, the Registrant's loss reserve related to the liquidity support and credit enhancement provided to the QSPE was \$13 million.

The Registrant utilizes securitization trusts formed by independent third parties to facilitate the securitization process of residential mortgage loans, certain floating-rate home equity lines of credit, certain auto loans and other consumer loans. The cash flows to and from the securitization trusts are principally limited to the initial proceeds from the securitization trust at the time of sale with subsequent cash flows relating to retained interests. The Registrant's securitization policy permits the retention of subordinated tranches, servicing rights, interest-only strips, residual interests, credit recourse, other residual interests and, in some cases, a cash reserve account. At June 30, 2006, the Registrant had retained servicing assets totaling \$489 million, subordinated tranche security interests totaling \$23 million and residual interests totaling \$30 million.

The Registrant had the following cash flows with these unconsolidated QSPEs:

**TABLE 35: Cash Flows with Unconsolidated QSPEs**

| <b>For the six months ended June 30 (\$ in millions)</b>                 | <b>2006</b>   | <b>2005</b> |
|--------------------------------------------------------------------------|---------------|-------------|
| Proceeds from transfers, including new securitizations                   | <b>\$ 982</b> | 744         |
| Proceeds from collections reinvested in revolving-period securitizations | <b>51</b>     | 67          |
| Transfers received from QSPEs                                            |               |             |
| Fees received                                                            | <b>17</b>     | 16          |

As of June 30, 2006, the Registrant had provided credit recourse on approximately \$1.3 billion of residential mortgage loans sold to unrelated third parties. In the event of any customer default, pursuant to the credit recourse provided, the Registrant is required to reimburse the third party. The maximum amount of credit risk in the event of nonperformance by the underlying borrowers is equivalent to the total outstanding balance of \$1.3 billion. In the event of nonperformance, the Registrant has rights to the underlying collateral value attached to the loan. Consistent with its overall approach in estimating credit losses for various categories of residential mortgage loans held in its loan portfolio, the Registrant maintains an estimated credit loss reserve of \$19 million relating to these residential mortgage loans sold.



**Table of Contents****Quantitative and Qualitative Disclosure about Market Risk (continued)****CONTRACTUAL OBLIGATIONS AND COMMITMENTS**

The Registrant has certain obligations and commitments to make future payments under contracts. At June 30, 2006, the aggregate contractual obligations and commitments were:

**TABLE 36: Contractual Obligations and Other Commitments**

|                                                      | Greater than        |              |              |         |        |
|------------------------------------------------------|---------------------|--------------|--------------|---------|--------|
| As of June 30, 2006 (\$ in millions)                 | Less than<br>1 year | 1-3<br>years | 3-5<br>years | 5 years | Total  |
| Contractually obligated payments due by period:      |                     |              |              |         |        |
| Total deposits                                       | \$ 67,318           | 940          | 59           | 2,206   | 70,523 |
| Long-term debt (a)                                   | 3,800               | 3,035        | 2,657        | 5,010   | 14,502 |
| Short-term borrowings (b)                            | 7,768               |              |              |         | 7,768  |
| Noncancelable leases                                 | 68                  | 127          | 107          | 329     | 631    |
| Partnership investment commitments (c)               | 163                 |              |              |         | 163    |
| Purchase obligations                                 | 14                  | 13           |              |         | 27     |
| Total contractually obligated payments due by period | \$ 79,131           | 4,115        | 2,823        | 7,545   | 93,614 |
| Other commitments by expiration period:              |                     |              |              |         |        |
| Letters of credit (d)                                | \$ 2,442            | 3,283        | 1,752        | 433     | 7,910  |
| Commitments to extend credit (e)                     | 22,374              | 17,032       |              |         | 39,406 |
| Total other commitments by expiration period         | \$ 24,816           | 20,315       | 1,752        | 433     | 47,316 |

- (a) Includes borrowings with an original maturity of greater than one year. For additional information, see the Borrowings discussion in the Balance Sheet Analysis section of Management's Discussion and Analysis.
- (b) Includes federal funds purchased, bank notes, securities sold under repurchase agreements and borrowings with an original maturity of less than one year. For additional information, see the Borrowings discussion in the Balance Sheet Analysis section of Management's Discussion and Analysis.
- (c) Includes low-income housing, historic and new market tax credit investments.
- (d) Letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party.
- (e) Commitments to extend credit are agreements to lend, typically having fixed expiration dates or other termination clauses that may require payment of a fee. Many of the commitments to extend credit may expire without being drawn upon. The total commitment amounts do not necessarily represent future cash flow requirements.

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### **Controls and Procedures (Item 4)**

The Registrant maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Registrant's Securities Exchange Act of 1934 ( "Exchange Act" ) reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to the Registrant's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure based closely on the definition of "disclosure controls and procedures" in Exchange Act Rules 13a-15(e) and 15d-15(e). In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As of the end of the period covered by this report, the Registrant carried out an evaluation, under the supervision and with the participation of the Registrant's management, including the Registrant's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Registrant's disclosure controls and procedures. Based on the foregoing, the Registrant's Chief Executive Officer and Chief Financial Officer concluded that the Registrant's disclosure controls and procedures were effective, in all material respects, to ensure that information required to be disclosed in the reports the Registrant files and submits under the Exchange Act is recorded, processed, summarized and reported as and when required.

The Registrant's management also conducted an evaluation of internal control over financial reporting to determine whether any changes occurred during the quarter covered by this report that have materially affected, or are reasonably likely to materially affect, the Registrant's internal control over financial reporting. Based on this evaluation, there has been no such change during the quarter covered by this report.

**Table of Contents****Fifth Third Bancorp and Subsidiaries****Condensed Consolidated Financial Statements and Notes (Item 1)****Condensed Consolidated Balance Sheets (unaudited)**

| (\$ in millions, except share data)         | June 30,<br>2006  | As of<br>December 31,<br>2005 | June 30,<br>2005 |
|---------------------------------------------|-------------------|-------------------------------|------------------|
| <b>Assets</b>                               |                   |                               |                  |
| Cash and due from banks                     | \$ 2,670          | 3,078                         | 2,781            |
| Available-for-sale and other securities (a) | 20,345            | 21,924                        | 24,647           |
| Held-to-maturity securities (b)             | 358               | 389                           | 307              |
| Trading securities                          | 173               | 117                           | 84               |
| Other short-term investments                | 207               | 158                           | 113              |
| Loans held for sale                         | 931               | 1,304                         | 783              |
| Portfolio loans and leases:                 |                   |                               |                  |
| Commercial loans                            | 20,618            | 19,174                        | 18,013           |
| Construction loans                          | 6,698             | 7,037                         | 6,201            |
| Commercial mortgage loans                   | 9,792             | 9,188                         | 9,091            |
| Commercial lease financing                  | 4,899             | 4,852                         | 4,639            |
| Residential mortgage loans                  | 7,875             | 7,152                         | 7,042            |
| Consumer loans                              | 22,556            | 22,084                        | 20,610           |
| Consumer lease financing                    | 1,420             | 1,751                         | 1,994            |
| Unearned income                             | (1,281)           | (1,313)                       | (1,294)          |
| Total portfolio loans and leases            | 72,577            | 69,925                        | 66,296           |
| Allowance for loan and lease losses         | (753)             | (744)                         | (722)            |
| Total portfolio loans and leases, net       | 71,824            | 69,181                        | 65,574           |
| Bank premises and equipment                 | 1,853             | 1,726                         | 1,581            |
| Operating lease equipment                   | 150               | 143                           | 161              |
| Goodwill                                    | 2,194             | 2,169                         | 2,178            |
| Intangible assets                           | 185               | 208                           | 231              |
| Servicing rights                            | 489               | 441                           | 378              |
| Other assets                                | 4,732             | 4,387                         | 4,342            |
| <b>Total Assets</b>                         | <b>\$ 106,111</b> | <b>105,225</b>                | <b>103,160</b>   |
| <b>Liabilities</b>                          |                   |                               |                  |
| Deposits:                                   |                   |                               |                  |
| Demand                                      | \$ 14,078         | 14,609                        | 14,393           |
| Interest checking                           | 16,788            | 18,282                        | 18,811           |
| Savings                                     | 12,061            | 11,276                        | 9,653            |
| Money market                                | 6,505             | 6,129                         | 4,732            |
| Other time                                  | 10,627            | 9,313                         | 8,513            |
| Certificates - \$100,000 and over           | 5,691             | 4,343                         | 3,986            |
| Foreign office                              | 4,773             | 3,482                         | 3,089            |
| Total deposits                              | 70,523            | 67,434                        | 63,177           |
| Federal funds purchased                     | 2,493             | 5,323                         | 4,523            |
| Other short-term borrowings                 | 5,275             | 4,246                         | 4,972            |

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|                                                   |                   |         |         |
|---------------------------------------------------|-------------------|---------|---------|
| Accrued taxes, interest and expenses              | 1,995             | 2,142   | 2,456   |
| Other liabilities                                 | 1,767             | 1,407   | 1,185   |
| Long-term debt                                    | 14,502            | 15,227  | 17,494  |
| <b>Total Liabilities</b>                          | <b>96,555</b>     | 95,779  | 93,807  |
| <b>Shareholders' Equity</b>                       |                   |         |         |
| Common stock (c)                                  | 1,295             | 1,295   | 1,295   |
| Preferred stock (d)                               | 9                 | 9       | 9       |
| Capital surplus                                   | 1,788             | 1,827   | 1,756   |
| Retained earnings                                 | 8,319             | 8,007   | 7,702   |
| Accumulated other comprehensive income            | (683)             | (413)   | (135)   |
| Treasury stock                                    | (1,172)           | (1,279) | (1,274) |
| <b>Total Shareholders' Equity</b>                 | <b>9,556</b>      | 9,446   | 9,353   |
| <b>Total Liabilities and Shareholders' Equity</b> | <b>\$ 106,111</b> | 105,225 | 103,160 |

- (a) Amortized cost: **June 30, 2006 - \$21,376**, December 31, 2005 - \$22,533 and June 30, 2005 - \$24,814.
- (b) Market values: **June 30, 2006 - \$358**, December 31, 2005 - \$389 and June 30, 2005 - \$307.
- (c) Common shares: Stated value \$2.22 per share; authorized 1,300,000,000; outstanding at **June 30, 2006 - 557,894,188 (excludes 25,532,916 treasury shares)**, December 31, 2005 - 555,623,430 (excludes 27,803,674 treasury shares) and June 30, 2005 - 555,938,071 (excludes 27,489,033 treasury shares).
- (d) 490,750 shares of undesignated no par value preferred stock are authorized of which none had been issued; 7,250 shares of 8.0% cumulative Series D convertible (at \$23.5399 per share) perpetual preferred stock with a stated value of \$1,000 per share were authorized, issued and outstanding; 2,000 shares of 8.0% cumulative Series E perpetual preferred stock with a stated value of \$1,000 per share were authorized, issued and outstanding.

**Table of Contents****Fifth Third Bancorp and Subsidiaries****Condensed Consolidated Financial Statements and Notes (continued)****Condensed Consolidated Statements of Income (unaudited)**

|                                                                      | For the three months   |       | For the six months     |       |
|----------------------------------------------------------------------|------------------------|-------|------------------------|-------|
|                                                                      | ended June 30,<br>2006 | 2005  | ended June 30,<br>2006 | 2005  |
| (\$ in millions, except per share data)                              |                        |       |                        |       |
| <b>Interest Income</b>                                               |                        |       |                        |       |
| Interest and fees on loans and leases                                | \$ 1,227               | 936   | 2,375                  | 1,803 |
| Interest on securities:                                              |                        |       |                        |       |
| Taxable                                                              | 239                    | 268   | 481                    | 534   |
| Exempt from income taxes                                             | 8                      | 10    | 16                     | 20    |
| Total interest on securities                                         | 247                    | 278   | 497                    | 554   |
| Interest on other short-term investments                             | 3                      | 1     | 4                      | 2     |
| Total interest income                                                | 1,477                  | 1,215 | 2,876                  | 2,359 |
| <b>Interest Expense</b>                                              |                        |       |                        |       |
| Interest on deposits:                                                |                        |       |                        |       |
| Interest checking                                                    | 102                    | 71    | 201                    | 134   |
| Savings                                                              | 87                     | 35    | 163                    | 61    |
| Money market                                                         | 64                     | 28    | 119                    | 53    |
| Other time                                                           | 105                    | 61    | 194                    | 113   |
| Certificates - \$100,000 and over                                    | 61                     | 29    | 109                    | 54    |
| Foreign office                                                       | 52                     | 29    | 96                     | 56    |
| Total interest on deposits                                           | 471                    | 253   | 882                    | 471   |
| Interest on federal funds purchased                                  | 48                     | 29    | 99                     | 54    |
| Interest on short-term bank notes                                    |                        | 2     |                        | 6     |
| Interest on other short-term borrowings                              | 52                     | 34    | 97                     | 61    |
| Interest on long-term debt                                           | 196                    | 147   | 377                    | 267   |
| Total interest expense                                               | 767                    | 465   | 1,455                  | 859   |
| <b>Net Interest Income</b>                                           | 710                    | 750   | 1,421                  | 1,500 |
| Provision for loan and lease losses                                  | 71                     | 60    | 149                    | 127   |
| <b>Net Interest Income After Provision for Loan and Lease Losses</b> | 639                    | 690   | 1,272                  | 1,373 |
| <b>Noninterest Income</b>                                            |                        |       |                        |       |
| Electronic payment processing revenue                                | 211                    | 183   | 407                    | 354   |
| Service charges on deposits                                          | 135                    | 132   | 261                    | 253   |
| Mortgage banking net revenue                                         | 41                     | 46    | 88                     | 87    |
| Investment advisory revenue                                          | 96                     | 92    | 187                    | 182   |
| Corporate banking revenue                                            | 82                     | 74    | 157                    | 136   |
| Other noninterest income                                             | 76                     | 93    | 157                    | 200   |
| Securities gains (losses), net                                       | 14                     | 15    | 15                     | 30    |
| Total noninterest income                                             | 655                    | 635   | 1,272                  | 1,242 |
| <b>Noninterest Expense</b>                                           |                        |       |                        |       |

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|                                                              |                |             |              |              |
|--------------------------------------------------------------|----------------|-------------|--------------|--------------|
| Salaries, wages and incentives                               | 303            | 295         | 586          | 561          |
| Employee benefits                                            | 69             | 67          | 156          | 148          |
| Equipment expense                                            | 29             | 25          | 56           | 50           |
| Net occupancy expense                                        | 59             | 54          | 118          | 108          |
| Other noninterest expense                                    | 299            | 287         | 574          | 565          |
| <b>Total noninterest expense</b>                             | <b>759</b>     | <b>728</b>  | <b>1,490</b> | <b>1,432</b> |
| <b>Income Before Income Taxes and Cumulative Effect</b>      | <b>535</b>     | <b>597</b>  | <b>1,054</b> | <b>1,183</b> |
| Applicable income taxes                                      | 153            | 180         | 312          | 361          |
| <b>Income Before Cumulative Effect</b>                       | <b>382</b>     | <b>417</b>  | <b>742</b>   | <b>822</b>   |
| Cumulative effect of change in accounting principle, net (a) |                |             | 4            |              |
| <b>Net Income</b>                                            | <b>\$ 382</b>  | <b>417</b>  | <b>746</b>   | <b>822</b>   |
| <b>Net Income Available to Common Shareholders (b)</b>       | <b>\$ 382</b>  | <b>417</b>  | <b>745</b>   | <b>821</b>   |
| <b>Earnings Per Share</b>                                    | <b>\$ 0.69</b> | <b>0.75</b> | <b>1.34</b>  | <b>1.48</b>  |
| <b>Earnings Per Diluted Share</b>                            | <b>\$ 0.69</b> | <b>0.75</b> | <b>1.34</b>  | <b>1.47</b>  |

- (a) Reflects a benefit of \$4 million (net of \$2 million of tax) for the adoption of SFAS No. 123(R) as of January 1, 2006 due to the recognition of an estimate of forfeiture experience to be realized for all unvested stock-based awards outstanding.
- (b) Dividends on Preferred Stock are \$.185 and \$.370 for the three and six month periods ended June 30, 2006 and 2005, respectively.

**Table of Contents****Fifth Third Bancorp and Subsidiaries****Condensed Consolidated Financial Statements and Notes (continued)****Condensed Consolidated Statements of Changes in Shareholders' Equity (unaudited)**

| (\$ in millions, except per share data)                                  | For the six months ended June 30, |              |
|--------------------------------------------------------------------------|-----------------------------------|--------------|
|                                                                          | 2006                              | 2005         |
| <b>Total shareholders' equity, beginning</b>                             | <b>\$ 9,446</b>                   | <b>8,924</b> |
| Net income                                                               | 746                               | 822          |
| Other comprehensive income, net of tax:                                  |                                   |              |
| Change in unrealized gains and (losses):                                 |                                   |              |
| Available-for-sale securities                                            | (275)                             | (59)         |
| Qualifying cash flow hedges                                              | 5                                 | 33           |
| Change in additional pension liability                                   |                                   | 60           |
| Comprehensive income                                                     | 476                               | 856          |
| Cash dividends declared:                                                 |                                   |              |
| Common stock (2006 - \$.78 per share and 2005 - \$.70 per share)         | (434)                             | (389)        |
| Preferred stock (a)                                                      |                                   |              |
| Stock-based awards exercised, including treasury shares issued           | 24                                | 40           |
| Impact of cumulative effect of change in accounting principle            | (6)                               |              |
| Stock-based compensation expense                                         | 44                                | 37           |
| Loans repaid (issued) related to the exercise of stock-based awards, net | 5                                 | 4            |
| Change in corporate tax benefit related to stock-based compensation      |                                   | 14           |
| Shares acquired for treasury                                             |                                   | (1,645)      |
| Shares issued in business combination                                    |                                   | 1,509        |
| Other                                                                    | 1                                 | 3            |
| <b>Total shareholders' equity, ending</b>                                | <b>\$ 9,556</b>                   | <b>9,353</b> |

(a) Dividends on preferred stock are \$.370 million for the six months ended June 30, 2006 and 2005, respectively.

**Table of Contents****Fifth Third Bancorp and Subsidiaries****Condensed Consolidated Financial Statements and Notes (continued)****Condensed Consolidated Statements of Cash Flows (unaudited)**

|                                                                                     | For the six months |                |
|-------------------------------------------------------------------------------------|--------------------|----------------|
|                                                                                     | ended June 30,     |                |
| (\$ in millions)                                                                    | 2006               | 2005           |
| <b>Operating Activities</b>                                                         |                    |                |
| Net income                                                                          | \$ 746             | 822            |
| Adjustments to reconcile net income to net cash provided by operating activities:   |                    |                |
| Provision for loan and lease losses                                                 | 149                | 127            |
| Depreciation, amortization and accretion                                            | 193                | 196            |
| Cumulative effect of change in accounting principle                                 | (4)                |                |
| Stock-based compensation expense                                                    | 44                 | 37             |
| (Benefit) provision for deferred income taxes                                       | (55)               | 34             |
| Realized securities gains                                                           | (27)               | (33)           |
| Realized securities losses                                                          | 12                 | 3              |
| Proceeds from sales/transfers of residential mortgage and other loans held for sale | 4,736              | 4,950          |
| Net gains on sales of loans                                                         | (65)               | (76)           |
| Increase in residential mortgage and other loans held for sale                      | (3,197)            | (3,439)        |
| Increase in trading securities                                                      | (56)               | (7)            |
| Increase in other assets                                                            | (317)              | (677)          |
| Increase in accrued taxes, interest and expenses                                    | 57                 | 136            |
| Increase in other liabilities                                                       | 139                | 170            |
| <b>Net Cash Provided by Operating Activities</b>                                    | <b>2,355</b>       | <b>2,243</b>   |
| <b>Investing Activities</b>                                                         |                    |                |
| Proceeds from sales of available-for-sale securities                                | 448                | 3,676          |
| Proceeds from calls, paydowns and maturities of available-for-sale securities       | 1,608              | 2,697          |
| Purchases of available-for-sale securities                                          | (894)              | (5,449)        |
| Proceeds from calls, paydowns and maturities of held-to-maturity securities         | 34                 | 33             |
| Purchases of held-to-maturity securities                                            | (2)                | (83)           |
| (Increase) decrease in other short-term investments                                 | (49)               | 448            |
| Increase in loans and leases                                                        | (3,896)            | (4,346)        |
| (Increase) decrease in operating lease equipment                                    | (17)               | 120            |
| Purchases of bank premises and equipment                                            | (247)              | (235)          |
| Proceeds from disposal of bank premises and equipment                               | 42                 | 37             |
| Net cash (paid) acquired in business combination                                    | (5)                | 242            |
| <b>Net Cash Used In Investing Activities</b>                                        | <b>(2,978)</b>     | <b>(2,860)</b> |
| <b>Financing Activities</b>                                                         |                    |                |
| Increase in core deposits                                                           | 449                | 367            |
| Increase in certificates - \$100,000 and over, including foreign office             | 2,640              | 741            |
| Decrease in federal funds purchased                                                 | (2,830)            | (669)          |
| Decrease in other short-term notes                                                  |                    | (775)          |
| Increase in short-term borrowings                                                   | 1,016              | 39             |
| Proceeds from issuance of long-term debt                                            | 1,834              | 3,662          |

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|                                                           |                 |              |
|-----------------------------------------------------------|-----------------|--------------|
| Repayment of long-term debt                               | (2,502)         | (554)        |
| Payment of cash dividends                                 | (422)           | (390)        |
| Exercise of stock-based awards, net                       | 29              | 44           |
| Purchases of treasury stock                               |                 | (1,645)      |
| Other                                                     | 1               | 17           |
| <b>Net Cash Provided by Financing Activities</b>          | <b>215</b>      | <b>837</b>   |
| <b>(Decrease) Increase in Cash and Due from Banks</b>     | <b>(408)</b>    | <b>220</b>   |
| <b>Cash and Due from Banks at Beginning of Period</b>     | <b>3,078</b>    | <b>2,561</b> |
| <b>Cash and Due from Banks at End of Period</b>           | <b>\$ 2,670</b> | <b>2,781</b> |
| <b>Cash Payments</b>                                      |                 |              |
| Interest                                                  | \$ 1,410        | 771          |
| Federal income taxes                                      | 314             | 201          |
| <b>Supplemental Cash Flow Information</b>                 |                 |              |
| Transfer from portfolio loans to loans held for sale, net | 1,104           | 1,659        |
| Business acquisitions:                                    |                 |              |
| Fair value of tangible assets acquired (noncash)          | 6               | 5,149        |
| Goodwill and identifiable intangible assets acquired      | 17              | 1,304        |
| Liabilities assumed and note issued                       | (18)            | (5,186)      |
| Stock options                                             |                 | (63)         |
| Common stock issued                                       |                 | (1,446)      |

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### **Notes to Condensed Consolidated Financial Statements (unaudited)**

#### **1. Basis of Presentation**

In the opinion of management, the unaudited Condensed Consolidated Financial Statements include all adjustments, which consist of normal recurring accruals, necessary to present fairly the financial position as of June 30, 2006 and 2005, the results of operations for the three and six months ended June 30, 2006 and 2005, the cash flows for the six months ended June 30, 2006 and 2005 and the changes in shareholders' equity for the six months ended June 30, 2006 and 2005. In accordance with accounting principles generally accepted in the United States of America for interim financial information, these statements do not include certain information and footnote disclosures required for complete annual financial statements. The results of operations for the three and six months ended June 30, 2006 and 2005 and the cash flows for the six months ended June 30, 2006 and 2005 are not necessarily indicative of the results to be expected for the full year. Financial information as of December 31, 2005 has been derived from the audited Consolidated Financial Statements of the Registrant included in the Annual Report on Form 10-K.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Certain reclassifications have been made to prior periods' Condensed Consolidated Financial Statements and related notes to conform with the current period presentation.

#### **2. New Accounting Pronouncements**

In December 2004, the FASB issued SFAS No. 123 (Revised 2004), *Share-Based Payment*. This Statement requires measurement of the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award with the cost to be recognized over the vesting period. This Statement was effective for financial statements as of the beginning of the first interim or annual reporting period of the first fiscal year beginning after June 15, 2005. On January 1, 2006, the Registrant elected to adopt this Statement using the modified retrospective application. Adoption of this Statement had three impacts on the Registrant's Condensed Consolidated Financial Statements: i) the recognition of a benefit for the cumulative effect of change in accounting principle of approximately \$4 million (net of \$2 million of tax) during the first quarter of 2006 due to the recognition of an estimate of forfeiture experience to be realized for all unvested stock-based awards outstanding; ii) the reclassification in the Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2005 of \$14 million of net cash provided related to the excess corporate tax benefit received on stock-based compensation, previously recorded in the operating activities section, to the financing activities section and iii) the recognition of approximately \$9 million of incremental salaries, wages and incentives expense in the second quarter of 2006 related to the issuance in April 2006 of stock-based awards to retirement-eligible employees. The adoption did not have an impact on basic or diluted earnings per share. For further information on stock-based compensation see Note 11.

In December 2003, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants issued Statement of Position (SOP) 03-3, *Accounting for Certain Loans and Debt Securities Acquired in a Transfer*. SOP 03-3 addresses the accounting for acquired loans that show evidence of having deteriorated in terms of credit quality since their origination (i.e. impaired loans) and for which a loss is deemed probable of occurring. SOP 03-3 requires acquired loans to be recorded at their fair value, defined as the present value of future cash flows including interest income, to be recognized over the life of the loan. SOP 03-3 prohibits the carryover of an allowance for loan loss on certain acquired loans within its scope considered in the future cash flows assessment. SOP 03-3 was effective for loans acquired in fiscal years beginning after December 15, 2004 and has not had a material effect on the Registrant's Condensed Consolidated Financial Statements.

In March 2004, the Emerging Issues Task Force (EITF) reached a consensus on Issue 03-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*. The EITF reached a consensus on an other-than-temporary impairment model for debt and equity securities accounted for under SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, and cost method investments. In September 2004, the FASB issued Staff Position (FSP) No. EITF 03-01-1, *Effective Date of Paragraphs 10-20 of EITF 03-01*. This FSP delayed the effective date of the measurement and recognition guidance contained in paragraphs 10-20 of Issue 03-01. In November 2005, the FASB issued FSP FAS 115-1 and FAS 124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*. This FSP nullifies certain requirements of Issue 03-1 and supersedes EITF Abstracts, Topic No. D-44, *Recognition of Other-Than-Temporary Impairment upon the Planned Sale of a Security Whose Cost Exceeds Fair Value*. Based on the clarification provided in FSP FAS 115-1 and FAS 124-1, the amount of any other-than-temporary impairment that needs to be recognized will continue to be dependent on market conditions, the occurrence of certain events or changes in circumstances relative to an investee and an entity's intent and ability to hold the impaired investment at the time of the valuation. FSP FAS 115-1 and FAS 124-1 was effective for reporting periods beginning after December 15, 2005. Adoption of this FSP did not have a material effect on the Registrant's Condensed Consolidated Financial Statements.

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In May 2005, the FASB issued SFAS No. 154, Accounting Changes and Error Corrections a Replacement of APB Opinion No. 20 and FASB Statement No. 3. This Statement replaces APB Opinion No. 20, Accounting Changes, and FASB Statement No. 3, Reporting Accounting Changes in Interim Financial Statements, and changes the requirements for the accounting for and reporting of a change in accounting principle. This Statement requires retrospective application to prior periods financial statements of changes in accounting principle, unless it is impracticable to determine either the period-specific effects or the

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### **Notes to Condensed Consolidated Financial Statements (continued)**

cumulative effect of the change. This Statement applies to all voluntary changes in accounting principle. It also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. This Statement is effective for accounting changes and error corrections made in fiscal years beginning after December 15, 2005. The adoption of this Statement did not have a material effect on the Registrant's Condensed Consolidated Financial Statements.

In August 2005, the FASB issued an Exposure Draft, *Accounting for Transfers of Financial Assets*, an amendment of FASB Statement No. 140. This Exposure Draft would amend FASB Statement No. 140 by addressing the criteria necessary for obtaining sales accounting on the transfer of all or a portion of financial assets as well as the requirements for qualification as a Qualified Special Purpose Entity (QSPE). The proposed changes to the criteria for obtaining sales accounting include a requirement that all arrangements or agreements, including those entered into subsequent to the sale, made in connection with the transfer of financial assets be considered in the determination of whether the financial assets were legally isolated from the transferor and its consolidated affiliates, the establishment of additional conditions for obtaining sales treatment on the transfer of a portion of a financial asset and the requirement that a transferee maintain the right to pledge or exchange the assets it receives and no condition exists that constrains the transferee from taking advantage of its right to pledge or exchange its assets, or provides more than a trivial benefit to the transferor. The proposed changes to the requirements for qualifying as a QSPE include prohibiting a QSPE from holding equity instruments, unless the equity instruments were received as a result of the efforts to collect its financial assets, as well as a requirement to evaluate whether a combination of involvements with a QSPE provide the holder of those involvements with an opportunity to obtain a more than trivial incremental benefit relative to the benefit that would be obtained if separate parties had those same involvements. In December 2005, the FASB announced the effective date of the Exposure Draft had been delayed. The final Statement is expected to be issued in the first quarter of 2007. Although the Registrant is still evaluating the potential impact of the Exposure Draft on its Condensed Consolidated Financial Statements, in its current form the Exposure Draft will require the consolidation of an unconsolidated QSPE that is wholly owned by an independent third-party, unless certain aspects of the current operational nature of the QSPE are modified. The outstanding balance of commercial loans transferred by the Registrant to the QSPE was approximately \$3.4 billion at June 30, 2006.

In February 2006, the FASB issued SFAS No. 155, *Accounting for Certain Hybrid Financial Instruments*, an amendment of FASB Statement No. 133 and 140. This Statement amends FASB Statements No. 133, *Accounting for Derivative Instruments and Hedging Activities*, and No. 140 as well as resolves issues addressed in Statement No. 133 Implementation Issue No. D1, *Application of Statement No. 133 to Beneficial Interests in Securitized Financial Assets*. Specifically, this Statement: i) permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation; ii) clarifies which interest-only strips and principal-only strips are not subject to the requirements of Statement No. 133; iii) establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation; iv) clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives; and v) amends Statement No. 140 to eliminate the prohibition on a qualifying SPE from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. This Statement is effective for all financial instruments acquired or issued after the beginning of the first fiscal year that begins after September 15, 2006. The adoption of this Statement is not expected to have a material effect on the Registrant's Condensed Consolidated Financial Statements.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets*, an amendment of FASB Statement No. 140. This Statement amends FASB Statement No. 140 and requires that all separately recognized servicing rights be initially measured at fair value, if practicable. For each class of separately recognized servicing assets and liabilities, this Statement permits the Registrant to choose either to report servicing assets and liabilities at fair value or at amortized cost. Under the fair value approach, servicing assets and liabilities will be recorded at fair value at each reporting date with changes in fair value recorded in earnings in the period in which the changes occur. Under the amortized cost method, servicing assets and liabilities are amortized in proportion to and over the period of estimated net servicing income or net servicing loss and are assessed for impairment based on fair value at each reporting date. This Statement is effective as of the beginning of the first fiscal year that begins after September 15, 2006. The Registrant is currently in the process of determining which methodology to use to value recognized servicing assets and liabilities and therefore has not yet determined the potential impact of the Statement on its Condensed Consolidated Financial Statements.

In July 2006, the FASB issued Staff Position (FSP) FAS 13-2, *Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction*. This Statement addresses the accounting for a change or projected change in the timing of lessor cash flows, but not the total net income, relating to income taxes generated by a leveraged lease transaction. This Statement amends SFAS No. 13, *Accounting for Leases*, and applies to all transactions classified as leveraged leases. The timing of cash flows relating to income taxes generated by a leveraged lease is an important assumption that affects the periodic income recognized by the lessor. Under this Statement, the projected timing of income tax cash flows generated by a leveraged lease transaction are required to be reviewed

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annually or more frequently if events or circumstances indicate that a change in timing has occurred or is projected to occur. If during the lease term the expected timing of the income tax cash flows generated by a leveraged lease is revised, the rate of return and the allocation of income would be recalculated from the

**Table of Contents****Notes to Condensed Consolidated Financial Statements (continued)**

inception of the lease. Upon adoption, the cumulative effect of the change in the net investment balance resulting from the recalculation will be recognized as an adjustment to the beginning balance of retained earnings. On an ongoing basis following the adoption, a change in the net investment balance resulting from a recalculation will be recognized as a gain or a loss in the period in which the assumption changed and included in income from continuing operations in the same line item used when leveraged lease income is recognized. These amounts would then be recognized back into income over the remaining terms of the affected leases. Additionally, upon adoption, only tax positions that meet the more-likely-than-not recognition threshold should be reflected in the financial statements and all recognized tax positions in a leveraged lease must be measured in accordance with FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109, issued in July 2006. During May 2005, the Registrant filed suit in the United States District Court for the Southern District of Ohio related to a dispute with the Internal Revenue Service concerning the timing of deductions associated with certain leveraged lease transactions in its 1997 tax return. The Internal Revenue Service has also proposed adjustments to the tax effects of certain leveraged lease transactions in subsequent tax return years. The proposed adjustments, including penalties, relate to the Registrant's portfolio of lease-in lease-out transactions, service contract leases and qualified technology equipment leases with both domestic and foreign municipalities. The Registrant is challenging the Internal Revenue Service's proposed treatment of all of these leasing transactions. The Registrant's original net investment in these leases totaled approximately \$900 million. The Registrant continues to believe that its treatment of these leveraged leases was appropriate and in compliance with applicable tax law and regulations. While management cannot predict with certainty the result of the suit, given the tax treatment of these transactions has been challenged by the Internal Revenue Service, the Registrant believes a resolution may involve a projected change in the timing of these leveraged lease cash flows. Accordingly, the Registrant is currently in the process of evaluating the potential impact on its Condensed Consolidated Financial Statements. This Statement is effective for fiscal years beginning after December 15, 2006.

In July 2006, the FASB issued Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109. This Statement clarifies the accounting for uncertainty in income taxes recognized in accordance with FASB Statement No. 109,

Accounting for Income Taxes. This Statement also prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Statement also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The evaluation of a tax position in accordance with this Statement is a two-step process. The first step is a recognition process to determine whether it is more likely than not that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The second step is a measurement process whereby a tax position that meets the more likely than not recognition threshold is calculated to determine the amount of benefit to recognize in the financial statements. This Statement is effective for fiscal years beginning after December 15, 2006 and the cumulative effect of applying the provisions of this Statement will be recognized as an adjustment to the beginning balance of retained earnings. The Registrant is currently in the process of evaluating the impact of adopting this Statement on its Condensed Consolidated Financial Statements.

**3. Intangible Assets and Goodwill**

Intangible assets consist of core deposits, servicing rights, customer lists and non-competition agreements. Intangibles, excluding servicing rights, are amortized on either a straight-line or an accelerated basis over their estimated useful lives, generally over a period of up to 25 years. The Registrant reviews intangible assets for possible impairment whenever events or changes in circumstances indicate that carrying amounts may not be recoverable. The details of the Registrant's intangible assets are shown in the following table.

| (\$ in millions)                               | Gross Carrying Amount | Accumulated Amortization | Valuation Allowance | Net Carrying Amount |
|------------------------------------------------|-----------------------|--------------------------|---------------------|---------------------|
| <b>As of June 30, 2006:</b>                    |                       |                          |                     |                     |
| Mortgage servicing rights                      | \$ 1,138              | (627)                    | (28)                | 483                 |
| Other consumer and commercial servicing rights | 23                    | (17)                     |                     | 6                   |
| Core deposits                                  | 417                   | (258)                    |                     | 159                 |
| Other                                          | 39                    | (13)                     |                     | 26                  |
| Total intangible assets                        | \$ 1,617              | (915)                    | (28)                | 674                 |

As of December 31, 2005:

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|                                                |    |       |       |      |     |
|------------------------------------------------|----|-------|-------|------|-----|
| Mortgage servicing rights                      | \$ | 1,075 | (596) | (46) | 433 |
| Other consumer and commercial servicing rights |    | 22    | (14)  |      | 8   |
| Core deposits                                  |    | 432   | (244) |      | 188 |
| Other                                          |    | 29    | (9)   |      | 20  |
| Total intangible assets                        | \$ | 1,558 | (863) | (46) | 649 |
| As of June 30, 2005:                           |    |       |       |      |     |
| Mortgage servicing rights                      | \$ | 1,003 | (556) | (79) | 368 |
| Other consumer and commercial servicing rights |    | 22    | (12)  |      | 10  |
| Core deposits                                  |    | 432   | (225) |      | 207 |
| Other                                          |    | 29    | (5)   |      | 24  |
| Total intangible assets                        | \$ | 1,486 | (798) | (79) | 609 |

**Table of Contents****Notes to Condensed Consolidated Financial Statements (continued)**

As of June 30, 2006, all of the Registrant's intangible assets were being amortized. Amortization expense recognized on intangible assets (including servicing rights) for the three and six months ended June 30, 2006 and 2005 were as follows:

|                                                   | For the three months   |      | For the six months     |      |
|---------------------------------------------------|------------------------|------|------------------------|------|
| (\$ in millions)                                  | ended June 30,<br>2006 | 2005 | ended June 30,<br>2006 | 2005 |
| Amortization expense (including servicing rights) | \$ 28                  | 29   | 56                     | 60   |

Estimated amortization expense, including servicing rights, for years ending December 31, 2006 through 2010 is as follows:

|                  |        |
|------------------|--------|
| (\$ in millions) |        |
| 2006 (a)         | \$ 111 |
| 2007             | 102    |
| 2008             | 90     |
| 2009             | 77     |
| 2010             | 66     |

(a) Includes six months actual and six months estimated.

Changes in the net carrying amount of goodwill by operating segment for the six months ended June 30, 2006 and 2005 were as follows:

|                                    | Commercial    | Branch     | Consumer   | Investment | Processing<br>Solutions | Total        |
|------------------------------------|---------------|------------|------------|------------|-------------------------|--------------|
| (\$ in millions)                   | Banking       | Banking    | Lending    | Advisors   |                         |              |
| Balance as of December 31, 2005    | \$ 871        | 798        | 182        | 127        | 191                     | 2,169        |
| Acquisitions                       |               |            |            |            | 14                      | 14           |
| Reclassification                   |               |            |            | 11         |                         | 11           |
| <b>Balance as of June 30, 2006</b> | <b>\$ 871</b> | <b>798</b> | <b>182</b> | <b>138</b> | <b>205</b>              | <b>2,194</b> |
| Balance as of December 31, 2004    | \$ 373        | 254        | 58         | 103        | 191                     | 979          |
| Acquisitions                       | 502           | 548        | 125        | 24         |                         | 1,199        |
| <b>Balance as of June 30, 2005</b> | <b>\$ 875</b> | <b>802</b> | <b>183</b> | <b>127</b> | <b>191</b>              | <b>2,178</b> |

SFAS No. 142, Goodwill and Other Intangible Assets, issued in June 2001, discontinued the practice of amortizing goodwill and initiated an annual review for impairment. Impairment is to be examined more frequently if certain indicators are encountered. The Registrant has completed its most recent annual goodwill impairment test required by this Statement as of September 30, 2005 and has determined that no impairment exists.

In the table above, acquisition activity includes acquisitions in the respective period plus purchase accounting adjustments related to previous acquisitions. During the first quarter of 2006, the Registrant acquired a credit card processing company. The acquisition resulted in the recognition of \$14 million of goodwill and did not have a material impact on the financial results of the Registrant. Additionally, during the first quarter of 2006, \$11 million of goodwill was reclassified from other intangible assets.



**Table of Contents****Notes to Condensed Consolidated Financial Statements (continued)****4. Retained Interests**

As of June 30, 2006, the key economic assumptions used in measuring the Registrant's servicing rights and residual interests were as follows:

| (\$ in millions)             | Rate       | Fair Value | Weighted-Average Life (in years) | Prepayment Speed Assumption (annual) | Discount Rate (annual) | Weighted-Average Default Rate |
|------------------------------|------------|------------|----------------------------------|--------------------------------------|------------------------|-------------------------------|
| Residential mortgage loans:  |            |            |                                  |                                      |                        |                               |
| Servicing assets             | Fixed      | \$ 490     | 8.25                             | 9.0%                                 | 9.8%                   | N/A                           |
| Servicing assets             | Adjustable | 46         | 3.5                              | 25.5                                 | 10.5                   | N/A                           |
| Home equity lines of credit: |            |            |                                  |                                      |                        |                               |
| Servicing assets             | Adjustable | 4          | 2.4                              | 35.0                                 | 11.7                   | N/A                           |
| Residual interest            | Adjustable | 22         | 1.7                              | 35.0                                 | 11.7                   | .35%(a)                       |
| Automotive loans:            |            |            |                                  |                                      |                        |                               |
| Servicing assets             | Fixed      | 2          | .9                               | 1.55                                 | 12.0                   | N/A                           |
| Residual interest            | Fixed      | 8          | .9                               | 1.55                                 | 12.0                   | 1.25(b)                       |

(a) Annualized rate

(b) Cumulative rate

Based on historical credit experience, expected credit losses for servicing rights have been deemed not to be material. The Registrant serviced \$27.1 billion of residential mortgage loans and \$.7 billion of consumer loans for other investors at June 30, 2006.

Changes in capitalized servicing rights for the six months ended June 30:

| (\$ in millions)             | 2006   | 2005 |
|------------------------------|--------|------|
| Beginning balance            | \$ 441 | 352  |
| Amount capitalized           | 64     | 63   |
| Amortization                 | (34)   | (37) |
| Servicing valuation recovery | 18     |      |
| Ending balance               | \$ 489 | 378  |

Changes in the servicing rights valuation reserve for the six months ended June 30:

| (\$ in millions)             | 2006    | 2005 |
|------------------------------|---------|------|
| Beginning balance            | \$ (46) | (79) |
| Servicing valuation recovery | 18      |      |
| Ending balance               | \$ (28) | (79) |

The Registrant maintains a non-qualifying hedging strategy to manage a portion of the risk associated with changes in impairment on the MSR portfolio. This strategy includes the purchase of various available-for-sale securities (primarily principal only strips) and free-standing derivatives (principal only swaps, swaptions and interest rate swaps). The interest income, mark-to-market adjustments and gain or loss from sale activities associated with these portfolios are expected to economically hedge a portion of the change in value of the MSR portfolio caused

by fluctuating discount rates, earnings rates and prepayment speeds.

The increase in interest rates during the first half of 2006 and the resulting impact of changing prepayment speeds led to the recovery of \$18 million in temporary impairment on the MSR portfolio. The increase in longer-term rates in the first quarter of 2005 was offset by a decrease in the second quarter resulting in no net impact to the temporary valuation reserve in the first half of 2005. In addition, the Registrant recognized a net loss of \$6 million and a net gain of \$8 million in the six months ended June 30, 2006 and 2005, respectively, related to changes in fair value and settlement of free-standing derivatives purchased to economically hedge the MSR portfolio. As of June 30, 2006 and 2005, other assets included free-standing derivative instruments related to the MSR portfolio with a fair value of \$10 million and \$29 million, respectively, and other liabilities included a fair value of \$13 million and \$18 million, respectively. The outstanding notional amounts on the free-standing derivative instruments related to the MSR portfolio totaled \$.9 billion and \$3.7 billion as of June 30, 2006 and 2005, respectively. As of June 30, 2006 the available-for-sale securities portfolio included \$240 million of securities related to the non-qualifying hedging strategy.

Temporary impairment or impairment recovery, effected through a change in the MSR valuation reserve, are captured as a component of mortgage banking net revenue in the Condensed Consolidated Statements of Income.

**Table of Contents****Notes to Condensed Consolidated Financial Statements (continued)****5. Derivative Financial Instruments**

The Registrant maintains an overall interest rate risk management strategy that incorporates the use of derivative instruments to minimize significant unplanned fluctuations in earnings and cash flows caused by interest rate volatility. The Registrant's interest rate risk management strategy involves modifying the repricing characteristics of certain assets and liabilities so that changes in interest rates do not adversely affect the net interest margin and cash flows. Derivative instruments that the Registrant may use as part of its interest rate risk management strategy include interest rate swaps, interest rate floors, interest rate caps, forward contracts, options and swaptions. Interest rate swap contracts are exchanges of interest payments, such as fixed-rate payments for floating-rate payments, based on a common notional amount and maturity date. Interest rate floors protect against declining rates, while rate caps protect against rising interest rates. Forward contracts are contracts in which the buyer agrees to purchase, and the seller agrees to make delivery of, a specific financial instrument at a predetermined price or yield. Options provide the purchaser with the right, but not the obligation, to purchase or sell a contracted item during a specified period at an agreed upon price. Swaptions, which have the features of a swap and an option, allow, but do not require, counterparties to exchange streams of payments over a specified period of time.

The Registrant enters into foreign exchange derivative contracts to economically hedge certain foreign denominated loans. Derivative instruments that the Registrant may use to economically hedge these foreign denominated loans include foreign exchange swaps and forward contracts.

As part of its overall risk management strategy relative to its mortgage banking activity, the Registrant may enter into various free-standing derivatives (principal only swaps, swaptions, floors, options and interest rate swaps) to economically hedge interest rate lock commitments and changes in fair value of its largely fixed-rate MSR portfolio. Principal only swaps are total return swaps based on changes in the value of the underlying mortgage principal only trust. The Registrant also enters into forward contracts to economically hedge the change in the fair value of its residential mortgage loans held-for-sale due to the changes in interest rates.

The Registrant also enters into foreign exchange contracts and interest rate swaps, floors and caps for the benefit of commercial customers. The Registrant may economically hedge significant exposures related to these commercial customer free-standing derivatives by entering into offsetting third-party contracts with approved, reputable counterparties with substantially matching terms and currencies. Credit risks arise from the possible inability of counterparties to meet the terms of their contracts and from any resultant exposure to movement in foreign currency exchange rates, limiting the Registrant's exposure to the replacement value of the contracts rather than the notional, principal or contract amounts. The Registrant minimizes the credit risk through credit approvals, limits and monitoring procedures. The Registrant hedges its interest rate exposure on commercial customer transactions by executing offsetting swap agreements with primary dealers.

**FAIR VALUE HEDGES** - The Registrant may enter into interest rate swaps to convert its fixed-rate, long-term debt to floating-rate debt. Decisions to convert fixed-rate debt to floating are made primarily by consideration of the asset/liability mix of the Registrant, the desired asset/liability sensitivity and interest rate levels. For the quarter ended June 30, 2006, certain interest rate swaps met the criteria required to qualify for the shortcut method of accounting. Based on this shortcut method of accounting treatment, no ineffectiveness is assumed. For an interest rate swap accounted for as a fair value hedge, ineffectiveness is the difference between the changes in the fair value of the interest rate swap and the long-term debt. If any interest rate swap does not qualify for the shortcut method of accounting, the ineffectiveness is reported within interest expense in the Condensed Consolidated Statements of Income. For the three months ended June 30, 2006, changes in the fair value of any interest rate swap attributed to hedge ineffectiveness were insignificant to the Registrant's Condensed Consolidated Statements of Income.

During 2005 and 2006, the Registrant terminated interest rate swaps designated as fair value hedges and in accordance with SFAS No. 133, an amount equal to the fair value of the swaps at the date of the termination was recognized as a premium or discount on the previously hedged long-term debt and is being amortized as an adjustment to yield.

The following table reflects the market value of all fair value hedges included in the Condensed Consolidated Balance Sheets:

|                  |          |              |          |
|------------------|----------|--------------|----------|
| (\$ in millions) | June 30, | December 31, | June 30, |
|                  |          | 2005         | 2005     |

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|                                                           | 2006   | 2005 |    |
|-----------------------------------------------------------|--------|------|----|
| Included in other assets:                                 |        |      |    |
| Interest rate swaps related to debt                       | \$ 3   | 21   | 46 |
| Total included in other assets                            | \$ 3   | 21   | 46 |
| Included in other liabilities:                            |        |      |    |
| Interest rate swaps related to debt                       | \$ 158 | 103  | 94 |
| Forward contracts related to mortgage loans held for sale |        | 3    | 3  |
| Total included in other liabilities                       | \$ 158 | 106  | 97 |

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### **Notes to Condensed Consolidated Financial Statements (continued)**

**CASH FLOW HEDGES** - The Registrant may enter into interest rate swaps to convert floating-rate assets and liabilities to fixed rates and to hedge certain forecasted transactions. The assets and liabilities are typically grouped and share the same risk exposure for which they are being hedged. The Registrant may also enter into forward contracts to hedge certain forecasted transactions.

The Registrant has no outstanding cash flow hedges converting floating-rate assets or liabilities to fixed-rates as of June 30, 2006 or December 31, 2005. As of June 30, 2005, the Registrant had \$2 million of outstanding cash flow hedges recorded in other liabilities. Changes in the fair market value of derivative contracts qualifying as cash flow hedges are recorded, net of tax, in accumulated other comprehensive income. As of June 30, 2006 and December 31, 2005, there were no deferred gains or losses, net of tax, related to outstanding cash flow hedges recorded in accumulated other comprehensive income. At June 30, 2005, there were \$1 million in deferred losses, net of tax, included in accumulated other comprehensive income related to outstanding cash flow hedges. Gains and losses on these derivative contracts are reclassified from accumulated other comprehensive income to current period earnings when the forecasted transaction affects earnings and are included in the line item in which the hedged item's effect in earnings is recorded. For the three months ended June 30, 2006 and 2005, no deferred gains or losses on outstanding cash flow hedges were reclassified into current period earnings. Additionally, any ineffectiveness is included in the line item in which the hedged item's effect in earnings is recorded. All components of each derivative instrument's gain or loss are included in the assessment of hedge effectiveness. As of June 30, 2006, there were no instances of designated hedges no longer qualifying as cash flow hedges.

In prior periods, the Registrant terminated certain derivatives qualifying as cash flow hedges. The deferred gains or losses of these terminated instruments, net of tax, are included in accumulated other comprehensive income and are being amortized over the designated hedging periods, which range up to 12 years. As of June 30, 2006, December 31, 2005 and June 30, 2005, \$8 million, \$13 million and \$23 million, respectively, in net deferred losses, net of tax, related to terminated cash flow hedges were recorded in accumulated other comprehensive income. For the three months ended June 30, 2006 and 2005, \$2 million and \$4 million, respectively, in net deferred losses, net of tax, on the terminated cash flow hedges were amortized into earnings. As of June 30, 2006, \$8 million in net deferred losses, net of tax, on terminated cash flow hedges included in accumulated other comprehensive income are expected to be reclassified into earnings during the next 12 months.

**FREE-STANDING DERIVATIVE INSTRUMENTS** - The Registrant enters into various derivative contracts that focus on providing derivative products to commercial customers. These derivative contracts are not designated against specific assets or liabilities on the Condensed Consolidated Balance Sheets or to forecasted transactions and, therefore, do not qualify for hedge accounting. These instruments include foreign exchange derivative contracts entered into for the benefit of commercial customers involved in international trade to hedge their exposure to foreign currency fluctuations and various other derivative contracts for the benefit of commercial customers. The Registrant may economically hedge significant exposures related to these derivative contracts entered into for the benefit of customers by entering into offsetting contracts with approved, reputable, independent counterparties with substantially matching terms.

The Registrant also enters into foreign exchange derivative contracts to economically hedge certain foreign denominated loans. The Registrant does not designate these instruments against the foreign denominated loans, and therefore, does not obtain hedge accounting treatment.

The Registrant enters into forward contracts to economically hedge the change in fair value of its residential mortgage loans held-for-sale due to changes in interest rates. Additionally, interest rate lock commitments issued on residential mortgage loan commitments that will be held for resale are also considered free-standing derivative instruments and the interest rate exposure on these commitments is also economically hedged primarily with forward contracts. The Registrant also enters into a combination of free-standing derivative instruments (principal only swaps, swaptions, floors, forward contracts, options and interest rate swaps) to economically hedge changes in fair value of its largely fixed-rate MSR portfolio. Additionally, the Registrant occasionally may enter into free-standing derivative instruments (options, swaptions and interest rate swaps) in order to minimize significant fluctuations in earnings and cash flows caused by interest rate volatility. Revaluation gains and losses on interest rate lock commitments and free-standing derivative instruments related to the MSR portfolio and residential mortgage loans held for sale are recorded as a component of mortgage banking net revenue. Revaluation gains and losses on foreign exchange derivative contracts and other commercial customer derivative contracts are recorded as a component of corporate banking revenue. Revaluation gains and losses on interest rate risk derivative contracts are recorded within other noninterest income in the Condensed Consolidated Statements of Income. The net gains (losses) recorded in the Condensed Consolidated Statements of Income relating to free-standing derivative instruments are summarized in the following table:

**Table of Contents****Notes to Condensed Consolidated Financial Statements (continued)**

| (\$ in millions)                                                                             | Three months ended<br>June 30, |      | Six months ended<br>June 30, |      |
|----------------------------------------------------------------------------------------------|--------------------------------|------|------------------------------|------|
|                                                                                              | 2006                           | 2005 | 2006                         | 2005 |
| Foreign exchange contracts                                                                   | \$ 11                          | 12   | \$ 25                        | 25   |
| Forward contracts related to interest rate lock commitments and mortgage loans held-for-sale | 2                              | (2)  | 4                            | 1    |
| Interest rate lock commitments                                                               | 2                              | 1    | (1)                          | (1)  |
| Derivative instruments related to MSR portfolio                                              | (5)                            | 18   | (6)                          | 8    |
| Derivative instruments related to interest rate risk                                         | (1)                            | 1    | (1)                          | 2    |

The following table reflects the market value of all free-standing derivatives included in the Condensed Consolidated Balance Sheets:

| (\$ in millions)                                                                             | June 30,<br>2006 | December 31,<br>2005 | June 30,<br>2005 |
|----------------------------------------------------------------------------------------------|------------------|----------------------|------------------|
|                                                                                              |                  |                      |                  |
| Included in other assets:                                                                    |                  |                      |                  |
| Foreign exchange contracts                                                                   | \$ 149           | 118                  | 140              |
| Interest rate contracts for customers                                                        | 128              | 48                   | 59               |
| Interest rate lock commitments                                                               | 2                | 1                    | 2                |
| Derivative instruments related to MSR portfolio                                              | 10               | 4                    | 29               |
| Forward contracts related to interest rate lock commitments and mortgage loans held-for-sale | 6                |                      |                  |
| Derivative instruments related to interest rate risk                                         | 9                |                      |                  |
| Total included in other assets                                                               | \$ 304           | 171                  | 230              |
| Included in other liabilities:                                                               |                  |                      |                  |
| Foreign exchange contracts                                                                   | \$ 137           | 104                  | 122              |
| Interest rate contracts for customers                                                        | 128              | 48                   | 59               |
| Interest rate lock commitments                                                               | 1                |                      |                  |
| Derivative instruments related to MSR portfolio                                              | 13               | 10                   | 18               |
| Forward contracts related to interest rate lock commitments and mortgage loans held-for-sale | 1                | 1                    | 1                |
| Total included in other liabilities                                                          | \$ 280           | 163                  | 200              |

The following table summarizes the Registrant's derivative instrument positions (excluding \$24.2 billion in notional amount of customer accommodation derivatives) at June 30, 2006:

| (\$ in millions)                                                                     | Notional<br>Balance | Weighted-Average<br>Remaining<br>Maturity<br>(in months) | Average<br>Receive<br>Rate | Average<br>Pay<br>Rate |
|--------------------------------------------------------------------------------------|---------------------|----------------------------------------------------------|----------------------------|------------------------|
|                                                                                      |                     |                                                          |                            |                        |
| Interest rate swaps related to debt:                                                 |                     |                                                          |                            |                        |
| Receive fixed/pay floating                                                           | \$ 2,575            | 98                                                       | 5.07%                      | 5.29%                  |
| Mortgage lending commitments:                                                        |                     |                                                          |                            |                        |
| Forward contracts on mortgage loans held-for-sale and interest rate lock commitments | 1,200               | 1                                                        |                            |                        |
| Mortgage servicing rights portfolio:                                                 |                     |                                                          |                            |                        |
| Principal only swaps                                                                 | 57                  | 7                                                        |                            | 5.36                   |
| Interest rate swaps Receive fixed/pay floating                                       | 650                 | 55                                                       | 5.13                       | 5.13                   |

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|                                                |          |     |      |      |
|------------------------------------------------|----------|-----|------|------|
| Interest rate swaps Receive floating/pay fixed | 225      | 109 | 5.26 | 5.04 |
| Interest rate futures/forwards                 | 9        | 2   |      |      |
| Total                                          | \$ 4,716 |     |      |      |

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### **Notes to Condensed Consolidated Financial Statements (continued)**

#### **6. Guarantees**

The Registrant has performance obligations upon the occurrence of certain events under financial guarantees provided in certain contractual arrangements. These various arrangements are summarized below.

As of June 30, 2006, the Registrant had issued \$7.9 billion of financial and performance standby letters of credit to guarantee the performance of various customers to third parties. The maximum amount of credit risk in the event of nonperformance by these parties is equivalent to the contract amount and totals \$7.9 billion. Upon issuance, the Registrant recognizes a liability equivalent to the amount of fees received from the customer for these standby letter of credit commitments. At June 30, 2006, the reserve related to these standby letters of credit was less than \$1 million. Approximately 70% of the total standby letters of credit are secured and in the event of nonperformance by the customers, the Registrant has rights to the underlying collateral provided including commercial real estate, physical plant and property, inventory, receivables, cash and marketable securities.

Through June 30, 2006, the Registrant had transferred, subject to credit recourse, certain primarily floating-rate, short-term, investment grade commercial loans to an unconsolidated QSPE that is wholly owned by an independent third-party. The outstanding balance of such loans at June 30, 2006 was \$3.4 billion. These loans may be transferred back to the Registrant upon the occurrence of an event specified in the legal documents that established the QSPE. These events include borrower default on the loans transferred, bankruptcy preferences initiated against underlying borrowers and ineligible loans transferred by the Registrant to the QSPE. The maximum amount of credit risk in the event of nonperformance by the underlying borrowers is approximately equivalent to the total outstanding balance of \$3.4 billion at June 30, 2006. In addition, the Registrant's agreement to provide liquidity support to the QSPE increased to \$3.8 billion as of June 30, 2006. At June 30, 2006, the Registrant's loss reserve related to the liquidity support and credit enhancement provided to the QSPE was \$13 million.

As of June 30, 2006, the Registrant had provided credit recourse on approximately \$1.3 billion of residential mortgage loans sold to unrelated third parties. In the event of any customer default, pursuant to the credit recourse provided, the Registrant is required to reimburse the third party. The maximum amount of credit risk in the event of nonperformance by the underlying borrowers is equivalent to the total outstanding balance of \$1.3 billion. In the event of nonperformance, the Registrant has rights to the underlying collateral value attached to the loan. Consistent with its overall approach in estimating credit losses for various categories of residential mortgage loans held in its loan portfolio, the Registrant maintains an estimated credit loss reserve of \$19 million relating to these residential mortgage loans sold.

As of June 30, 2006, the Registrant has also fully and unconditionally guaranteed \$376 million of certain long-term borrowing obligations issued by four wholly-owned issuing trust entities that have been deconsolidated consistent with the provisions of FIN 46.

The Registrant, through its electronic payment processing division, processes VISA® and MasterCard® merchant card transactions. Pursuant to VISA® and MasterCard® rules, the Registrant assumes certain contingent liabilities relating to these transactions, which typically arise from billing disputes between the merchant and cardholder that are ultimately resolved in the cardholder's favor. In such cases, these transactions are charged back to the merchant and disputed amounts are refunded to the cardholder. In the event that the Registrant is unable to collect these amounts from the merchant, it will bear the loss for refunded amounts. The likelihood of incurring a contingent liability arising from chargebacks is relatively low, as most products or services are delivered when purchased and credits are issued on returned items. For the six months ended June 30, 2006, the Registrant processed approximately \$62 million of chargebacks presented by issuing banks, resulting in no material actual losses to the Registrant. The Registrant accrues for probable losses based on historical experience and did not carry a material credit loss reserve at June 30, 2006.

Fifth Third Securities, Inc. ( FTS ), a subsidiary of the Registrant, guarantees the collection of all margin account balances held by its brokerage clearing agent for the benefit of FTS customers. FTS is responsible for payment to its brokerage clearing agent for any loss, liability, damage, cost or expense incurred as a result of customers failing to comply with margin or margin maintenance calls on all margin accounts. The margin account balance held by the brokerage clearing agent as of June 30, 2006 was \$55 million. In the event of any customer default, FTS has rights to the underlying collateral provided. Given the existence of the underlying collateral provided as well as the negligible historical credit losses, FTS does not maintain any loss reserve.

#### **7. Business Combinations**

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On January 1, 2005, the Registrant acquired in a merger 100% of the outstanding stock of First National Bankshares, Inc. ( First National ), a bank holding company headquartered in Naples, Florida. First National operated 77 full-service banking centers located primarily in Orlando, Tampa, Sarasota, Naples and Fort Myers. The acquisition of First National allows the Registrant to expand its presence in the rapidly expanding Florida market.

Under the terms of the transaction, each share of First National common stock was exchanged for .5065 shares of the Registrant's common stock, resulting in the issuance of 30.6 million shares of common stock. The common stock issued to effect the transaction was valued at \$47.30 per share, the closing price of the Registrant's common stock on the previous trading day, for a total transaction value of \$1.5 billion. The total purchase price also included the fair value of stock awards issued in exchange for stock awards held by First National employees, for which the aggregate fair value was \$63 million.

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### **Notes to Condensed Consolidated Financial Statements (continued)**

The assets and liabilities of First National were recorded on the Condensed Consolidated Balance Sheet at their respective fair values as of the closing date. The results of First National's operations were included in the Registrant's Condensed Consolidated Statement of Income from the date of acquisition. In addition, the Registrant realized charges against its earnings for acquisition related expenses of \$1 million and \$8 million for the three and six months ended June 30, 2005, respectively. The acquisition related expenses consisted primarily of travel and relocation costs, printing, closure of duplicate facilities, supplies and other costs associated with the conversion.

The transaction resulted in total goodwill and intangible assets of \$1.3 billion based upon the purchase price, the fair values of the acquired assets and assumed liabilities and applicable purchase accounting adjustments. Of this total intangibles amount, \$85 million was allocated to core deposit intangibles, \$7 million was allocated to customer lists and \$13 million was allocated to noncompete agreements. The core deposit intangible and the customer lists are being amortized using an accelerated method over 10 years. The noncompete agreements are being amortized using the straight-line method over the duration of the agreements. The remaining \$1.2 billion of intangible assets was recorded as goodwill. Goodwill recognized in the First National acquisition is not deductible for income tax purposes.

The pro forma effect and the financial results of First National included in the results of operations subsequent to the date of acquisition were not material to the Registrant's financial condition or the operating results for the periods presented.

### **8. Related Party Transactions**

At June 30, 2006 and 2005, certain directors, executive officers, principal holders of the Registrant's common stock and associates of such persons were indebted, including undrawn commitments to lend, to the Registrant's banking subsidiaries in the aggregate amount, net of participations, of \$270 million and \$271 million, respectively. As of June 30, 2006 and 2005, the outstanding balance on loans to related parties, net of participations and undrawn commitments, were \$65 million and \$78 million, respectively.

Commitments to lend to related parties as of June 30, 2006 and 2005, net of participations, were comprised of \$258 million and \$262 million, respectively, in loans and guarantees for various business and personal interests made to Registrant and subsidiary directors and \$12 million and \$10 million, respectively, to certain executive officers. This indebtedness was incurred in the ordinary course of business on substantially the same terms as those prevailing at the time of comparable transactions with unrelated parties.

None of the Registrant's affiliates, officers, directors or employees has an interest in or receives any remuneration from any special purpose entities or qualified special purpose entities with which the Registrant transacts business.

### **9. Legal and Regulatory Proceedings**

During May 2005, the Registrant filed suit in the United States District Court for the Southern District of Ohio related to a dispute with the Internal Revenue Service concerning the timing of deductions associated with certain leveraged lease transactions in its 1997 tax return. The Internal Revenue Service has also proposed adjustments to the tax effects of certain leveraged lease transactions in subsequent tax return years. The proposed adjustments, including penalties, relate to the Registrant's portfolio of lease-in lease-out transactions, service contract leases and qualified technology equipment leases with both domestic and foreign municipalities. The Registrant is challenging the Internal Revenue Service's proposed treatment of all of these leasing transactions. The Registrant's original net investment in these leases totaled approximately \$900 million. The Registrant continues to believe that its treatment of these leveraged leases was appropriate and in compliance with applicable tax law and regulations. While management cannot predict with certainty the result of the suit, given the tax treatment of these transactions has been challenged by the Internal Revenue Service, the Registrant believes a resolution may involve a projected change in the timing of the leveraged lease cash flows. Recently issued FSP 13-2, which is effective for fiscal years beginning after December 15, 2006, mandates that a change in the projected timing of cash flows, excluding interest assessments, will impact the timing of cumulative income recognized. The Registrant is currently in the process of evaluating the potential impact of FSP 13-2 on its Condensed Consolidated Financial Statements.

On April 26, 2006 the Registrant was added as a defendant in a consolidated antitrust class action lawsuit originally filed against Visa®, MasterCard® and several other major financial institutions in the United States District Court for the Eastern District of New York. The plaintiffs, merchants operating commercial businesses throughout the U.S. and trade associations, claim that the interchange fees charged by card-issuing banks are unreasonable and seek injunctive relief and unspecified damages. As this litigation is still in its early stages, it is not possible for management to assess the probability of a material adverse outcome or the range of possible damages to the Registrant, if any.

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The Registrant and its subsidiaries are not parties to any other material litigation other than those arising in the normal course of business. While it is impossible to ascertain the ultimate resolution or range of financial liability with respect to these contingent matters, management believes any resulting liability from these other actions would not have a material effect upon the Registrant's consolidated financial position or results of operations.

**Table of Contents****Notes to Condensed Consolidated Financial Statements (continued)****10. Retirement and Benefit Plans**

The following table summarizes the components of net periodic pension cost:

| (\$ in thousands)                               | For the three months<br>ended June 30, |         | For the six months<br>ended June 30, |         |
|-------------------------------------------------|----------------------------------------|---------|--------------------------------------|---------|
|                                                 | 2006                                   | 2005    | 2006                                 | 2005    |
| Service cost                                    | \$ 113                                 | 162     | 232                                  | 324     |
| Interest cost                                   | 4,002                                  | 3,415   | 7,328                                | 6,877   |
| Expected return on assets                       | (4,571)                                | (4,595) | (9,520)                              | (8,606) |
| Amortization of actuarial loss                  | 1,945                                  | 2,357   | 4,339                                | 4,639   |
| Amortization of unrecognized prior service cost | 130                                    | 129     | 259                                  | 258     |
| Settlement                                      |                                        | 439     |                                      | 585     |
| Net periodic pension cost                       | \$ 1,619                               | 1,907   | 2,638                                | 4,077   |

Net periodic pension cost is recorded as a component of employee benefits in the Condensed Consolidated Statements of Income. The plan assumptions are evaluated annually and are updated as necessary. The discount rate assumption reflects the yield on a portfolio of high quality fixed-income instruments that have a similar duration to the plan's liabilities. The long-term rate of return assumption reflects the average return expected on the assets invested to provide for the plan's liabilities. In determining the expected long-term rate of return, the Registrant evaluated actuarial and economic inputs, including long-term inflation rate assumptions and broad equity and bond indices long-term return projections, as well as actual long-term historical plan performance. Based on the current year actuarial assumptions, the Registrant did not make any cash contributions to its pension plans during the six months ended June 30, 2006.

**11. Stock-Based Compensation**

Effective January 1, 2006, the Registrant adopted SFAS No. 123 (Revised 2004), Share-Based Payment. This Statement requires measurement of the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award with the cost to be recognized over the vesting period. As the Registrant had previously adopted the fair value method of accounting for stock-based compensation described in SFAS No. 123, the adoption did not have a material impact on salaries, wages and incentives expense reported in the Condensed Consolidated Statements of Income. The adoption did result in the recognition of a benefit, during the first quarter of 2006, for the cumulative effect of change in accounting principle of approximately \$4 million (net of \$2 million of tax) due to the recognition of an estimate of forfeiture experience to be realized for all unvested stock-based awards outstanding.

Stock-based compensation awards are eligible for issuance under the Incentive Compensation Plan, adopted on January 20, 2004 and approved by shareholders on March 23, 2004, to key employees, officers and directors of the Registrant and its subsidiaries. The Incentive Compensation Plan provides for nonqualified and incentive stock options, stock appreciation rights, restricted stock and restricted stock units, performance shares and performance units and stock awards. Option and stock appreciation right grants are at fair market value at the date of the grant, have up to 10-year terms and vest and become fully exercisable at the end of three to four years of continued employment.

For the six months ended June 30, 2006, approximately 1.1 million restricted stock awards and 6.9 million stock appreciation rights were granted. For the six months ended June 30, 2005, approximately .9 million restricted stock awards and 4.8 million stock appreciation rights were granted. The weighted-average fair values of stock appreciation rights granted were \$7.33 and \$9.34 for the six months ended June 30, 2006 and 2005, respectively. The fair value of stock appreciation rights is estimated on the date of grant using the Black-Scholes pricing model with the following assumptions used for grants:

2006      2005

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|                                 |              |       |
|---------------------------------|--------------|-------|
| Expected dividend yield         | <b>4.06%</b> | 3.48% |
| Expected option life (in years) | <b>6.0</b>   | 6.0   |
| Expected volatility             | <b>23%</b>   | 26%   |
| Risk-free interest rate         | <b>4.88%</b> | 4.25% |

Stock-based compensation expense was \$30 million and \$19 million for the three months ended June 30, 2006 and 2005, respectively, and \$44 million and \$37 million for the six months ended June 30, 2006 and 2005, respectively, and is included in salaries, wages and incentives expense in the Condensed Consolidated Statements of Income. Stock-based compensation expense for the three months ended June 30, 2006 included \$9 million of expense related to the issuance in April 2006 of stock-based awards to retirement eligible employees.

**Table of Contents****Notes to Condensed Consolidated Financial Statements (continued)****12. Other Comprehensive Income**

The Registrant has elected to present the disclosures required by SFAS No. 130, Reporting Comprehensive Income, in the Consolidated Statements of Changes in Shareholders' Equity. Disclosure of the reclassification adjustments, related tax effects allocated to other comprehensive income and accumulated other comprehensive income for the six months ended June 30 were as follows:

| (\$ in millions)                                                                                   | Pre-Tax<br>Activity | Tax<br>Effect | Net<br>Activity | Beginning<br>Balance | Net<br>Activity | Ending<br>Balance |
|----------------------------------------------------------------------------------------------------|---------------------|---------------|-----------------|----------------------|-----------------|-------------------|
| <b>2006</b>                                                                                        |                     |               |                 |                      |                 |                   |
| Losses on available-for-sale securities                                                            | \$ (407)            | 142           | (265)           |                      |                 |                   |
| Reclassification adjustment for net gains recognized in net income                                 | (15)                | 5             | (10)            |                      |                 |                   |
| Unrecognized losses on available-for-sale securities                                               | (422)               | 147           | (275)           | \$ (395)             | (275)           | (670)             |
| Reclassification adjustment for net losses on cash flow hedge derivatives recognized in net income | 8                   | (3)           | 5               |                      |                 |                   |
| Unrecognized gains (losses) on cash flow hedge derivatives                                         | 8                   | (3)           | 5               | (13)                 | 5               | (8)               |
| Change in minimum pension liability                                                                |                     |               |                 | (5)                  |                 | (5)               |
| Total                                                                                              | \$ (414)            | 144           | (270)           | \$ (413)             | (270)           | (683)             |
| <b>2005</b>                                                                                        |                     |               |                 |                      |                 |                   |
| Losses on available-for-sale securities                                                            | \$ (23)             | 8             | (15)            |                      |                 |                   |
| Reclassification adjustment for net gains recognized in net income                                 | (30)                | 10            | (20)            |                      |                 |                   |
| Unrecognized losses on available-for-sale securities                                               | (53)                | 18            | (35)            | \$ (72)              | (35)            | (107)             |
| Gains on cash flow hedge derivatives                                                               | 7                   | (2)           | 5               |                      |                 |                   |
| Reclassification adjustment for net losses recognized in net income                                | 6                   | (2)           | 4               |                      |                 |                   |
| Unrecognized gains (losses) on cash flow hedge derivatives                                         | 13                  | (4)           | 9               | (33)                 | 9               | (24)              |
| Change in minimum pension liability                                                                | 93                  | (33)          | 60              | (64)                 | 60              | (4)               |
| Total                                                                                              | \$ 53               | (19)          | 34              | \$ (169)             | 34              | (135)             |

**13. Earnings Per Share**

The calculation of earnings per share and the reconciliation of earnings per share and earnings per diluted share were as follows:

| (in millions, except per share data) | For the three months ended June 30, |                   |                     | 2005   |                   |                     |
|--------------------------------------|-------------------------------------|-------------------|---------------------|--------|-------------------|---------------------|
|                                      | Income                              | Average<br>Shares | Per Share<br>Amount | Income | Average<br>Shares | Per Share<br>Amount |
| <b>Earnings per share:</b>           |                                     |                   |                     |        |                   |                     |
| Net income                           | \$ 382                              |                   |                     | \$ 417 |                   |                     |

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|                                                 |        |     |         |        |     |         |
|-------------------------------------------------|--------|-----|---------|--------|-----|---------|
| Net income available to common shareholders (a) | \$ 382 | 555 | \$ 0.69 | \$ 417 | 554 | \$ 0.75 |
|-------------------------------------------------|--------|-----|---------|--------|-----|---------|

## **Earnings per diluted share:**

|                                             |        |     |         |        |     |         |
|---------------------------------------------|--------|-----|---------|--------|-----|---------|
| Net income available to common shareholders | \$ 382 | 555 | \$ 0.69 | \$ 417 | 554 | \$ 0.75 |
|---------------------------------------------|--------|-----|---------|--------|-----|---------|

Effect of dilutive securities:

|                    |   |   |
|--------------------|---|---|
| Stock based awards | 2 | 4 |
|--------------------|---|---|

Convertible preferred stock (b)

|                                                                      |        |     |         |        |     |         |
|----------------------------------------------------------------------|--------|-----|---------|--------|-----|---------|
| Net income available to common shareholders plus assumed conversions | \$ 382 | 557 | \$ 0.69 | \$ 417 | 558 | \$ 0.75 |
|----------------------------------------------------------------------|--------|-----|---------|--------|-----|---------|

---

(a) Dividends on preferred stock are \$.185 million for the three months ended June 30, 2006 and 2005.

(b) The additive effect to income from dividends on convertible preferred stock is \$.145 million and the average share dilutive effect from convertible preferred stock is ..308 million shares for the three months ended June 30, 2006 and 2005.

**Table of Contents****Notes to Condensed Consolidated Financial Statements (continued)**

| (in millions, except per share data)                                     | For the six months ended June 30, |                           |                     |        |                           |                     |
|--------------------------------------------------------------------------|-----------------------------------|---------------------------|---------------------|--------|---------------------------|---------------------|
|                                                                          | Income                            | 2006<br>Average<br>Shares | Per Share<br>Amount | Income | 2005<br>Average<br>Shares | Per Share<br>Amount |
| <b>Earnings per share:</b>                                               |                                   |                           |                     |        |                           |                     |
| Income before cumulative effect                                          | \$ 742                            |                           |                     | \$ 822 |                           |                     |
| Net income available to common shareholders before cumulative effect (a) | 741                               | 555                       | \$ 1.34             | 821    | 555                       | \$ 1.48             |
| Cumulative effect of change in accounting principle, net of tax          | 4                                 |                           |                     |        |                           |                     |
| Net income available to common shareholders (a)                          | \$ 745                            | 555                       | \$ 1.34             | \$ 821 | 555                       | \$ 1.48             |
| <b>Earnings per diluted share:</b>                                       |                                   |                           |                     |        |                           |                     |
| Net income available to common shareholders before cumulative effect     | \$ 741                            | 555                       | \$ 1.34             | \$ 821 | 555                       | \$ 1.48             |
| Effect of dilutive securities:                                           |                                   |                           |                     |        |                           |                     |
| Stock based awards                                                       |                                   | 2                         |                     |        | 5                         | (0.01)              |
| Convertible preferred stock (b)                                          |                                   |                           |                     |        |                           |                     |
| Income plus assumed conversions before cumulative effect                 | 741                               | 557                       | 1.34                | 822    | 560                       | 1.47                |
| Cumulative effect of change in accounting principle, net of tax          | 4                                 |                           |                     |        |                           |                     |
| Net income available to common shareholders plus assumed conversions     | \$ 745                            | 557                       | \$ 1.34             | \$ 822 | 560                       | \$ 1.47             |

(a) Dividends on preferred stock are \$.370 million for the six months ended June 30, 2006 and 2005.

(b) The additive effect to income from dividends on convertible preferred stock is \$.290 million and the average share dilutive effect from convertible preferred stock is .308 million shares for the six months ended June 30, 2006 and 2005.

Options to purchase 34.9 million and 28.5 million shares outstanding during the three months ended June 30, 2006 and 2005, respectively, were not included in the computation of net income per diluted share because the exercise prices of these options were greater than the average market price of the common shares, and therefore, the effect would be antidilutive.

**14. Business Segments**

The Registrant's principal activities include Commercial Banking, Branch Banking, Consumer Lending, Investment Advisors and Processing Solutions. During the first quarter of 2006, the Registrant began reporting its Retail line of business as two business segments, Branch Banking and Consumer Lending. All prior year information has been updated to reflect this presentation. Commercial Banking offers banking, cash management and financial services to large and middle-market businesses, government and professional customers. Branch Banking provides a full range of deposit and loans and lease products to individuals and small businesses through retail locations. Consumer Lending includes the Registrant's mortgage, home equity and other indirect lending activities. Investment Advisors provides a full range of investment alternatives for individuals, companies and not-for-profit organizations. Processing Solutions provides electronic funds transfer, debit, credit and merchant transaction processing, operates the Jeanie® ATM network and provides other data processing services to affiliated and unaffiliated customers. The Other/Eliminations column includes the unallocated portion of the investment portfolio, certain non-deposit funding, unassigned equity and certain support activities and other items not attributed to the business segments.

The Registrant manages interest rate risk centrally at the corporate level by employing an FTP methodology. This methodology insulates the business segments from interest rate risk, enabling them to focus on serving customers through loan originations and deposit taking. The FTP system assigns charge rates and credit rates to classes of assets and liabilities, respectively, based on expected duration. The statements of income in the table below are on an FTP basis. In addition to the previously mentioned items, the Other/Eliminations column includes the net effect of the FTP methodology.

Results of the Registrant's business segments are presented based on its management structure and management accounting practices. The structure and practices are specific to the Registrant; therefore, the financial results of the Registrant's business segments are not necessarily

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comparable with similar information for other financial institutions. The Registrant refines its methodologies from time to time as management accounting practices are improved and businesses change. Revisions to the Registrant's methodologies are applied on a retroactive basis.

The financial results of the business segments include allocations for shared services and headquarters expenses. Even with these allocations, the financial results are not necessarily indicative of the business segments' financial condition and results of operations as if they were to exist as independent entities. Additionally, the business segments form synergies by taking advantage of cross-sell opportunities and when funding operations by accessing the capital markets as a collective unit. The financial information for each segment is reported on the basis used internally by the Registrant's management to evaluate performance and allocate resources. The allocation has been consistently applied for all periods presented. Revenues from affiliated transactions are typically charged at rates available to and transacted with unaffiliated customers.

**Table of Contents****Notes to Condensed Consolidated Financial Statements (continued)**

Results of operations and selected financial information by operating segment are as follows:

|                                                               | Commercial | Branch  | Consumer | Investment |                         | Other/       |         |
|---------------------------------------------------------------|------------|---------|----------|------------|-------------------------|--------------|---------|
| (\$ in millions)                                              | Banking    | Banking | Lending  | Advisors   | Processing<br>Solutions | Eliminations | Total   |
| <b>For the three months ended June 30, 2006:</b>              |            |         |          |            |                         |              |         |
| Net interest income (a)                                       | \$ 380     | 476     | 99       | 59         | 9                       | (307)        | 716     |
| Provision for loan and lease losses                           | 31         | 26      | 23       | 1          | 2                       | (12)         | 71      |
| Net interest income after provision for loan and lease losses | 349        | 450     | 76       | 58         | 7                       | (295)        | 645     |
| Noninterest income:                                           |            |         |          |            |                         |              |         |
| Electronic payment processing revenue                         | 3          | 49      |          |            | 170                     | (11)         | 211     |
| Service charges on deposits                                   | 38         | 93      |          | 2          | 1                       | 1            | 135     |
| Mortgage banking net revenue                                  |            | 1       | 39       | 1          |                         |              | 41      |
| Investment advisory revenue                                   | 1          | 23      |          | 97         |                         | (25)         | 96      |
| Corporate banking revenue                                     | 78         | 3       |          | 1          |                         |              | 82      |
| Other noninterest income                                      | 8          | 26      | 21       |            | 2                       | 19           | 76      |
| Securities gains (losses), net                                |            | (1)     |          |            | 25                      | (10)         | 14      |
| Total noninterest income                                      | 128        | 194     | 60       | 101        | 198                     | (26)         | 655     |
| Noninterest expense:                                          |            |         |          |            |                         |              |         |
| Salaries, wages and incentives                                | 49         | 91      | 20       | 35         | 15                      | 93           | 303     |
| Employee benefits                                             | 11         | 26      | 8        | 7          | 3                       | 14           | 69      |
| Equipment expense                                             |            | 8       |          |            | 2                       | 19           | 29      |
| Net occupancy expense                                         | 3          | 30      | 2        | 2          | 1                       | 21           | 59      |
| Other noninterest expense                                     | 126        | 118     | 49       | 53         | 107                     | (154)        | 299     |
| Total noninterest expense                                     | 189        | 273     | 79       | 97         | 128                     | (7)          | 759     |
| Income before income taxes                                    | 288        | 371     | 57       | 62         | 77                      | (314)        | 541     |
| Applicable income taxes (a)                                   | 86         | 131     | 20       | 22         | 27                      | (127)        | 159     |
| Net income                                                    | \$ 202     | 240     | 37       | 40         | 50                      | (187)        | 382     |
| Average assets                                                | \$ 35,444  | 44,078  | 21,579   | 5,791      | 1,289                   | (2,440)      | 105,741 |
| <b>For the three months ended June 30, 2005:</b>              |            |         |          |            |                         |              |         |
| Net interest income (a)                                       | \$ 352     | 416     | 107      | 47         | 9                       | (173)        | 758     |
| Provision for loan and lease losses                           | 23         | 23      | 14       | 1          | 3                       | (4)          | 60      |
| Net interest income after provision for loan and lease losses | 329        | 393     | 93       | 46         | 6                       | (169)        | 698     |
| Noninterest income:                                           |            |         |          |            |                         |              |         |
| Electronic payment processing revenue                         | 3          | 41      |          |            | 149                     | (10)         | 183     |
| Service charges on deposits                                   | 38         | 91      |          | 2          | 1                       |              | 132     |
| Mortgage banking net revenue                                  |            | 1       | 43       |            |                         | 2            | 46      |
| Investment advisory revenue                                   |            | 22      |          | 92         |                         | (22)         | 92      |
| Corporate banking revenue                                     | 73         | 3       |          | 1          |                         | (3)          | 74      |

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|                                |           |        |        |       |       |       |         |
|--------------------------------|-----------|--------|--------|-------|-------|-------|---------|
| Other noninterest income       | 12        | 27     | 33     | 1     | 2     | 18    | 93      |
| Securities gains (losses), net |           |        |        |       |       | 15    | 15      |
| Total noninterest income       | 126       | 185    | 76     | 96    | 152   |       | 635     |
| Noninterest expense:           |           |        |        |       |       |       |         |
| Salaries, wages and incentives | 49        | 90     | 16     | 34    | 11    | 95    | 295     |
| Employee benefits              | 10        | 25     | 8      | 7     | 2     | 15    | 67      |
| Equipment expense              |           | 7      |        |       | 1     | 17    | 25      |
| Net occupancy expense          | 3         | 27     | 2      | 2     | 1     | 19    | 54      |
| Other noninterest expense      | 114       | 112    | 60     | 51    | 94    | (144) | 287     |
| Total noninterest expense      | 176       | 261    | 86     | 94    | 109   | 2     | 728     |
| Income before income taxes     | 279       | 317    | 83     | 48    | 49    | (171) | 605     |
| Applicable income taxes (a)    | 86        | 112    | 29     | 17    | 17    | (73)  | 188     |
| Net income                     | \$ 193    | 205    | 54     | 31    | 32    | (98)  | 417     |
| Average assets                 | \$ 31,597 | 41,498 | 19,690 | 4,626 | 1,177 | 4,177 | 102,765 |

(a) Includes taxable-equivalent adjustments of \$6 million and \$8 million for the three months ended June 30, 2006 and 2005, respectively.

**Table of Contents****Notes to Condensed Consolidated Financial Statements (continued)**

|                                                                 | Commercial | Branch  | Consumer | Investment |                         | Other/       |         |
|-----------------------------------------------------------------|------------|---------|----------|------------|-------------------------|--------------|---------|
| (\$ in millions)                                                | Banking    | Banking | Lending  | Advisors   | Processing<br>Solutions | Eliminations | Total   |
| <b>For the six months ended June 30, 2006:</b>                  |            |         |          |            |                         |              |         |
| Net interest income (a)                                         | \$ 755     | 928     | 198      | 113        | 18                      | (578)        | 1,434   |
| Provision for loan and lease losses                             | 67         | 48      | 51       | 3          | 4                       | (24)         | 149     |
| Net interest income after provision for loan and lease losses   | 688        | 880     | 147      | 110        | 14                      | (554)        | 1,285   |
| Noninterest income:                                             |            |         |          |            |                         |              |         |
| Electronic payment processing revenue                           | 7          | 93      |          | 1          | 330                     | (24)         | 407     |
| Service charges on deposits                                     | 77         | 178     |          | 3          | 3                       |              | 261     |
| Mortgage banking net revenue                                    |            | 2       | 85       | 1          |                         |              | 88      |
| Investment advisory revenue                                     | 1          | 46      |          | 188        |                         | (48)         | 187     |
| Corporate banking revenue                                       | 150        | 6       |          | 1          |                         |              | 157     |
| Other noninterest income                                        | 16         | 49      | 47       | 3          | 2                       | 40           | 157     |
| Securities gains (losses), net                                  |            | (1)     |          |            | 25                      | (9)          | 15      |
| Total noninterest income                                        | 251        | 373     | 132      | 197        | 360                     | (41)         | 1,272   |
| Noninterest expense:                                            |            |         |          |            |                         |              |         |
| Salaries, wages and incentives                                  | 96         | 180     | 38       | 68         | 29                      | 175          | 586     |
| Employee benefits                                               | 25         | 52      | 18       | 17         | 7                       | 37           | 156     |
| Equipment expense                                               | 1          | 15      | 1        | 1          | 3                       | 35           | 56      |
| Net occupancy expense                                           | 7          | 59      | 4        | 5          | 2                       | 41           | 118     |
| Other noninterest expense                                       | 245        | 230     | 96       | 101        | 208                     | (306)        | 574     |
| Total noninterest expense                                       | 374        | 536     | 157      | 192        | 249                     | (18)         | 1,490   |
| Income before income taxes and cumulative effect                | 565        | 717     | 122      | 115        | 125                     | (577)        | 1,067   |
| Applicable income taxes (a)                                     | 169        | 253     | 42       | 41         | 45                      | (225)        | 325     |
| Income before cumulative effect                                 | 396        | 464     | 80       | 74         | 80                      | (352)        | 742     |
| Cumulative effect of change in accounting principle, net of tax |            |         |          |            |                         | 4            | 4       |
| Net income                                                      | \$ 396     | 464     | 80       | 74         | 80                      | (348)        | 746     |
| Average assets                                                  | \$ 34,922  | 43,404  | 21,340   | 5,441      | 1,271                   | (1,137)      | 105,241 |
| <b>For the six months ended June 30, 2005:</b>                  |            |         |          |            |                         |              |         |
| Net interest income (a)                                         | \$ 695     | 809     | 211      | 92         | 17                      | (307)        | 1,517   |
| Provision for loan and lease losses                             | 52         | 43      | 41       | 3          | 5                       | (17)         | 127     |
| Net interest income after provision for loan and lease losses   | 643        | 766     | 170      | 89         | 12                      | (290)        | 1,390   |
| Noninterest income:                                             |            |         |          |            |                         |              |         |
| Electronic payment processing revenue                           | 6          | 77      |          |            | 291                     | (20)         | 354     |
| Service charges on deposits                                     | 76         | 171     |          | 4          | 2                       |              | 253     |
| Mortgage banking net revenue                                    |            | 2       | 82       | 1          |                         | 2            | 87      |
| Investment advisory revenue                                     | 2          | 43      |          | 183        |                         | (46)         | 182     |
| Corporate banking revenue                                       | 132        | 6       |          | 1          |                         | (3)          | 136     |
| Other noninterest income                                        | 22         | 48      | 72       | 1          | 14                      | 43           | 200     |

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|                                |           |        |        |       |       |       |         |
|--------------------------------|-----------|--------|--------|-------|-------|-------|---------|
| Securities gains (losses), net |           |        |        |       |       | 30    | 30      |
| Total noninterest income       | 238       | 347    | 154    | 190   | 307   | 6     | 1,242   |
| Noninterest expense:           |           |        |        |       |       |       |         |
| Salaries, wages and incentives | 91        | 176    | 31     | 69    | 22    | 172   | 561     |
| Employee benefits              | 23        | 51     | 16     | 15    | 5     | 38    | 148     |
| Equipment expense              | 1         | 13     | 1      | 1     | 2     | 32    | 50      |
| Net occupancy expense          | 5         | 52     | 3      | 4     | 1     | 43    | 108     |
| Other noninterest expense      | 221       | 214    | 115    | 103   | 185   | (273) | 565     |
| Total noninterest expense      | 341       | 506    | 166    | 192   | 215   | 12    | 1,432   |
| Income before income taxes     | 540       | 607    | 158    | 87    | 104   | (296) | 1,200   |
| Applicable income taxes (a)    | 168       | 213    | 56     | 31    | 37    | (127) | 378     |
| Net income                     | \$ 372    | 394    | 102    | 56    | 67    | (169) | 822     |
| Average assets                 | \$ 31,000 | 41,302 | 19,453 | 4,685 | 1,140 | 4,311 | 101,891 |

(a) Includes taxable-equivalent adjustments of \$13 and \$17 million for the six months ended June 30, 2006 and 2005, respectively.

**Table of Contents****PART II. OTHER INFORMATION****Legal Proceedings (Item 1)**

During May 2005, the Registrant filed suit in the United States District Court for the Southern District of Ohio related to a dispute with the Internal Revenue Service concerning the timing of deductions associated with certain leveraged lease transactions in its 1997 tax return. The Internal Revenue Service has also proposed adjustments to the tax effects of certain leveraged lease transactions in subsequent tax return years. The proposed adjustments, including penalties, relate to the Registrant's portfolio of lease-in lease-out transactions, service contract leases and qualified technology equipment leases with both domestic and foreign municipalities. The Registrant is challenging the Internal Revenue Service's proposed treatment of all of these leasing transactions. The Registrant's original net investment in these leases totaled approximately \$900 million. The Registrant continues to believe that its treatment of these leveraged leases was appropriate and in compliance with applicable tax law and regulations. While management cannot predict with certainty the result of the suit, given the tax treatment of these transactions has been challenged by the Internal Revenue Service, the Registrant believes a resolution may involve a projected change in the timing of the leveraged lease cash flows. Recently issued FSP 13-2, which is effective for fiscal years beginning after December 15, 2006, mandates that a change in the projected timing of cash flows, excluding interest assessments, will impact the timing of cumulative income recognized. See additional discussion of FSP 13-2 in Note 2. The Registrant is currently in the process of evaluating the potential impact of FSP 13-2 on its Condensed Consolidated Financial Statements.

On April 26, 2006 the Registrant was added as a defendant in a consolidated antitrust class action lawsuit originally filed against Visa®, MasterCard® and several other major financial institutions in the United States District Court for the Eastern District of New York. The plaintiffs, merchants operating commercial businesses throughout the U.S. and trade associations, claim that the interchange fees charged by card-issuing banks are unreasonable and seek injunctive relief and unspecified damages. As this litigation is still in its early stages, it is not possible for management to assess the probability of a material adverse outcome or the range of possible damages to the Registrant, if any.

The Registrant and its subsidiaries are not parties to any other material litigation other than those arising in the normal course of business. While it is impossible to ascertain the ultimate resolution or range of financial liability with respect to these contingent matters, management believes any resulting liability from these other actions would not have a material effect upon the Registrant's consolidated financial position or results of operations.

**Risk Factors (Item 1A)**

There have been no material changes made during the second quarter of 2006 to the risk factors as previously disclosed in the Registrant's 2005 Form 10-K.

**Unregistered Sales of Equity Securities and Use of Proceeds (Item 2)****Purchases of Equity Securities by the Issuer and Affiliated Purchasers**

| Period        |                | Total Number of<br>Shares<br>Purchased (a) | Average<br>Price Paid<br>Per<br>Share | Total Number of Shares<br>Purchased as Part of<br>Publicly Announced Plans<br>or Programs | Maximum Number of<br>Shares that May Yet Be<br>Purchased Under the Plans<br>or Programs |
|---------------|----------------|--------------------------------------------|---------------------------------------|-------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------|
| April 1, 2006 | April 30, 2006 | 39,806                                     | \$ 38.43                              |                                                                                           | 17,846,953                                                                              |
| May 1, 2006   | May 31, 2006   | 29,309                                     | 39.50                                 |                                                                                           | 17,846,953                                                                              |
| June 1, 2006  | June 30, 2006  | 26,372                                     | 37.83                                 |                                                                                           | 17,846,953                                                                              |
| Total         |                | 95,487                                     | \$ 38.59                              |                                                                                           | 17,846,953                                                                              |

(a) The Registrant repurchased 39,806, 29,309 and 26,372 shares during April, May and June, respectively, in connection with various employee compensation plans. These purchases are not included against the maximum number of shares that may yet be purchased under the Board of Directors' authorization.



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**Signatures**

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

Fifth Third Bancorp  
Registrant

Date: August 3, 2006

/s/ Christopher G. Marshall  
Christopher G. Marshall  
Executive Vice President and  
Chief Financial Officer

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**Exhibits (Item 6)**

(a) List of Exhibits

- (3)(i) Second Amended Articles of Incorporation, as amended (Incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2001).
- (3)(ii) Code of Regulations, as amended. (Incorporated by reference to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2006).
- (10) Offer letter from Fifth Third Bancorp to Christopher G. Marshall dated April 12, 2006.
- (31)(i) Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by Chief Executive Officer.
- (31)(ii) Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by Chief Financial Officer.
- (32)(i) Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 by Chief Executive Officer.
- (32)(ii) Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 by Chief Financial Officer.