PNC FINANCIAL SERVICES GROUP INC
Form 10-K/A
February 04, 2008
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-K/A

AMENDMENT NO. 1

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2006

Commission file number 001-09718

THE PNC FINANCIAL SERVICES GROUP, INC.

(Exact name of registrant as specified in its charter)

Pennsylvania	**25-1435979**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

One PNC Plaza

249 Fifth Avenue

Pittsburgh, Pennsylvania 15222-2707

(Address of principal executive offices, including zip code)

Registrant s telephone number, including area code **- (412) 762-2000**

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value $5.00	New York Stock Exchange
$1.60 Cumulative Convertible Preferred Stock-Series C, par value $1.00	New York Stock Exchange
$1.80 Cumulative Convertible Preferred Stock-Series D, par value $1.00	New York Stock Exchange
Series G Junior Participating Preferred Share Purchase Rights	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

$1.80 Cumulative Convertible Preferred Stock - Series A, par value $1.00

$1.80 Cumulative Convertible Preferred Stock - Series B, par value $1.00

8.25% Convertible Subordinated Debentures Due 2008

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes X No __

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes __ No X

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

Indicate by check mark if the disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. __

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 X Accelerated filer __ Non-accelerated filer __

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

The aggregate market value of the registrant s outstanding voting common stock held by nonaffiliates on June 30, 2006, determined using the per share closing price on that date on the New York Stock Exchange of $70.17, was approximately $20.6 billion. There is no non-voting common equity of the registrant outstanding.

Number of shares of registrant s common stock outstanding at February 16, 2007: 293,164,316

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement of The PNC Financial Services Group, Inc. to be filed pursuant to Regulation 14A for the annual meeting of shareholders to be held on April 24, 2007 (Proxy Statement) are incorporated by reference into Part III of this Form 10-K.

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FORM 10-K/A

AMENDMENT NO. 1

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EXPLANATORY NOTE

The PNC Financial Services Group, Inc. (PNC or the Corporation) is filing this Amendment No. 1 to its Annual Report on Form 10-K for the year ended December 31, 2006, to reflect the following:

a. The restatement of the Consolidated Statement of Cash Flows for the year ended December 31, 2006, as discussed in Note 1 Accounting Policies of the Notes To Consolidated Financial Statements included in Part II, Item 8: Financial Statements and Supplementary Data.

b. Audited consolidated financial statements of BlackRock, Inc., (BlackRock) for the year ended December 31, 2006. The BlackRock audited consolidated financial statements are included in Part IV, Item 15 (a) (2): Financial Statement Schedules, through incorporation by reference to pages F-5 through F-67 of BlackRock s 2006 Annual Report on Form 10-K. This information is being included in this Amendment No. 1 pursuant to the requirements of SEC Regulation S-X, Article 3-09.

Except for Items 8 and 9A of Part II and Item 15 of Part IV, no other information in the Form 10-K is being amended by this Amendment. This Amendment continues to speak as of March 1, 2007, the date of the original filing of PNC s 2006 Annual Report on Form 10-K, and PNC has not updated the disclosure in this Amendment to speak as of any later date.

The original pagination used in the March 1, 2007 Form 10-K filing has been retained in this Amendment No. 1.

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ITEM 8 - FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of

The PNC Financial Services Group, Inc.

Pittsburgh, Pennsylvania

We have audited the accompanying consolidated balance sheets of The PNC Financial Services Group, Inc. and subsidiaries (the Company) as of December 31, 2006 and 2005, and the related consolidated statements of income, shareholders equity, and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of The PNC Financial Services Group, Inc. and subsidiaries as of December 31, 2006 and 2005, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the consolidated financial statements, the Company adopted Statement of Financial Accounting Standard No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R)* as of December 31, 2006.

As discussed in Note 1 to the consolidated financial statements, the accompanying consolidated statement of cash flows for the year ended December 31, 2006 has been restated.

As a result of the transaction discussed in Note 2 to the consolidated financial statements, the Company no longer

consolidates BlackRock, Inc. (BlackRock). Beginning September 30, 2006, the Company recognized its investment in BlackRock using the equity method of accounting.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company s internal control over financial reporting as of December 31, 2006, based on the criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 1, 2007 expressed an unqualified opinion on management s assessment of the effectiveness of the Company s internal control over financial reporting and an unqualified opinion on the effectiveness of the Company s internal control over financial reporting.

/s/ Deloitte & Touche LLP
Pittsburgh, Pennsylvania
March 1, 2007 (February 4, 2008 as to the effects of the
restatement discussed in Note 1.)

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CONSOLIDATED INCOME STATEMENT

THE PNC FINANCIAL SERVICES GROUP, INC.

	Year ended December 31		
In millions, except per share data	**2006**	2005	2004
Interest Income			
Loans	**$3,203**	$2,669	$2,043
Securities available for sale	**1,049**	822	568
Other	**360**	243	141
Total interest income	**4,612**	3,734	2,752
Interest Expense			
Deposits	**1,590**	981	484
Borrowed funds	**777**	599	299
Total interest expense	**2,367**	1,580	783
Net interest income	**2,245**	2,154	1,969
Provision for credit losses	**124**	21	52
Net interest income less provision for credit losses	**2,121**	2,133	1,917
Noninterest Income			
Asset management	**1,420**	1,443	994
Fund servicing	**893**	870	817
Service charges on deposits	**313**	273	252
Brokerage	**246**	225	219
Consumer services	**365**	293	259
Corporate services	**626**	485	423
Equity management gains	**107**	96	67
Net securities gains (losses)	**(207)**	(41)	55
Trading	**183**	157	113
Net gains related to BlackRock	**2,066**		
Other	**315**	372	373
Total noninterest income	**6,327**	4,173	3,572
Noninterest Expense			
Compensation	**2,128**	2,061	1,755
Employee benefits	**304**	332	309
Net occupancy	**310**	313	267
Equipment	**303**	296	290
Marketing	**104**	106	87
Other	**1,294**	1,198	1,004
Total noninterest expense	**4,443**	4,306	3,712
Income before minority interest and income taxes	**4,005**	2,000	1,777
Minority interest in income of BlackRock	**47**	71	42
Income taxes	**1,363**	604	538
Net income	**$2,595**	$1,325	$1,197
Earnings Per Common Share			
Basic	**$8.89**	$4.63	$4.25
Diluted	**$8.73**	$4.55	$4.21
Average Common Shares Outstanding			
Basic	**292**	286	281
Diluted	**297**	290	284

See accompanying Notes To Consolidated Financial Statements.

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CONSOLIDATED BALANCE SHEET

THE PNC FINANCIAL SERVICES GROUP, INC.

In millions, except par value	December 31 **2006**	2005
Assets		
Cash and due from banks	**$3,523**	$3,518
Federal funds sold and resale agreements	**1,763**	350
Other short-term investments, including trading securities	**3,130**	2,543
Loans held for sale	**2,366**	2,449
Securities available for sale	**23,191**	20,710
Loans, net of unearned income of $795 and $835	**50,105**	49,101
Allowance for loan and lease losses	**(560)**	(596)
Net loans	**49,545**	48,505
Goodwill	**3,402**	3,619
Other intangible assets	**641**	847
Equity investments	**5,330**	1,323
Other	**8,929**	8,090
Total assets	**$101,820**	$91,954
Liabilities		
Deposits		
Noninterest-bearing	**$16,070**	$14,988
Interest-bearing	**50,231**	45,287
Total deposits	**66,301**	60,275
Borrowed funds		
Federal funds purchased	**2,711**	4,128
Repurchase agreements	**2,051**	1,691
Bank notes and senior debt	**3,633**	3,875
Subordinated debt	**3,962**	4,469
Other	**2,671**	2,734
Total borrowed funds	**15,028**	16,897
Allowance for unfunded loan commitments and letters of credit	**120**	100
Accrued expenses	**3,970**	2,770
Other	**4,728**	2,759
Total liabilities	**90,147**	82,801
Minority and noncontrolling interests in consolidated entities	**885**	590
Shareholders Equity		
Preferred stock (a)		
Common stock - $5 par value		
Authorized 800 shares, issued 353 shares	**1,764**	1,764
Capital surplus	**1,651**	1,299
Retained earnings	**10,985**	9,023
Accumulated other comprehensive loss	**(235)**	(267)
Common stock held in treasury at cost: 60 and 60 shares	**(3,377)**	(3,256)
Total shareholders equity	**10,788**	8,563
Total liabilities, minority and noncontrolling interests, and shareholders equity	**$101,820**	$91,954

(a) Less than $.5 million at each date.

See accompanying Notes To Consolidated Financial Statements.

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CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITY

THE PNC FINANCIAL SERVICES GROUP, INC.

In millions	Shares Outstanding Common Stock	Common Stock	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
Balance at January 1, 2004 (a)	277	1,764	1,079	7,642	60	(3,900)	$ 6,645
Net income				1,197			1,197
Net unrealized securities losses					(69)		(69)
Net unrealized losses on cash flow hedge derivatives					(42)		(42)
Other					(3)		(3)
Comprehensive income							1,083
Cash dividends declared							
Common				(565)			(565)
Preferred				(1)			(1)
Treasury stock activity	6		116			176	292
Tax benefit of stock option plans			15				15
Stock options granted			22				22
Subsidiary stock transactions			4				4
Restricted stock transactions			(22)				(22)
Balance at December 31, 2004 (a)	283	1,764	1,214	8,273	(54)	(3,724)	7,473
Net income				1,325			1,325
Net unrealized securities losses					(174)		(174)
Net unrealized losses on cash flow hedge derivatives					(32)		(32)
Other					(7)		(7)
Comprehensive income							1,112
Cash dividends declared							
Common				(574)			(574)
Preferred				(1)			(1)
Treasury stock activity	10		61			468	529
Tax benefit of stock option plans			7				7
Stock options granted			30				30
Subsidiary stock transactions			(5)				(5)
Restricted stock transactions			(8)				(8)
Balance at December 31, 2005 (a)	293	1,764	1,299	9,023	(267)	(3,256)	8,563
Net income				**2,595**			**2,595**
Net unrealized securities gains					**149**		**149**
Net unrealized gains on cash flow hedge derivatives					**13**		**13**
Additional minimum pension liability under SFAS 87					**(1)**		**(1)**
Other (b)					**3**		**3**
Comprehensive income							**2,759**
Cash dividends declared							
Common				**(632)**			**(632)**
Preferred				**(1)**			**(1)**
BlackRock/MLIM transaction (c)			**262**		`		**262**
Treasury stock activity (d)			**(12)**			**(121)**	**(133)**
Tax benefit of stock option plans			**29**				**29**
Stock options granted			**31**				**31**

Subsidiary stock transactions			**27**				**27**
Restricted stock transactions			**15**				**15**
Net effect of adopting SFAS 158					**(132)**		**(132)**
Balance at December 31, 2006 (a)	**293**	**$ 1,764**	**$ 1,651**	**$ 10,985**	**$ (235)**	**$ (3,377)**	**$ 10,788**

(a) Our preferred stock outstanding as of December 31, 2006, 2005, and 2004 and January 1, 2004 was less than $.5 million at each date and, therefore, is excluded from this presentation.
(b) Consists of interest-only strip valuation adjustments and foreign currency translation adjustments.
(c) Represents the portion of our gain on the BlackRock/MLIM transaction that was credited to capital surplus.
(d) Our net treasury stock activity in 2006 was less than .1 million shares issued and is excluded from this presentation.

See accompanying Notes To Consolidated Financial Statements.

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CONSOLIDATED STATEMENT OF CASH FLOWS

THE PNC FINANCIAL SERVICES GROUP, INC.

	Year ended December 31		
In millions	**2006 (As restated see Note 1)**	2005	2004
Operating Activities			
Net income	**$ 2,595**	$ 1,325	$ 1,197
Adjustments to reconcile net income to net cash provided by (used in) operating activities			
Provision for credit losses	**124**	21	52
Depreciation, amortization and accretion	**345**	375	302
Deferred income taxes	**752**	1	(194)
Net securities losses (gains)	**207**	41	(55)
Valuation adjustments	**45**	(6)	(37)
Net gains related to BlackRock	**(2,066)**		
Undistributed earnings of BlackRock	**(39)**		
Excess tax benefits from share-based payment arrangements	**(29)**	(4)	(3)
Net change in			
Loans held for sale	**435**	(680)	(265)
Other short-term investments	**156**	(613)	(1,191)
Accrued expenses and other liabilities	**83**	(1,326)	2,432
Other	**(449)**	186	(1,778)
Net cash provided (used) by operating activities	**2,159**	(680)	460
Investing Activities			
Repayment of securities	**3,667**	4,261	4,297
Sales			
Securities	**11,102**	13,304	14,206
Loans	**1,110**	39	151
Foreclosed and other nonperforming assets	**14**	20	23
Purchases			
Securities	**(15,707)**	(21,484)	(18,094)
Loans	**(3,072)**	(2,746)	(2,741)
Net change in			
Loans	**(278)**	(219)	(3,228)
Federal funds sold and resale agreements	**(1,413)**	1,775	241
Cash received from divestitures		26	512
Net cash paid for acquisitions	**(58)**	(530)	(299)
Purchases of corporate and bank-owned life insurance	**(425)**		
Other	**(302)**	(242)	(261)
Net cash used by investing activities	**(5,362)**	(5,796)	(5,193)
Financing Activities			
Net change in			
Noninterest-bearing deposits	**968**	(280)	1,023
Interest-bearing deposits	**4,940**	3,538	4,724
Federal funds purchased	**(1,417)**	3,908	
Repurchase agreements	**359**	5	265
Commercial paper	**(10)**	(2,241)	25
Other short-term borrowed funds	**249**	(404)	775
Sales/issuances			
Bank notes and senior debt	**1,964**	2,285	500
Subordinated debt		494	504
Other long-term borrowed funds	**279**	1,641	464
Treasury stock	**343**	220	159

Perpetual trust securities	**489**		
Repayments/maturities			
Bank notes and senior debt	**(2,200)**	(755)	(900)
Subordinated debt	**(471)**	(351)	(200)
Other long-term borrowed funds	**(1,150)**	(559)	(1,489)
Excess tax benefits from share-based payment arrangements	**29**	4	3
Acquisition of treasury stock	**(531)**	(166)	(292)
Cash dividends paid	**(633)**	(575)	(566)
Net cash provided by financing activities	**3,208**	6,764	4,995
Net Increase In Cash And Due From Banks	**5**	288	262
Cash and due from banks at beginning of period	**3,518**	3,230	2,968
Cash and due from banks at end of period	**$ 3,523**	$ 3,518	$ 3,230
Cash Paid For			
Interest	**$ 2,376**	$ 1,515	$ 782
Income taxes	**471**	504	486
Non-cash Items			
Investment in BlackRock, net	**3,179**		
Transfer from (to) loans to (from) loans held for sale, net	**2,280**	93	(32)
Transfer from loans to other assets	**13**	16	22

See accompanying Notes To Consolidated Financial Statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

THE PNC FINANCIAL SERVICES GROUP, INC.

BUSINESS

We are one of the largest diversified financial services companies in the United States based on assets, with businesses engaged in:

- Retail banking,
- Corporate and institutional banking,
- Asset management, and
- Global fund processing services.

We provide many of our products and services nationally and others in our primary geographic markets located in Pennsylvania; New Jersey; the greater Washington, DC area, including Maryland and Virginia; Ohio; Kentucky; and Delaware. We also provide certain global fund processing services internationally. We are subject to intense competition from other financial services companies and are subject to regulation by various domestic and international authorities.

NOTE 1 ACCOUNTING POLICIES

BASIS OF FINANCIAL STATEMENT PRESENTATION

Our consolidated financial statements include the accounts of the parent company and its subsidiaries, most of which are wholly owned, and certain partnership interests and variable interest entities. See Note 2 Acquisitions regarding the deconsolidation of BlackRock, Inc. (BlackRock) from PNC s Consolidated Balance Sheet effective September 29, 2006. Our investment in BlackRock has been accounted for under the equity method of accounting since that date. We prepared these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America (generally accepted accounting principles or GAAP). We have eliminated intercompany accounts and transactions. We have also reclassified certain prior year amounts to conform with the 2006 presentation. These reclassifications did not have a material impact on our consolidated financial condition or results of operations.

RESTATEMENT OF THE 2006 CONSOLIDATED STATEMENT OF CASH FLOWS

Subsequent to the issuance of our 2006 Consolidated Financial Statements, we determined that the Consolidated Statement of Cash Flows for the year ended December 31, 2006 should be restated. The restatement resulted from the misclassification of cash flows related to our fourth quarter 2006 issuance of perpetual trust securities (see Note 3). The cash flows related to the issuance of these securities totaling $489 million had previously been classified within the Operating Activities section of the Consolidated Statement of Cash Flows. We have concluded that the cash flows of this transaction should have been classified within the Financing Activities section of the Consolidated Statement of Cash Flows. As a result, we have restated the accompanying Consolidated Statement of Cash Flows for the year ended December 31, 2006.

The effect of the restatement on the 2006 Consolidated Statement of Cash Flows is as follows:

	As Previously Reported	As Restated
Operating Activities:		
Net change in Other	40	(449)
Net cash provided (used) by operating activities	2,648	2,159
Financing Activities:		
Sales/issuances Perpetual trust securities		489
Net cash provided by financing activities	2,719	3,208

The restatement had no impact on the Net Increase In Cash And Due From Banks set forth in the Consolidated Statement of Cash Flows for the year ended December 31, 2006 or the balance of Cash and due from banks in the Consolidated Balance Sheet as of December 31, 2006.

The restatement does not affect our Consolidated Income Statement, Consolidated Balance Sheet or Consolidated Statement of Shareholders Equity as of or for the year ended December 31, 2006. Accordingly, our previously reported revenues, net income, earnings per share, total assets and regulatory capital as of and for the year ended December 31, 2006 remain unchanged. In addition, the restatement did not impact our Consolidated Income Statements, the Consolidated Statements of Cash Flows or the Consolidated Statements of Shareholders Equity for the years ended December 31, 2005 or 2004 or the Consolidated Balance Sheet as of December 31, 2005.

Special Purposes Entities

Special purpose entities are broadly defined as legal entities structured for a particular purpose. We use special purpose entities in various legal forms to conduct normal business activities. Special purpose entities that meet the criteria for a Qualifying Special Purpose Entity (QSPE) as defined in Statement of Financial Accounting Standards No. (SFAS) 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, are not required to be consolidated. We review special purpose entities that are not QSPEs for consolidation in accordance with Financial Accounting Standards Board (FASB) Interpretation No. 46 (Revised 2003), Consolidation of Variable Interest Entities (FIN 46R).

In general, a variable interest entity (VIE) is a special purpose entity formed as a corporation, partnership, limited liability corporation, or any other legal structure used to conduct activities or hold assets that either:

Does not have equity investors with voting rights that can directly or indirectly make decisions about the entity s activities through those voting rights or similar rights, or

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- Has equity investors that do not provide enough equity for the entity to finance its activities.

A VIE often holds financial assets, including loans or receivables, real estate or other property.

We consolidate a VIE if we are considered to be its primary beneficiary. The primary beneficiary is subject to absorbing the majority of the expected losses from the VIE s activities, is entitled to receive a majority of the entity s residual returns, or both. Upon consolidation of a VIE, we generally record all of the VIE s assets, liabilities and noncontrolling interests at fair value, with future changes based upon consolidation accounting principles. See Note 3 Variable Interest Entities for more information about non-consolidated VIEs in which we hold a significant interest.

Business Combinations

We record the net assets of companies that we acquire at their estimated fair value at the date of acquisition and we include the results of operations of the acquired business in our consolidated income statement from the date of acquisition. We recognize as goodwill the excess of the purchase price over the estimated fair value of the net assets acquired.

Subsidiary Stock Transactions

We recognize as income, when appropriate, any gain from the sale or issuance by subsidiaries of their stock to third parties. The gain is the difference between our basis in the stock and the increase in the book value per share of the subsidiaries equity and is recorded in noninterest income in the Consolidated Income Statement. We provide applicable taxes on the gain.

Use of Estimates

We prepare the consolidated financial statements using financial information available at the time, which requires us to make estimates and assumptions that affect the amounts reported. Actual results may differ from these estimates and the differences may be material to the consolidated financial statements.

Revenue Recognition

We earn net interest and noninterest income from various sources, including:

- Lending,
- Securities portfolio,
- Asset management and fund servicing,
- Customer deposits,
- Loan servicing,
- Brokerage services, and
- Securities and derivatives trading activities, including foreign exchange.

We also earn revenue from selling loans and securities, and we recognize income or loss from certain private equity activities. We earn fees and commissions from:

- Issuing loan commitments, standby letters of credit and financial guarantees,
- Selling various insurance products,
- Providing treasury management services,
- Providing merger and acquisition advisory and related services, and
- Participating in certain capital markets transactions.

Revenue earned on interest-earning assets is recognized based on the effective yield of the financial instrument.

We recognize asset management and fund servicing fees primarily as the services are performed. Asset management fees are generally based on a percentage of the fair value of the assets under management and performance fees are generally based on a percentage of the returns on such assets. Certain performance fees are earned upon attaining specified investment return thresholds and are recorded as earned. Beginning in the fourth quarter of 2006, asset management fees also includes our proportionate share of the earnings of BlackRock under the equity method of accounting.

Fund servicing fees are primarily based on a percentage of the fair value of the fund assets and the number of shareholder accounts we service.

Service charges on deposit accounts are recognized as charged. Brokerage fees and gains on the sale of securities and certain derivatives are recognized on a trade-date basis.

We record private equity income or loss based on changes in the valuation of the underlying investments or when we dispose of our interest. Dividend income from private equity investments is generally recognized when received.

We recognize revenue from loan servicing, securities and derivatives and foreign exchange trading, and securities underwriting activities as they are earned based on contractual terms, as transactions occur or as services are provided. We recognize revenue from the sale of loans upon closing of the transaction.

In certain circumstances, revenue is reported net of associated expenses in accordance with GAAP.

Cash and Cash Equivalents

Cash and due from banks are considered cash and cash equivalents for financial reporting purposes.

Investments

We have interests in various types of investments. The accounting for these investments is dependent on a number of factors including, but not limited to, items such as:

- Marketability of the investment,
- Ownership interest,
- Our plans for the investment, and
- The nature of the investment.

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Investment in BlackRock

As described in Note 2 Acquisitions, we deconsolidated the assets and liabilities of BlackRock from our Consolidated Balance Sheet at September 30, 2006 and now account for our investment in BlackRock under the equity method of accounting. Under the equity method, our investment in the equity of BlackRock is reflected on our Consolidated Balance Sheet in the caption Equity Investments, while our proportionate share of BlackRock s earnings is reported on our Consolidated Income Statement in the caption Asset Management.

Private Equity Investments

We report private equity investments, which include direct investments in companies, interests in limited partnerships, and affiliated partnership interests, at estimated fair values. These estimates are based on available information and may not necessarily represent amounts that we will ultimately realize through distribution, sale or liquidation of the investments. The valuation procedures applied to direct investments include techniques such as multiples of cash flow of the entity, independent appraisals of the entity or the pricing used to value the entity in a recent financing transaction. We value affiliated partnership interests based on the underlying investments of the partnership using procedures consistent with those applied to direct investments. We generally value limited partnership investments based on the financial statements we receive from the general partner. We include all private equity investments on the Consolidated Balance Sheet in Equity Investments. Changes in the fair value of these assets are recognized in noninterest income.

We consolidate private equity funds when we are the sole general partner in a limited partnership and have determined that we have control of the partnership.

Equity Securities and Partnership Interests

We account for equity investments other than BlackRock and private equity investments under one of the following methods:

Marketable equity securities are recorded on a trade-date basis and are accounted for at fair value based on the securities quoted market prices from a national securities exchange. Dividend income on these securities is recognized in net interest income. Those purchased with the intention of recognizing short-term profits are classified as trading, carried at market value and classified as short-term investments. Both realized and unrealized gains and losses on trading securities are included in noninterest income. Marketable equity securities not classified as trading are designated as securities available for sale and are carried at fair value with unrealized gains and losses, net of income taxes, reflected in accumulated other comprehensive income or loss. Any unrealized losses that we have determined to be other-than-temporary are recognized in the period that the determination is made.

Investments in nonmarketable equity securities are recorded using the cost method of accounting. The cost method is used for those investments since we do not have significant influence over the investee. Under this method, there is no change to the cost basis unless there is an other-than-temporary decline in value. If the decline is determined to be other than temporary, we write down the cost basis of the investment to a new cost basis that represents realizable value. The amount of the write-down is accounted for as a loss included in noninterest income in the period the determination is made. Distributions received from income on cost method investments are included in interest or noninterest income depending on the type of investment. We include nonmarketable equity securities in Other Assets on the Consolidated Balance Sheet.

For investments in limited partnerships, limited liability companies and other minor investments that are not required to be consolidated, we use either the cost method or the equity method. The cost method is described above for nonmarketable equity securities. We use the cost method for minor investments in which we have no influence over the operations of the investee and when cost appropriately reflects our economic interest in the underlying investment. We use the equity method for all other general and limited partner ownership interests and limited liability company investments. Under the equity method, we record our equity ownership share of net income or loss of the investee in noninterest income. Investments described above are included in Equity Investments on the Consolidated Balance Sheet.

Debt Securities

Debt securities are recorded on a trade-date basis. We classify debt securities as held to maturity and carry them at amortized cost if we have the positive intent and ability to hold the securities to maturity. Debt securities that we purchase for short-term appreciation or other trading purposes are carried at market value and classified as short-term investments. Realized and unrealized gains and losses on trading securities are included in noninterest income.

Debt securities not classified as held to maturity or trading are designated as securities available for sale and carried at fair value with unrealized gains and losses, net of income taxes, reflected in accumulated other comprehensive income or loss. Other-than-temporary declines in the fair value of available for sale debt securities are recognized as a securities loss included in noninterest income in the period in which the determination is made. We review all debt securities that are in an unrealized loss position for other-than-temporary impairment on a quarterly basis.

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We include all interest on debt securities, including amortization of premiums and accretion of discounts using the interest method, in net interest income. We compute gains and losses realized on the sale of debt securities available for sale on a specific security basis and include them in noninterest income.

Loans And Leases

Except as described below, loans are stated at the principal amounts outstanding, net of unearned income, unamortized deferred fees and costs on originated loans, and premiums or discounts on loans purchased. Interest income related to loans other than nonaccrual loans is accrued based on the principal amount outstanding and credited to net interest income as earned using the interest method. Loan origination fees, direct loan origination costs, and loan premiums and discounts are deferred and amortized to income, over periods not exceeding the contractual life of the loan, using methods that are not materially different from the interest method.

As of January 1, 2006, we adopted SFAS 155, Accounting for Certain Hybrid Financial Instruments an amendment of FASB Statements No. 133 and 140, which was issued in February 2006. SFAS 155 permits a fair value election for previously bifurcated hybrid financial instruments on an instrument-by-instrument basis, clarifies the scope of SFAS 133, Accounting for Derivative Instruments and Hedging Activities, regarding interest-only and principal-only strips, and provides further guidance on certain issues regarding beneficial interests in securitized financial assets, concentrations of credit risk and qualifying special purpose entities. Beginning January 1, 2006, we elected to account for certain previously bifurcated hybrid instruments under this standard. As such, certain loans are accounted for at fair value with changes in fair value reported in trading revenue. The fair value of these loans was $216 million, or less than .5% of the total loan portfolio, at December 31, 2006. The adoption of SFAS 155 did not have a significant impact on our accounting for beneficial interests.

We also provide financing for various types of equipment, aircraft, energy and power systems, and rolling stock through a variety of lease arrangements. Direct financing leases are carried at the aggregate of lease payments plus estimated residual value of the leased property, less unearned income. Leveraged leases, a form of financing lease, are carried net of nonrecourse debt. We recognize income over the term of the lease using the interest method. Lease residual values are reviewed for other-than-temporary impairment on a quarterly basis. Gains or losses on the sale of leased assets are included in other noninterest income while valuation adjustments on lease residuals are included in other noninterest expense.

Loan Sales, Securitizations And Retained Interests

We recognize the sale of loans or other financial assets when the transferred assets are legally isolated from our creditors and the appropriate accounting criteria are met. We also sell

mortgage and other loans through secondary market securitizations. In certain cases, we may retain a portion or all of the securities issued, interest-only strips, one or more subordinated tranches, servicing rights and, in some cases, cash reserve accounts, all of which are considered retained interests in the transferred assets. Our loan sales and securitizations are generally structured without recourse to us and with no restrictions on the retained interests. In the event we are obligated for recourse liabilities in a sale, our policy is to record such liabilities at fair value upon closing of the transaction. Gains or losses recognized on the sale of the loans depend on the allocation of carrying value between the loans sold and the retained interests, based on their relative fair market values at the date of sale. We generally estimate fair value based on the present value of future expected cash flows using assumptions as to discount rates, interest rates, prepayment speeds, credit losses and servicing costs, if applicable. Gains or losses on these transactions are reported in noninterest income.

As of January 1, 2006, we adopted SFAS 156, Accounting for Servicing of Financial Assets an amendment of FASB Statement No. 140. SFAS 156 was issued in March 2006 and requires all newly recognized servicing rights and obligations to be initially measured at fair value. For each class of recognized servicing rights and obligations, the standard permits the election of either the amortization method or the fair value measurement method for subsequent measurement of the asset or obligation. For separately recognized servicing rights and obligations retained or purchased related to commercial loans and commercial mortgages, we have elected to account for them under the amortization method, which requires us to amortize the servicing assets or liabilities in proportion to and over the periods of estimated net servicing income or net servicing loss. For servicing rights or obligations related to residential mortgage loans, we have elected to account for subsequent adjustments using the fair value method with changes in the value of the right or obligation reflected in noninterest income.

Each quarter, we evaluate our servicing assets that are being carried at amortized cost for impairment by categorizing the pools of assets underlying servicing rights by product type. A valuation allowance is recorded and reduces current income when the carrying amount of a specific asset category exceeds its fair value.

We classify securities retained as debt securities available for sale or other assets, depending on the form of the retained interest. Retained interests that are subject to prepayment risk are reviewed on a quarterly basis for impairment. If the fair value of the retained interest is below its carrying amount and the decline is determined to be other-than-temporary, then the decline is reflected as a charge to noninterest income. We recognize other adjustments to the fair market value of retained interests classified as available for sale securities through accumulated other comprehensive income or loss.

Loans And Commitments held for sale

We designate loans and related loan commitments as held for sale when we have a positive intent to sell them. We transfer loans and commitments to the loans held for sale category at the lower of cost or fair market value. At the time of transfer, related write-downs on the loans and commitments are recorded as charge-offs or as a separate liability. We establish a new cost basis upon transfer and recognize any subsequent lower of cost or market adjustment as a valuation allowance with charges included in noninterest income. Gains or losses on the actual sale of these loans and commitments are included in noninterest income when realized.

We apply the lower of cost or market analysis on pools of homogeneous loans and commitments on a net aggregate basis. For non-homogeneous loans and commitments, we do this analysis on an individual loan and commitment basis.

Interest income with respect to loans held for sale other than those in nonaccrual status is accrued based on the principal amount outstanding.

In certain circumstances, loans and commitments designated as held for sale may be later transferred back to the loan portfolio based on a change in strategy to retain the credit exposure to those customers. We transfer these loans and commitments to the portfolio at the lower of cost or market value.

Nonperforming Assets

Nonperforming assets include:

- Nonaccrual loans,
- Troubled debt restructurings,
- Nonaccrual loans held for sale, and
- Foreclosed assets.

Other than consumer loans, we generally classify loans and loans held for sale as nonaccrual when we determine that the collection of interest or principal is doubtful or when a default of interest or principal has existed for 90 days or more and the loans are not well-secured or in the process of collection. When the accrual of interest is discontinued, accrued but uncollected interest credited to income in the current year is reversed and unpaid interest accrued in the prior year, if any, is charged against the allowance for loan and lease losses. We charge off loans other than consumer loans based on the facts and circumstances of the individual loan.

Consumer loans well-secured by residential real estate, including home equity and home equity lines of credit, are classified as nonaccrual at 12 months past due. Loans are considered well secured if the fair market value of the property, less 15% to cover potential foreclosure expenses, is greater than or equal to the principal balance including any superior liens. A fair market value assessment of the property is initiated when the loan becomes 80 to 90 days past due. The procedures for foreclosure of these loans is consistent with our general foreclosure process discussed below. The

classification of consumer loans well-secured by residential real estate as nonaccrual loans at 12 months past due is in accordance with Federal Financial Institutions Examination Council guidelines. We charge off these loans based on the facts and circumstances of the individual loan.

Consumer loans not well-secured or in the process of collection are classified as nonaccrual at 120 days past due if they are home equity loans and at 180 days past due if they are home equity lines of credit. These loans are recorded at the lower of cost or market value, less liquidation costs and the unsecured portion of these loans is generally charged off in the month they become nonaccrual.

A loan is categorized as a troubled debt restructuring in the period of restructuring if a significant concession is granted due to deterioration in the financial condition of the borrower.

Nonperforming loans are generally not returned to performing status until the obligation is brought current and the borrower has performed in accordance with the contractual terms for a reasonable period of time and collection of the contractual principal and interest is no longer doubtful. Nonaccrual commercial and commercial real estate loans and troubled debt restructurings are designated as impaired loans. We recognize interest collected on these loans on the cash basis or cost recovery method.

Foreclosed assets are comprised of any asset seized or property acquired through a foreclosure proceeding or acceptance of a deed-in-lieu of foreclosure. Depending on various state statutes, legal proceedings are initiated on or about the 65th day of delinquency. If no other remedies arise from the legal proceedings, the final outcome will result in the sheriff s sale of the property. When PNC acquires the deed, the transfer of loans to other real estate owned (OREO) will be completed. These assets are recorded on the date acquired at the lower of the related loan balance or market value of the collateral less estimated disposition costs. We estimate market values primarily based on appraisals when available or quoted market prices on liquid assets. Subsequently, foreclosed assets are valued at the lower of the amount recorded at acquisition date or the current market value less estimated disposition costs. Valuation adjustments on these assets and gains or losses realized from disposition of such property are reflected in noninterest expense.

Allowance For Loan And Lease Losses

We maintain the allowance for loan and lease losses at a level that we believe to be adequate to absorb estimated probable credit losses inherent in the loan portfolio. The allowance is increased by the provision for credit losses, which is charged against operating results, and decreased by the amount of charge-offs, net of recoveries. Our determination of the adequacy of the allowance is based on periodic evaluations of the loan and lease portfolios and other relevant factors. This evaluation is inherently subjective as it requires material

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estimates, all of which may be susceptible to significant change, including, among others:

- Expected default probabilities,
- Loss given default,
- Exposure at default,
- Amounts and timing of expected future cash flows on impaired loans,
- Value of collateral,
- Estimated losses on consumer loans and residential mortgages, and
- Amounts for changes in economic conditions and potential estimation or judgmental imprecision.

In determining the adequacy of the allowance for loan and lease losses, we make specific allocations to impaired loans, to pools of watchlist and nonwatchlist loans and to consumer and residential mortgage loans. We also allocate reserves to provide coverage for probable losses not covered in specific, pool and consumer reserve methodologies related to qualitative and measurement factors. While allocations are made to specific loans and pools of loans, the total reserve is available for all credit losses.

Specific allocations are made to significant individual impaired loans and are determined in accordance with SFAS 114, Accounting by Creditors for Impairment of a Loan, with impairment measured based on the present value of the loan s expected cash flows, the loan s observable market price or the fair value of the loan s collateral. We establish a specific allowance on all other impaired loans based on their loss given default credit risk rating.

Allocations to loan pools are developed by business segment based on probability of default and loss given default risk ratings by using historical loss trends and our judgment concerning those trends and other relevant factors. These factors may include, among others:

- Actual versus estimated losses,
- Regional and national economic conditions, and
- Business segment and portfolio concentrations.

Loss factors are based on industry and/or internal experience and may be adjusted for significant factors that, based on our judgment, impact the collectibility of the portfolio as of the balance sheet date. Consumer and residential mortgage loan allocations are made at a total portfolio level based on historical loss experience adjusted for portfolio activity.

While our pool reserve methodologies strive to reflect all risk factors, there continues to be a certain element of uncertainty associated with, but not limited to, potential estimation errors and imprecision in the estimation process due to the inherent lag of information. We provide additional reserves that are designed to provide coverage for expected losses attributable to such risks. In addition, these incremental reserves also include factors which may not be directly measured in the

determination of specific or pooled reserves. These factors include:

- Industry concentration and conditions,
- Credit quality trends,
- Recent loss experience in particular segments of the portfolio,
- Ability and depth of lending management,
- Changes in risk selection and underwriting standards, and
- Bank regulatory considerations.

Allowance For Unfunded Loan Commitments And Letters Of Credit

We maintain the allowance for unfunded loan commitments and letters of credit at a level we believe is adequate to absorb estimated probable losses related to these unfunded credit facilities. We determine the adequacy of the allowance based on periodic evaluations of the unfunded credit facilities including an assessment of the probability of commitment usage, credit risk factors for loans outstanding to these same customers, and the terms and expiration dates of the unfunded credit facilities. Net adjustments to the allowance for unfunded loan commitments and letters of credit are included in the provision for credit losses.

Mortgage and other loan Servicing Rights

We provide servicing under various commercial and residential loan servicing contracts. These contracts are either purchased in the open market or retained as part of a commercial mortgage loan securitization, residential mortgage loan sale or other commercial loan sale. Prior to January 1, 2006, purchased contracts were recorded at cost and the servicing rights retained from the sale or securitization of loans were recorded based on their relative fair value to all of the assets securitized or sold. As a result of the adoption of SFAS 156, beginning January 1, 2006 all newly acquired servicing rights were initially measured at fair value. Fair value is based on the present value of the expected future cash flows, including assumptions as to:

- Interest rates for escrow and deposit balance earnings,
- Discount rates,
- Estimated prepayment speeds, and
- Estimated servicing costs.

For subsequent measurements of our servicing rights we have elected to account for our commercial mortgage and commercial loan servicing rights as a class of assets under the amortization method. This determination was made based on the unique characteristics of the commercial mortgages and commercial loans underlying these servicing rights with regard to market inputs used in determining fair value and how we manage the risks inherent in the commercial servicing rights assets. Specific risk characteristics of the commercial mortgages include loan type, currency or exchange rate, prepayment speeds and expected cash flows. Specific risk characteristics of commercial loans include prepayment speeds and credit quality factors which could impact expected cash flows. We record the servicing assets as other intangible assets and amortize them over their estimated lives in proportion to estimated net servicing income. On a quarterly basis, we test the assets for impairment using various valuation models. If the estimated fair value of the assets is less than the carrying value, an impairment loss is recognized. Servicing fees are recognized as they are earned and are reported net of amortization expense in noninterest income. For residential mortgage servicing rights, we have elected to account for these assets under the fair value method. The primary risk of changes to the value of the residential mortgage servicing rights resides in the potential volatility in the economic assumptions used, primarily the prepayment speeds. The pricing methodology used by PNC to value residential mortgage servicing rights uses a combination of securities market data observations, model cash flow projections and anecdotal servicing observations and surveys. Changes in the fair values of these assets are reflected in net servicing revenue in noninterest income.

Fair Value of Financial Instruments

The fair value of financial instruments and the methods and assumptions used in estimating fair value amounts are detailed in Note 23 Fair Value of Financial Instruments.

Goodwill And Other Intangible Assets

We test goodwill and indefinite-lived intangible assets for impairment at least annually, or when events or changes in circumstances indicate the assets might be impaired. Finite-lived intangible assets are amortized to expense using accelerated or straight-line methods over their respective estimated useful lives. We review finite-lived intangible assets for impairment when events or changes in circumstances indicate that the asset s carrying amount is not recoverable from undiscounted future cash flows or it exceeds its fair value.

Depreciation And Amortization

For financial reporting purposes, we depreciate premises and equipment principally using the straight-line method over their estimated useful lives.

We use estimated useful lives for furniture and equipment ranging from one to 10 years, and depreciate buildings over an estimated useful life of up to 40 years. We amortize leasehold improvements over their estimated useful lives of up to 15 years or the respective lease terms, whichever is shorter.

We purchase, as well as internally develop and customize, certain software to enhance or perform internal business functions. Software development costs incurred in the planning and post-development project stages are charged to noninterest expense. Costs associated with designing software configuration and interfaces, installation, coding programs and testing systems are capitalized and amortized using the straight-line method over periods ranging from one to seven years.

Repurchase And Resale Agreements

Repurchase and resale agreements are treated as collateralized financing transactions and are carried at the amounts at which the securities will be subsequently reacquired or resold, including accrued interest, as specified in the respective agreements. Our policy is to take possession of securities purchased under agreements to resell. We monitor the market value of securities to be repurchased and resold and additional collateral may be obtained where considered appropriate to protect against credit exposure.

Other Comprehensive Income

Other comprehensive income consists, on an after-tax basis, primarily of unrealized gains or losses on securities available for sale and derivatives designated as cash flow hedges, and changes in pension, postretirement and postemployment liability adjustments. Details of each component are included in Note 22 Other Comprehensive Income.

Treasury Stock

We record common stock purchased for treasury at cost. At the date of subsequent reissue, the treasury stock account is reduced by the cost of such stock on the first-in, first-out basis.

Derivative Instruments And Hedging Activities

We use a variety of financial derivatives as part of our overall asset and liability risk management process to manage interest rate, market and credit risk inherent in our business activities. We use substantially all such instruments to manage risk related to changes in interest rates. Interest rate and total return swaps, interest rate caps and floors and futures contracts are the primary instruments we use for interest rate risk management.

Financial derivatives involve, to varying degrees, interest rate, market and credit risk. We manage these risks as part of our asset and liability management process and through credit policies and procedures. We seek to minimize counterparty credit risk by entering into transactions with only high-quality institutions, establishing credit limits, and generally requiring bilateral netting and collateral agreements.

We recognize all derivative instruments at fair value as either assets or liabilities in other assets or other liabilities. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship. For derivatives not designated as an accounting hedge, the gain or loss is recognized in trading noninterest income.

For those derivative instruments that are designated and qualify as hedging instruments, we must designate the hedging instrument, based on the exposure being hedged, as a fair value hedge, a cash flow hedge or a hedge of a net investment in a foreign operation. We have no derivatives that hedge the net investment in a foreign operation.

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We formally document the relationship between the hedging instruments and hedged items, as well as the risk management objective and strategy before undertaking a hedge. To qualify for hedge accounting, the derivatives and related hedged items must be designated as a hedge. For hedging relationships in which effectiveness is measured, we formally assess, both at the inception of the hedge and on an ongoing basis, if the derivatives are highly effective in offsetting changes in fair values or cash flows of the hedged item. If it is determined that the derivative instrument is not highly effective as a hedge, hedge accounting is discontinued.

For derivatives that are designated as fair value hedges (i.e., hedging the exposure to changes in the fair value of an asset or a liability attributable to a particular risk), changes in the fair value of the hedging derivative are recognized in earnings and offset by recognizing changes in the fair value of the hedged item attributable to the hedged risk. To the extent the hedge is ineffective, the changes in fair value will not offset and the difference is reflected in the same financial statement category as the hedged item.

For derivatives designated as cash flow hedges (i.e., hedging the exposure to variability in expected future cash flows), the effective portions of the gain or loss on derivatives are reported as a component of accumulated other comprehensive income or loss and subsequently reclassified in interest income in the same period or periods during which the hedged transaction affects earnings. As a result, the change in fair value of any ineffective portion of the hedging derivative is recognized immediately in earnings.

We discontinue hedge accounting when it is determined that the derivative is no longer qualifying as an effective hedge; the derivative expires or is sold, terminated or exercised; or the derivative is de-designated as a fair value or cash flow hedge or it is no longer probable that the forecasted transaction will occur by the end of the originally specified time period. If we determine that the derivative no longer qualifies as a fair value or cash flow hedge and therefore hedge accounting is discontinued, the derivative will continue to be recorded on the balance sheet at its fair value with changes in fair value included in current earnings. For a discontinued fair value hedge, the previously hedged item is no longer adjusted for changes in fair value.

When hedge accounting is discontinued because it is no longer probable that a forecasted transaction will occur, the derivative will continue to be recorded on the balance sheet at its fair value with changes in fair value included in current earnings, and the gains and losses in accumulated other comprehensive income or loss will be recognized immediately into earnings. When we discontinue hedge accounting because the hedging instrument is sold, terminated or no longer designated, the amount reported in other comprehensive income or loss up to the date of sale, termination or de-designation continues to be reported in other

comprehensive income or loss until the forecasted transaction affects earnings.

We did not terminate any cash flow hedges in 2006, 2005 or 2004 due to a determination that a forecasted transaction was no longer probable of occurring.

We occasionally purchase or originate financial instruments that contain an embedded derivative. Prior to January 1, 2006, we assessed at the inception of the transaction if economic characteristics of the embedded derivative were clearly and closely related to the economic characteristics of the financial instrument (host contract), whether the financial instrument that embodied both the embedded derivative and the host contract were measured at fair value with changes in fair value reported in earnings, and whether a separate instrument with the same terms as the embedded instrument would not meet the definition of a derivative. If the embedded derivative did not meet these three conditions, the embedded derivative would qualify as a derivative and be recorded apart from the host contract and carried at fair value with changes recorded in current earnings. On January 1, 2006, we adopted SFAS 155, which, among other provisions, permits a fair value election for hybrid financial instruments requiring bifurcation on an instrument-by-instrument basis. Beginning January 1, 2006, we elected to account for certain previously bifurcated hybrid instruments and certain newly acquired hybrid instruments under this fair value election on an instrument-by-instrument basis. As such, certain previously reported embedded derivatives are now reported with their host contracts at fair value in loans or other borrowed funds.

We enter into commitments to make loans whereby the interest rate on the loan is set prior to funding (interest rate lock commitments). We also enter into commitments to purchase mortgage loans (purchase commitments). Both interest rate lock commitments and purchase commitments on mortgage loans that will be held for resale are accounted for as free-standing derivatives. Interest rate lock commitments and purchase commitments that are considered to be derivatives are recorded at fair value in other assets or other liabilities. Fair value of interest rate lock commitments and purchase commitments is determined as the change in value that occurs after the inception of the commitment considering the projected security price, fees collected from the borrower and costs to originate, adjusted for anticipated fallout risk. We recognize the gain or loss from the change in fair value of these derivatives in trading noninterest income.

Income Taxes

We account for income taxes under the asset and liability method. Deferred tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that we expect will apply at the time when we believe the differences will reverse.

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Earnings Per Common Share

We calculate basic earnings per common share by dividing net income adjusted for preferred stock dividends declared by the weighted-average number of shares of common stock outstanding.

Diluted earnings per common share are based on net income available to common stockholders. We increase the weighted-average number of shares of common stock outstanding by the assumed conversion of outstanding convertible preferred stock and debentures from the beginning of the year or date of issuance, if later, and the number of shares of common stock that would be issued assuming the exercise of stock options and the issuance of incentive shares using the treasury stock method. These adjustments to the weighted-average number of shares of common stock outstanding are made only when such adjustments will dilute earnings per common share.

Stock-Based Compensation

We did not recognize stock-based employee compensation expense related to stock options granted before 2003 under prior GAAP.

Effective January 1, 2003, we adopted the fair value recognition provisions of SFAS 123, Accounting for Stock-Based Compensation, as amended by SFAS 148, Accounting for Stock-Based Compensation-Transition and Disclosure, prospectively to all employee awards granted, modified or settled after January 1, 2003. We did not restate results for prior years upon our adoption of SFAS 123. Since we adopted SFAS 123 prospectively, the cost related to stock-based employee compensation included in net income for 2005 and 2004 was less than what we would have recognized if we had applied the fair value based method to all awards since the original effective date of the standard.

In December 2004, the FASB issued SFAS 123R Share Based Payment, which replaced SFAS 123 and superseded APB 25. SFAS 123R requires compensation cost related to share-based payments to employees to be recognized in the financial statements based on their fair value. We adopted SFAS 123R effective January 1, 2006, using the modified prospective method of transition, which requires the provisions of SFAS 123R be applied to new awards and awards modified, repurchased or cancelled after the effective date. It also requires changes in the timing of expense recognition for awards granted to retirement-eligible employees and clarifies the accounting for the tax effects of stock awards. The adoption of SFAS 123R did not have a significant impact on our consolidated financial statements.

The following table shows the effect on net income and earnings per share if we had applied the fair value recognition provisions of SFAS 123, as amended, to all outstanding and unvested awards in each period.

Pro Forma Net Income And Earnings Per Share

	Year ended December 31		
In millions, except for per share data	**2006**	2005	2004
Net income	**$2,595**	$1,325	$1,197
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects	**63**	54	33
Deduct: Total stock-based employee compensation expense determined under the fair value method for all awards, net of related tax effects	**(63)**	(60)	(50)
Pro forma net income	**$2,595**	$1,319	$1,180
Earnings per share			
Basic-as reported	**$8.89**	$4.63	$4.25
Basic-pro forma	**8.89**	4.60	4.19
Diluted-as reported	**$8.73**	$4.55	$4.21
Diluted-pro forma	**8.73**	4.52	4.15

See Note 18 Stock-Based Compensation Plans for additional information.

Recent Accounting Pronouncements

In February 2007, the FASB issued SFAS 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115. This statement permits entities to choose to measure many financial instruments and certain other items at fair value.

The fair value option may be applied on an instrument by instrument basis with a few exceptions. The election is irrevocable and must be applied to entire instruments and not to portions of instruments. For PNC, the election to apply the standard and measure certain financial instruments at fair value would be effective prospectively beginning January 1, 2008.

During 2006, the FASB issued the following:

SFAS 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R). This statement affects the accounting and reporting for our qualified pension plan, our nonqualified retirement plans, our postretirement welfare benefit plans and our postemployment benefit plan. SFAS 158 requires recognition on the balance sheet of the over- or underfunded position of these plans as the difference between the fair value of plan assets and the related benefit obligations. To the extent that a plan s net funded status differs from the amounts currently recognized on the balance sheet, the difference, net of tax, will be recorded as part of accumulated other comprehensive income or loss (AOCI) within the shareholders equity section of the balance sheet. This guidance also requires the recognition of any unrecognized actuarial gains and losses and unrecognized prior service costs to AOCI, net of tax. Post-adoption changes in unrecognized actuarial gains and losses as well as unrecognized

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prior service costs will be recognized in other comprehensive income, net of tax. SFAS 158 was effective for PNC as of December 31, 2006, with no restatements permitted for prior year-end reporting periods. The year-end 2006 adjustment to our plans funded status for all unamortized net actuarial losses and prior service costs was $132 million after tax. The following table summarizes the effect of the initial impact of adopting SFAS 158.

Incremental Effect of Applying SFAS 158 on Individual Line Items in the Consolidated Balance Sheet December 31, 2006

In millions	Before Application of SFAS 158	Adjustments	After Application of SFAS 158
Other assets	$ 9,117	$ (188)	$ 8,929
Total assets	102,008	(188)	101,820
Other liabilities	4,784	(56)	4,728
Total liabilities	90,203	(56)	90,147
Accumulated other comprehensive loss	(103)	(132)	(235)
Total shareholders equity	$ 10,920	$ (132)	$ 10,788

SFAS 157, Fair Value Measurements, defines fair value and establishes a framework for measuring fair value which includes permissible valuation techniques and a hierarchy of inputs utilized in the measurement process. This statement applies whenever other accounting standards require or permit fair value measurement. We anticipate applying SFAS 157 prospectively beginning January 1, 2008, as required.

FASB Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in the financial statements and sets forth recognition, derecognition and measurement criteria for tax positions taken or expected to be taken in a tax filing. For PNC, this guidance will apply to all tax positions taken or expected to be taken beginning on January 1, 2007. We do not expect the adoption of FIN 48 to have a significant impact on our consolidated financial statements.

FASB Staff Position No. (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 guidance requires a recalculation of the timing of income recognition for a leveraged lease under SFAS 13, Accounting for Leases, when a change in the timing of income tax deductions directly related to the leveraged lease transaction occurs or is projected to occur. Any tax positions taken regarding the leveraged lease transaction must be recognized and
measured in accordance with FIN 48 described above. This guidance will be effective for PNC beginning January 1, 2007 with the cumulative effect of applying the provisions of this FSP being recognized through an adjustment to opening retained earnings. Any immediate or future reductions in earnings from the change in accounting would be recovered in subsequent years. Our adoption of the guidance in FSP FAS 13-2 resulted in an after-tax charge to beginning retained earnings at January 1, 2007 of approximately $149 million.

As described under the Loans And Leases section of the Note 1, we adopted SFAS 155 as of January 1, 2006. As described under the Loan Sales, Securitizations And Retained Interest section of Note 1, we also adopted SFAS 156 as of January 1, 2006. The adoption of SFAS 155 and SFAS 156 did not have a material impact on our consolidated financial statements.

In June 2005, the Emerging Issues Task Force (EITF) of the FASB issued EITF Issue 04-5, Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights. EITF 04-5 provides that the general partner(s) is presumed to control the limited partnership (including certain limited liability companies), unless the limited partners possess either substantive participating rights or the substantive ability to dissolve the limited partnership or otherwise remove the general partner(s) without cause (kick-out rights). Kick-out rights are substantive if they can be exercised by a simple majority of the limited partners voting interests. The guidance was effective for all limited partnerships as of January 1, 2006. The adoption of this guidance did not have a material impact on our consolidated financial statements.

NOTE 2 ACQUISITIONS

2006

BlackRock/MLIM Transaction

On September 29, 2006, Merrill Lynch contributed its investment management business (MLIM) to BlackRock in exchange for 65 million shares of newly issued BlackRock common and preferred stock. BlackRock accounted for the MLIM transaction under the purchase method of accounting.

Immediately following the closing, PNC continued to own approximately 44 million shares of BlackRock common stock representing an ownership interest of approximately 34% of the combined company (as compared with 69% immediately prior to the closing). Although PNC s share ownership percentage declined, PNC s investment in BlackRock increased due to the increase in total equity recorded by BlackRock as a result of the MLIM transaction.

Upon the closing of the BlackRock/MLIM transaction, the carrying value of our investment in BlackRock increased by approximately $3.1 billion to $3.8 billion, primarily reflecting

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PNC s portion of the increase in BlackRock s equity resulting from the value of shares issued in the transaction.

We also recorded a liability at September 30, 2006 for deferred taxes of approximately $.9 billion, related to the excess of the book value over the tax basis of our investment in BlackRock, and a liability of approximately $.6 billion related to our obligation to provide shares of BlackRock common stock to help fund BlackRock long-term incentive plan (LTIP) programs. The LTIP liability will be adjusted quarterly based on changes in BlackRock s common stock price and the number of remaining committed shares. Accordingly, at each quarter-end PNC will record a charge to earnings if the market price of BlackRock s common stock increases and will record a credit to earnings if BlackRock s stock price declines.

The overall balance sheet impact of the BlackRock/MLIM transaction was an increase to our shareholders equity of approximately $1.6 billion. The increase to equity was comprised of an after-tax gain of approximately $1.3 billion, net of the expense associated with the LTIP liability and the deferred taxes, and an after-tax increase to capital surplus of approximately $.3 billion. The recognition of the gain is consistent with our existing accounting policy for the sale or issuance by subsidiaries of their stock to third parties. The gain represents the difference between our basis in BlackRock stock prior to the BlackRock/MLIM transaction and the new book value per share and resulting increase in value of our investment realized from the transaction. The direct increase to capital surplus rather than inclusion in the gain resulted from the accounting treatment required due to existing BlackRock repurchase commitments or programs.

For 2004, 2005 and for the nine months ended September 30, 2006, our Consolidated Income Statement included our former approximately 69% - 71% ownership interest in BlackRock s net income through the closing date. However, beginning September 30, 2006, our Consolidated Balance Sheet no longer reflected the consolidation of BlackRock s balance sheet but recognized our ownership interest in BlackRock as an investment accounted for under the equity method. This accounting has resulted in a reduction in certain revenue and noninterest expense categories on PNC s Consolidated Income Statement as our share of BlackRock s net income is now reported within asset management noninterest income.

Mercantile Bankshares Corporation

On October 8, 2006 we entered into a definitive agreement with Mercantile Bankshares Corporation (Mercantile) for PNC to acquire Mercantile. Mercantile shareholders will be entitled to .4184 shares of PNC common stock and $16.45 in cash for each share of Mercantile, or in the aggregate approximately 53 million shares of PNC common stock and $2.1 billion in cash. Based on PNC s recent stock prices, the transaction is valued at approximately $6.0 billion in the aggregate.

Mercantile is a bank holding company with approximately $18 billion in assets that provides banking and investment and wealth management services through 240 offices in Maryland, Virginia, the District of Columbia, Delaware and southeastern Pennsylvania. The transaction is expected to close in March 2007 and is subject to customary closing conditions, including regulatory approvals. See Note 13 Borrowed Funds regarding February 2007 debt issuances related to this planned acquisition.

2005

SSRM Holdings, Inc.

Effective January 31, 2005, BlackRock closed the acquisition of SSRM Holdings, Inc. (SSRM), the holding company of State Street Research & Management Company and SSR Realty Advisors Inc., from MetLife, Inc. for an adjusted purchase price of approximately $265 million in cash and approximately 550,000 shares of BlackRock restricted class A common stock valued at $37 million. SSRM, through its subsidiaries, actively manages stock, bond, balanced and real estate portfolios for both institutional and individual investors. Substantially all of SSRM s operations were integrated into BlackRock as of the closing date. BlackRock acquired assets under management totaling $50 billion in connection with this transaction.

On January 18, 2005, our ownership in BlackRock was transferred from PNC Bank, N.A. to PNC Bancorp, Inc., our intermediate bank holding company. The transfer was effected primarily to give BlackRock more operating flexibility, particularly in connection with its acquisition of SSRM. As a result of the transfer, certain deferred tax liabilities recorded by PNC were reversed in the first quarter of 2005 in accordance with SFAS 109, Accounting for Income Taxes. The reversal of deferred tax liabilities increased our earnings by $45 million, or approximately $.16 per diluted share, in the first quarter of 2005.

Riggs National Corporation

We acquired Riggs National Corporation (Riggs), a Washington, D.C. based banking company, effective May 13, 2005. Under the terms of the agreement, Riggs merged into The PNC Financial Services Group, Inc. and PNC Bank, National Association (PNC Bank, N.A.) acquired substantially all of the assets of Riggs Bank, National Association, the principal banking subsidiary of Riggs. The acquisition gave us a substantial presence on which to build a market leading franchise in the affluent Washington, D.C. metropolitan area. In connection with the acquisition, Riggs shareholders received an aggregate of approximately $297 million in cash and 6.6 million shares of PNC common stock valued at $356 million.

Harris Williams & Co.

On October 11, 2005, we acquired Harris Williams & Co., one of the nation s largest firms focused on providing mergers and acquisitions advisory and related services to middle market companies, including private equity firms and private and public companies.

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NOTE 3 VARIABLE INTEREST ENTITIES

We are involved with various entities in the normal course of business that may be deemed to be VIEs. We consolidated certain VIEs as of December 31, 2006 and 2005 for which we were determined to be the primary beneficiary.

We hold significant variable interests in VIEs that have not been consolidated because we are not considered the primary beneficiary. Information on these VIEs follows:

Non-Consolidated VIEs Significant Variable Interests

In millions	Aggregate Assets	Aggregate Liabilities	PNC Risk of Loss
December 31, 2006			
Market Street	**$ 4,020**	**$ 4,020**	**$ 6,117(a)**
Collateralized debt obligations	**815**	**570**	**22**
Partnership interests in low income housing projects	**33**	**30**	**8**
Total	**$ 4,868**	**$ 4,620**	**$ 6,147**
December 31, 2005			
Collateralized debt obligations (b)	$ 6,290	$ 5,491	$ 51
Private investment funds (b)	5,186	1,051	13
Market Street	3,519	3,519	5,089 (a)
Partnership interests in low income housing projects	35	29	2
Total	$ 15,030	$ 10,090	$ 5,155

(a) PNC s risk of loss consists of off-balance sheet liquidity commitments to Market Street of $5.6 billion and other credit enhancements of $.6 billion at December 31, 2006. The comparable amounts at December 31, 2005 were $4.6 billion and $.4 billion, respectively.

(b) Primarily held by BlackRock. We deconsolidated BlackRock effective September 29, 2006. See Note 2 Acquisitions for additional information. Includes both PNC s direct risk of loss and BlackRock s risk of loss, limited to PNC s ownership interest in BlackRock.

The aggregate assets and liabilities of VIEs that we have consolidated in our financial statements are as follows:

Consolidated VIEs PNC Is Primary Beneficiary

In millions	Aggregate Assets	Aggregate Liabilities
December 31, 2006		
Partnership interests in low income housing projects	**$ 834**	**$ 834**
Total	**$ 834**	**$ 834**
December 31, 2005		
Partnership interests in low income housing projects	$ 680	$ 680
Other	12	10
Total	$ 692	$ 690

MARKET STREET

Market Street Funding LLC (Market Street), formerly Market Street Funding Corporation, is a multi-seller asset-backed commercial paper conduit that is owned by an independent third party. Market Street s activities are limited to the purchasing of assets or making of loans secured by

interests primarily in pools of receivables from US corporations that desire access to the commercial paper market. Market Street funds the purchases or loans by issuing commercial paper which has been rated A1/P1 by Standard & Poor s and Moody s, respectively, and is supported by pool-specific credit enhancement, liquidity facilities and program-level credit enhancement.

PNC Bank, N.A. provides certain administrative services, a portion of the program-level credit enhancement and the majority of liquidity facilities to Market Street in exchange for fees negotiated based on market rates. All of Market Street s assets at December 31, 2006 and 2005 collateralize the commercial paper obligations. PNC views its credit exposure for the Market Street transactions as limited. Facilities requiring PNC to fund for defaulted assets totaled $850 million at December 31, 2006. For 85% of the liquidity facilities at December 31, 2006, PNC is not required to fund if the assets are in default. PNC may be liable for funding under liquidity facilities for events such as borrower bankruptcies, collateral deficiencies or covenant violations. Additionally, PNC s obligations under the liquidity facilities are secondary to the risk of first loss provided by the borrower or another third party in the form of deal-specific credit enhancement for example, by the over collateralization of the assets. Deal-specific credit enhancement that supports the commercial paper issued by Market Street is generally structured to cover a multiple of the expected historical losses for the pool of assets and is sized to generally meet rating agency standards for comparably structured transactions. Credit enhancement is provided in part by PNC Bank, N.A. in the form of a cash collateral account that is funded by a loan facility that expires March 25, 2011. See Note 7 Loans, Commitments To Extend Credit and Concentrations of Credit Risk and Note 24 Commitments and Guarantees for additional information. Neither creditors nor equity investors in Market Street have any recourse to our general credit. PNC accrued program administrator fees and commitment fees related to PNC s portion of the liquidity facilities of $11.3 million and $3.7 million, respectively, for the year ended December 31, 2006.

Under the provisions of FASB Interpretation No. 46, Consolidation of Variable Interest Entities (FIN 46), we consolidated Market Street effective July 1, 2003 as we were deemed the primary beneficiary of Market Street. In October 2005, Market Street was restructured as a limited liability company and entered into a subordinated Note Purchase Agreement (Note) with an unrelated third party. Consistent with other market participants PNC elected to restructure Market Street and Market Street issued the Note for the primary purpose of providing our customers access to the asset-backed commercial paper markets in a more capital-efficient manner.

The Note provides first loss coverage whereby the investor absorbs losses up to the amount of the Note, which is $5.7 million as of December 31, 2006. The Note has an original maturity of eight years and bears interest at 18% with any default-related interest/fees charged by Market Street on specific transactions accruing to the benefit of the Note holder. Proceeds from the issuance of the Note were placed in a first loss reserve account that may be used to reimburse any losses incurred by Market Street, PNC Bank, N.A. or other providers under the liquidity facilities and the credit enhancement arrangements.

As a result of the Note issuance, we reevaluated whether PNC continued to be the primary beneficiary of Market Street under the provisions of FIN 46R. PNC evaluated the design of Market Street, its capital structure and relationships among the variable interest holders. PNC also performed a quantitative analysis, which computes and allocates expected loss or residual returns to variable interest holders. PNC considered variability generated from the risks specific to Market Street such as expected credit losses, facility pricing (including default-related pricing), and fee volatility in determining that the Note investor absorbed the majority of the expected variability and therefore is the primary beneficiary and required to consolidate Market Street. Based on this analysis, we determined that we were no longer the primary beneficiary and deconsolidated Market Street from our Consolidated Balance Sheet effective October 17, 2005.

As required under FIN 46R, reconsideration events such as changes in the Note contractual terms, additional Note investors and or changes in the inherent Market Street risks would trigger PNC to determine if the primary beneficiary has changed.

Low Income Housing Projects

We make certain equity investments in various limited partnerships that sponsor affordable housing projects utilizing the Low Income Housing Tax Credit (LIHTC) pursuant to Section 42 of the Internal Revenue Code. The purpose of these investments is to achieve a satisfactory return on capital, to facilitate the sale of additional affordable housing product offerings and to assist us in achieving goals associated with the Community Reinvestment Act. The primary activities of the limited partnerships include the identification, development and operation of multi-family housing that is leased to qualifying residential tenants. Generally, these types of investments are funded through a combination of debt and equity, with equity typically comprising 30% to 60% of the total project capital.

We consolidated those LIHTC investments in which we own a majority of the limited partnership interests. We also consolidated entities in which we, as a national syndicator of affordable housing equity, serve as the general partner (together with the aforementioned LIHTC investments), and no other entity owns a majority of the limited partnership interests. In these syndication transactions, we create funds in which our subsidiary is the general partner and sells limited partnership interests to third parties, and in some cases may also purchase a limited partnership interest in the fund. The

fund s limited partners can generally remove the general partner without cause at any time. The purpose of this business is to generate income from the syndication of these funds and to generate servicing fees by managing the funds. General partner activities include selecting, evaluating, structuring, negotiating, and closing the fund investments in operating limited partnerships, as well as oversight of the ongoing operations of the fund portfolio. The assets are primarily included in Equity Investments on our Consolidated Balance Sheet. Neither creditors nor equity investors in the LIHTC investments have any recourse to our general credit. The consolidated aggregate assets and debt of these LIHTC investments are provided in the Consolidated VIEs PNC Is Primary Beneficiary table and reflected in the Corporate & Institutional Banking business segment.

We have a significant variable interest in certain other limited partnerships that sponsor affordable housing projects. We do not own a majority of the limited partnership interests in these entities and are not the primary beneficiary. We use the equity method to account for our investment in these entities. Information regarding these partnership interests is reflected in the Non-Consolidated VIEs Significant Variable Interests table.

We also have subsidiaries that invest in and act as the investment manager for private equity funds organized as limited partnerships as part of our equity management activities. The funds invest in private equity investments to generate capital appreciation and profits. As permitted by FIN 46R, we have deferred applying the provisions of the interpretation for these entities pending further action by the FASB. Information on these entities follows:

Investment Company Accounting Deferred Application

In millions	Aggregate Assets	Aggregate Equity	PNC Risk of Loss
Private Equity Funds			
December 31, 2006	**$ 102**	**$ 102**	**$ 104**

December 31, 2005	$ 109	$ 109	$ 35

PNC s risk of loss in the tables above includes both the value of our equity investments and any unfunded commitments to the respective entities.

Perpetual Trust Securities

In December 2006, one of our indirect subsidiaries, PNC REIT Corp., sold $500 million of 6.517% Fixed-to-Floating Rate Non-Cumulative Exchangeable Perpetual Trust Securities (the Trust Securities) of PNC Preferred Funding Trust I, in a private placement. PNC REIT Corp. had previously acquired the Trust Securities from the trust in exchange for an equivalent amount of Fixed-to-Floating Rate Non-Cumulative Perpetual Preferred Securities (the LLC Preferred Securities), of PNC Preferred Funding LLC, (the LLC), held by PNC REIT Corp. The LLC s initial material assets consist of indirect interests in mortgages and mortgage-related assets previously owned by PNC REIT Corp.

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PNC REIT Corp. also owns 100% of the LLC s common voting securities. As a result, the LLC is an indirect subsidiary of PNC Bank, N.A. and is consolidated on our Consolidated Balance Sheet. PNC Preferred Funding Trust I s investment in the LLC Preferred Securities is characterized as a minority interest on our Consolidated Balance Sheet since we are not the primary beneficiary of PNC Preferred Funding Trust I. This minority interest totaled $490 million at December 31, 2006.

NOTE 4 REGULATORY MATTERS

We are subject to the regulations of certain federal and state agencies and undergo periodic examinations by such regulatory authorities.

The access to and cost of funding new business initiatives including acquisitions, the ability to pay dividends, the level of deposit insurance costs, and the level and nature of regulatory oversight depend, in large part, on a financial institution s capital strength. The minimum regulatory capital ratios are 4% for tier 1 risk-based, 8% for total risk-based and 4% for leverage. However, regulators may require higher capital levels when particular circumstances warrant. To qualify as well capitalized, regulators require banks to maintain capital ratios of at least 6% for tier 1 risk-based, 10% for total risk-based and 5% for leverage. At December 31, 2006 and December 31, 2005, each of our bank subsidiaries met the well capitalized capital ratio requirements. We believe our bank subsidiaries will continue to meet these requirements in 2007.

The following table sets forth regulatory capital ratios for PNC and its only significant bank subsidiary, PNC Bank, N.A.

Regulatory Capital

December 31	Amount		Ratios	
Dollars in millions	**2006**	2005	**2006**	2005
Risk-based capital				
Tier 1				
PNC	**$ 8,924**	$ 6,364	**10.4%**	8.3%
PNC Bank, N.A.	**6,159**	5,694	**8.0**	8.0
Total				
PNC	**11,559**	9,277	**13.5**	12.1
PNC Bank, N.A.	**8,541**	8,189	**11.1**	11.5
Leverage				
PNC	**NM**	NM	**9.3**	7.2
PNC Bank, N.A.	**NM**	NM	**7.2**	7.0

NM - Not Meaningful

The principal source of parent company cash flow is the dividends it receives from PNC Bank, N.A., which may be impacted by the following:

- Capital needs,
- Laws and regulations,
- Corporate policies,
- Contractual restrictions, and
- Other factors.

Also, there are statutory and regulatory limitations on the ability of national banks to pay dividends or make other capital distributions. The amount available for dividend payments to the parent company by PNC Bank, N.A. without prior regulatory approval was approximately $625 million at December 31, 2006.

Under federal law, bank subsidiaries generally may not extend credit to the parent company or its non-bank subsidiaries on terms and under circumstances that are not substantially the same as comparable extensions of credit to nonaffiliates. No extension of credit may be made to the parent company or a non-bank subsidiary which is in excess of 10% of the capital stock and surplus of such bank subsidiary or in excess of 20% of the capital and surplus of such bank subsidiary as to aggregate extensions of credit to the parent company and its non-bank subsidiaries. Such extensions of credit, with limited exceptions, must be fully collateralized by certain specified assets. In certain circumstances, federal regulatory authorities may impose more restrictive limitations.

Federal Reserve Board regulations require depository institutions to maintain cash reserves with the Federal Reserve Bank (FRB). During 2006, subsidiary banks maintained reserves which averaged $203 million.

NOTE 5 LEGAL PROCEEDINGS

Some of our subsidiaries are defendants (or have potential contractual contribution obligations to other defendants) in several pending lawsuits brought during late 2002 and 2003 arising out of the bankruptcy of Adelphia Communications Corporation and its subsidiaries. There also are threatened additional proceedings arising out of the same matters. One of the lawsuits was brought on Adelphia s behalf by the unsecured creditors committee and equity committee in Adelphia s consolidated bankruptcy proceeding and was removed to the United States District Court for the Southern District of New York by order dated February 9, 2006. The other lawsuits, one of which is a putative consolidated class action, were brought by holders of debt and equity securities of Adelphia and have been consolidated for pretrial purposes in that district court. These lawsuits arise out of lending and securities underwriting activities engaged in by these PNC subsidiaries together with other financial services companies. In the aggregate, more than 400 other financial services companies and numerous other companies and individuals have been named as defendants in one or more of the lawsuits. Collectively, with respect to some or all of the defendants, the lawsuits allege federal law claims, including violations of federal securities and other federal laws, violations of common law duties, aiding and abetting such violations, voidable preference payments, and fraudulent transfers, among other matters. The lawsuits seek unquantified monetary damages, interest, attorneys fees and other expenses, and a return of the alleged voidable preference and fraudulent transfer payments, among other remedies. The bank defendants, including the PNC defendants, have entered into a settlement of the consolidated class action referred to above.

This settlement was approved by the district court in November 2006. In December 2006, a group of class members appealed the order approving the settlement agreement to the United States Court of Appeals for the Second Circuit. The amount for which we would be responsible under this settlement is insignificant. We believe that we have defenses to the claims against us in these lawsuits, as well as potential claims against third parties, and intend to defend the remaining lawsuits vigorously. These lawsuits involve complex issues of law and fact, presenting complicated relationships among the many financial and other participants in the events giving rise to these lawsuits, and have not progressed to the point where we can predict the outcome of the remaining lawsuits other than the one for which a settlement is pending. It is not possible to determine what the likely aggregate recoveries on the part of the plaintiffs in these remaining matters might be or the portion of any such recoveries for which we would ultimately be responsible, but the final consequences to PNC could be material.

In April 2005, an amended complaint was filed in the putative class action against PNC, PNC Bank, N.A., our Pension Plan and its Pension Committee in the United States District Court for the Eastern District of Pennsylvania (originally filed in December 2004). The complaint claims violations of the Employee Retirement Income Security Act of 1974, as amended (ERISA), arising out of the January 1, 1999 conversion of our Pension Plan from a traditional defined benefit formula into a cash balance formula, the design and continued operation of the Plan, and other related matters. Plaintiffs seek to represent a class of all current and former employee-participants in and beneficiaries of the Plan as of December 31, 1998 and thereafter. Plaintiffs also seek to represent a subclass of all current and former employee participants in and beneficiaries of the Plan as of December 31, 1998 and thereafter who were or would have become eligible for an early retirement subsidy under the former Plan at some time prior to the date of the amended complaint. The plaintiffs are seeking unquantified damages and equitable relief available under ERISA, including interest, costs, and attorneys fees. In November 2005, the court granted our motion to dismiss the amended complaint. Plaintiffs appealed this ruling to the United States Court of Appeals for the Third Circuit, which affirmed the district court ruling in an opinion dated January 30, 2007. On February 13, 2007, plaintiffs filed in the court of appeals a petition for rehearing. Plaintiffs may seek further judicial review of the dismissal of their complaint.

In March 2006, a first amended complaint was filed in the United States District Court for the Eastern District of Texas by Data Treasury Corporation against PNC and PNC Bank, N.A., as well as more than 50 other financial institutions, vendors, and other companies, claiming that the defendants are infringing, and inducing or contributing to the infringement of, the plaintiff s patents, which allegedly involve check imaging, storage and transfer. The plaintiff

seeks unspecified damages and interest and trebling of both, attorneys fees and other expenses, and injunctive relief against the alleged infringement. We are not in a position to assess the likely outcome of this matter, including our exposure, if any. We believe that we have defenses to the claims against us in this lawsuit and intend to defend it vigorously. In January 2007, the district court entered an order staying the claims asserted against PNC under two of the four patents allegedly infringed by PNC, pending reexamination of these patents by the United States Patent and Trademark Office. The lawsuit will proceed with respect to the other two patents. Further, the stay may be lifted once the Patent and Trademark Office completes its reexamination.

In August 2006, a lawsuit was filed in the United States District Court for the Eastern District of Texas by Ronald A. Katz Technology Licensing L. P. (RAKTL) against PNC, PNC Bank, N.A., and other defendants. In September 2006, this lawsuit was divided into separate actions, and amended complaints were then filed, one of which was against PNC and PNC Bank, N.A. This lawsuit is one of many related RAKTL patent infringement actions pending in various federal district courts against a large number of defendants. Each of the actions involves a single family of related patents that RAKTL refers to as the interactive call processing patents. The amended complaint alleged that PNC and PNC Bank, N.A. are infringing, and inducing or contributing to the infringement of, certain of the plaintiff s patents. In January 2007, the court dismissed the lawsuit against PNC following a settlement under which PNC and its affiliates received a non-exclusive license covering patents held by RAKTL. As part of the settlement, we agreed to pay a licensing fee to RAKTL. The amount of the fee is not material to PNC.

In its Form 10-Q for the quarter ended March 31, 2005, Riggs disclosed a number of pending lawsuits. All material lawsuits have been finally resolved, except one where a settlement agreement has been reached, subject to final documentation. The pending settlement is not material to PNC.

As a result of the acquisition of Riggs, PNC is now responsible for Riggs obligations to provide indemnification to its directors, officers, and, in some cases, employees and agents against certain liabilities incurred as a result of their service on behalf of or at the request of Riggs. PNC is also now responsible for Riggs obligations to advance on behalf of covered individuals costs incurred in connection with certain claims or proceedings, subject to written undertakings to repay all amounts so advanced if it is ultimately determined that the individual is not entitled to indemnification. Since the acquisition, we have advanced such costs on behalf of covered individuals from Riggs and expect to continue to do so in the future at least with respect to lawsuits and other legal matters identified in Riggs first quarter 2005 Form 10-Q.

There are several pending judicial or administrative proceedings or other matters arising out of the three 2001 PAGIC transactions. These pending proceedings or other

matters are described below. Among the requirements of a June 2003 Deferred Prosecution Agreement that one of our subsidiaries entered into relating to the PAGIC transactions was the establishment of a Restitution Fund through our $90 million contribution. The Restitution Fund will be available to satisfy claims, including for the settlement of the pending securities litigation referred to below. Louis W. Fryman, chairman of Fox Rothschild LLP in Philadelphia, Pennsylvania, is administering the Restitution Fund.

In December 2004 and January and March 2005, we entered into settlement agreements relating to certain of the lawsuits and other claims arising out of the PAGIC transactions. These settlements are described below, following a description of each of these pending proceedings and other matters.

The several putative class action complaints filed during 2002 in the United States District Court for the Western District of Pennsylvania arising out of the PAGIC transactions were consolidated in a consolidated class action complaint brought on behalf of purchasers of our common stock between July 19, 2001 and July 18, 2002 (the Class Period). The consolidated class action complaint names PNC, our Chairman and Chief Executive Officer, our former Chief Financial Officer, our Controller, and our independent auditors for 2001 as defendants and seeks unquantified damages, interest, attorneys fees and other expenses. The consolidated class action complaint alleges violations of federal securities laws related to disclosures regarding the PAGIC transactions and related matters.

In August 2002, the United States Department of Labor began a formal investigation of the Administrative Committee of our Incentive Savings Plan (Plan) in connection with the Administrative Committee s conduct relating to our common stock held by the Plan. Both the Administrative Committee and PNC have cooperated fully with the investigation. In June 2003, the Administrative Committee retained Independent Fiduciary Services, Inc. (IFS) to serve as an independent fiduciary charged with the exclusive authority and responsibility to act on behalf of the Plan in connection with the pending securities class action litigation referred to above and to evaluate any legal rights the Plan might have against any parties relating to the PAGIC transactions. This authority includes representing the Plan s interests in connection with the Restitution Fund set up under the Deferred Prosecution Agreement. The Department of Labor has communicated with IFS in connection with the engagement.

We received a letter in June 2003 on behalf of an alleged shareholder demanding that we take appropriate legal action against our Chairman and Chief Executive Officer, our former Chief Financial Officer, and our Controller, as well as any other individuals or entities allegedly responsible for causing damage to PNC as a result of the PAGIC transactions. The Board referred this matter to a special committee of the Board for evaluation. The special committee completed its evaluation and reported its findings to the Board of Directors

and to counsel for the alleged shareholder. The special committee recommended against bringing any claims against our current or former executive officers but made certain recommendations with respect to resolution of potential claims we had with respect to certain other third parties.

In July 2003, the lead underwriter on our Executive Blended Risk insurance coverage filed a lawsuit for a declaratory judgment against PNC and PNC ICLC in the United States District Court for the Western District of Pennsylvania. The complaint seeks a determination that the defendants breached the terms and conditions of the policy and, as a result, the policy does not provide coverage for any loss relating to or arising out of the Department of Justice investigation or the PAGIC transactions. Alternatively, the complaint seeks a determination that the policy does not provide coverage for the payments made pursuant to the Deferred Prosecution Agreement. The complaint also seeks attorneys fees and costs. In July 2004, the court granted our motion to stay the action until resolution of the claims against PNC in the pending consolidated class action described above.

In December 2004, we entered into a tentative settlement of the consolidated class action. In March 2005, the parties filed a stipulation of settlement of this lawsuit with the United States District Court for the Western District of Pennsylvania. This settlement also covered claims by the plaintiffs against AIG Financial Products and others related to the PAGIC transactions.

In July 2006, the district court approved this settlement. The defendant in that class action not participating in this settlement, our former independent auditors for the years ended 2001 and before, had objected to it and, on August 10, 2006, appealed the decision of the district court approving the settlement to the United States Court of Appeals for the Third Circuit.

On December 20, 2006, our former independent auditors for the years ended 2001 and before filed with the district court a tentative settlement agreement with the plaintiffs regarding the plaintiffs claims against it. This tentative settlement remains subject to court approval. If this tentative settlement agreement is finally approved by the court and after it becomes effective, this defendant will dismiss its appeal of the court s approval of our settlement, which would then become final.

In December 2004, we also settled all claims between us, on the one hand, and AIG Financial Products and its affiliate, American International Surplus Lines Insurance Company (AISLIC), on the other hand, related to the PAGIC transactions. AIG Financial Products was our counterparty in the PAGIC transactions, and AISLIC is one of the insurers under our Executive Blended Risk insurance coverage. Subsequently, we settled claims against two of the other insurers under our Executive Blended Risk insurance coverage, as described below. Each of the amounts in these

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settlements represents a portion of the insurer s share of our overall claim against our insurers with respect to any amounts disbursed out of the Restitution Fund. We are preserving our claim against our insurers with which we have not settled.

The following are the key elements of these settlements that remain conditional at present, pending resolution of the appeal of the district court s approval of the settlement of the consolidated class action:

Payments into Settlement Fund. The insurers under our Executive Blended Risk insurance coverage have funded $30 million to be used for the benefit of the class. Third parties have funded additional amounts to be used for the same purpose. The plaintiffs have been in contact with Mr. Fryman, the administrator of the Restitution Fund, and intend to coordinate the administration and distribution of these settlement funds with the distribution of the Restitution Fund. Neither PNC nor any of our current or former officers, directors or employees will be required to contribute any funds to this settlement.

Assignment of Claims. We have assigned to the plaintiffs claims we may have against our former independent auditors for the years ended 2001 and before and all other unaffiliated third parties (other than AIG Financial Products and its predecessors, successors, parents, subsidiaries, affiliates and their respective directors, officers and employees (collectively, AIG)) relating to the subject matter of this lawsuit.

Insurance Claims. In March 2005, we settled our claim against one of our insurers under our Executive Blended Risk insurance coverage related to our contribution of $90 million to the Restitution Fund. Under this settlement, the insurer has paid us $11.25 million, but we are obligated to return this amount if the settlement of the consolidated class action referred to above does not receive court approval does not become effective or becomes unenforceable. The amount of this settlement will not be recognized in our income statement until the potential obligation to return the funds has been eliminated. This settlement was in addition to settlements with AISLIC in December 2004 and with another of our insurers under the Executive Blended Risk policy in January 2005.

Other Claims. In connection with the settlement of the consolidated class action, the claims of IFS on behalf of our Incentive Savings Plan and its participants are being resolved and the class covered by the settlement has been expanded to include participants in the Plan. The Department of Labor is not, however, a party to this settlement and thus the settlement does not necessarily resolve its investigation. In addition, the derivative claims asserted by one of our putative shareholders and any other derivative demands that may be filed in connection with the PAGIC transactions are being resolved as a result of the settlement of the consolidated class action.

Releases. We are releasing the insurers providing our Executive Blended Risk insurance coverage from any further liability to PNC arising out of the events that gave rise to the consolidated class action, except for the claims against these insurers (other than those with whom we have settled) relating to the $90 million payment to the Restitution Fund. In addition, PNC and AIG are releasing each other with respect to all claims between us arising out of the PAGIC transactions.

We will be responsible for the costs of administering the settlement and the Restitution Fund and may incur additional costs in the future in connection with the advancement of expenses and/or indemnification obligations related to the subject matter of this lawsuit. We do not expect such costs to be material.

In connection with industry-wide investigations of practices in the mutual fund industry including market timing, late day trading, employee trading in mutual funds and other matters, several of our subsidiaries have received requests for information and other inquiries from state and federal governmental and regulatory authorities. These subsidiaries are fully cooperating in all of these matters. In addition, as a result of the regulated nature of our business and that of a number of our subsidiaries, particularly in the banking and securities areas, we and our subsidiaries are the subject from time to time of investigations and other forms of regulatory inquiry, often as part of industry-wide regulatory reviews of specified activities. Our practice is to cooperate fully with these investigations and inquiries.

In addition to the proceedings or other matters described above, PNC and persons to whom we may have indemnification obligations, in the normal course of business, are subject to various other pending and threatened legal proceedings in which claims for monetary damages and other relief are asserted. We do not anticipate, at the present time, that the ultimate aggregate liability, if any, arising out of such other legal proceedings will have a material adverse effect on our financial position. However, we cannot now determine whether or not any claims asserted against us or others to whom we may have indemnification obligations, whether in the proceedings or other matters specifically described above or otherwise, will have a material adverse effect on our results of operations in any future reporting period.

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NOTE 6 SECURITIES

In millions	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
December 31, 2006				
SECURITIES AVAILABLE FOR SALE (a)				
Debt securities				
U.S. Treasury and government agencies	**$611**		**$(3)**	**$608**
Mortgage-backed	**17,325**	**$39**	**(156)**	**17,208**
Commercial mortgage-backed	**3,231**	**13**	**(25)**	**3,219**
Asset-backed	**1,615**	**3**	**(9)**	**1,609**
State and municipal	**140**	**1**	**(2)**	**139**
Other debt	**90**		**(3)**	**87**
Total debt securities	**23,012**	**56**	**(198)**	**22,870**
Corporate stocks and other	**321**	**1**	**(1)**	**321**
Total securities available for sale	**$23,333**	**$57**	**$(199)**	**$23,191**
December 31, 2005				
SECURITIES AVAILABLE FOR SALE (a)				
Debt securities				
U.S. Treasury and government agencies	$3,816		$(72)	$3,744
Mortgage-backed	13,794	$1	(251)	13,544
Commercial mortgage-backed	1,955	1	(37)	1,919
Asset-backed	1,073		(10)	1,063
State and municipal	159	1	(2)	158
Other debt	87		(1)	86
Total debt securities	20,884	3	(373)	20,514
Corporate stocks and other	196			196
Total securities available for sale	$21,080	$3	$(373)	$20,710
December 31, 2004				
SECURITIES AVAILABLE FOR SALE (a)				
Debt securities				
U.S. Treasury and government agencies	$4,735		$(13)	$4,722
Mortgage-backed	8,506	$9	(82)	8,433
Commercial mortgage-backed	1,380	5	(15)	1,370
Asset-backed	1,910	5	(14)	1,901
State and municipal	175	2	(1)	176
Other debt	33			33
Total debt securities	16,739	21	(125)	16,635
Corporate stocks and other	123	2		125
Total securities available for sale	$16,862	$23	$(125)	$16,760

(a) Securities held to maturity at December 31, 2006 and December 31, 2005 totaled less than $.5 million and at December 31, 2004 totaled $1 million.

We evaluate our securities available for sale portfolio in light of changing market conditions and other factors and, where appropriate, take steps intended to improve our overall positioning.

At December 31, 2006 and 2005, our most significant concentration of credit risk related to investments issued by the US government and its agencies. This exposure amounted to $.6 billion at December 31, 2006 and $3.7 billion at December 31, 2005.

The fair value of securities available for sale generally decreases when interest rates increase and vice versa. Net unrealized gains and losses in the securities available for sale portfolio are included in shareholders equity as accumulated other comprehensive income or loss, net of tax.

The expected weighted-average life of securities available for sale was 3 years and 8 months at December 31, 2006, 4 years and 1 month at December 31, 2005, and 2 years and 8 months at December 31, 2004.

During mid-August through early September 2006, we performed a comprehensive review of our securities available for sale portfolio and, by the end of September 2006, completed the process of executing portfolio rebalancing actions in response to the changing economic landscape, recent statements and actions by the Federal Open Market Committee (in particular, the decision not to raise the federal funds target rate), and our desire to position the securities portfolio to optimize total return performance over the long term.

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As a result, we repositioned our securities portfolio according to our market views. This included reallocating exposure to certain sectors, selling securities holdings we believed would likely underperform on a relative value basis, and retaining certain existing securities and purchasing incremental securities all of which we believe will outperform the market going forward as further discussed below.

As part of the rebalancing, we assessed the entire securities available for sale portfolio of which, for the majority of positions, fair value was less than amortized cost. We executed a strategy to reduce our US government agency and mortgage-backed security sector allocations and increase our interest rate swap sector allocation. We sold substantially all of our US government agency securities to reduce our interest rate spread exposure to that asset class. The US government agency securities that we retained are characterized by relatively short terms to maturity and smaller individual security balances. We also sold specific securities in the mortgage-backed portfolio (i.e., all of our holdings of specific coupon US government agency pass-through securities and collateralized mortgage obligations having specific collateral characteristics), and in the commercial mortgage-backed portfolio (i.e., all of our holdings of specific vintage securities) that we believe, given the underlying collateral, will underperform on a relative value basis. We retained the remaining holdings in our mortgage-backed portfolio including all of our holdings of mortgage-backed securities

collateralized by hybrid adjustable rate mortgage loans, our commercial mortgage-backed portfolio and our asset-backed portfolio. Our objective was to reduce the portfolio credit spread and interest rate volatility exposures, to position the portfolio for a steeper yield curve and to optimize the relative value performance of the portfolio. We assessed the securities retained relative to the same portfolio objectives, our market view and outlook, our desired sector allocations and our expectation of performance relative to market benchmarks, and, given our assessment, we confirmed our intent to hold these remaining securities until either recovery of fair value or maturity.

The portfolio rebalancing resulted in the sale during the third quarter of 2006 of $6.0 billion of securities available for sale at an aggregate pretax loss of $196 million, or $127 million after-tax. In connection with this rebalancing, we purchased approximately $1.8 billion of securities and added approximately $4.0 billion of interest rate swaps to maintain our interest rate risk position. We also reduced wholesale funding as a result of the actions taken.

The resulting net realized losses on the sale of the securities during the third quarter of 2006 were previously reflected as net unrealized securities losses within accumulated other comprehensive loss in the shareholders equity section of PNC s Consolidated Balance Sheet. Accordingly, total shareholders equity did not change as a result of these actions.

The following table presents unrealized loss and fair value of securities at December 31, 2006 and December 31, 2005 for which an other-than-temporary impairment has not been recognized. These securities are segregated between investments that have been in a continuous unrealized loss position for less than twelve months and twelve months or more.

In millions	Unrealized loss position less		Unrealized loss position			
December 31, 2006	than 12 months		12 months or more		Total	
	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value
Securities available for sale						
Debt securities						
U.S. Treasury and government agencies		**$15**	**$(3)**	**$302**	**$(3)**	**$317**
Mortgage-backed	**$(8)**	**2,717**	**(148)**	**6,925**	**(156)**	**9,642**
Commercial mortgage-backed	**(3)**	**924**	**(22)**	**778**	**(25)**	**1,702**
Asset-backed	**(1)**	**414**	**(8)**	**649**	**(9)**	**1,063**
State and municipal		**16**	**(2)**	**88**	**(2)**	**104**
Other debt		**65**	**(3)**	**59**	**(3)**	**124**
Total debt securities	**(12)**	**4,151**	**(186)**	**8,801**	**(198)**	**12,952**
Corporate stocks and other			**(1)**	**10**	**(1)**	**10**
Total	**$(12)**	**$4,151**	**$(187)**	**$8,811**	**$(199)**	**$12,962**
December 31, 2005						
Securities available for sale						
Debt securities						
U.S. Treasury and government agencies	$(33)	$1,898	$(39)	$1,553	$(72)	$3,451

Mortgage-backed	(161)	10,544	(90)	2,321	(251)	12,865
Commercial mortgage-backed	(29)	1,272	(8)	339	(37)	1,611
Asset-backed	(8)	835	(2)	98	(10)	933
State and municipal	(1)	58	(1)	53	(2)	111
Other debt	(1)	59		4	(1)	63
Total	$(233)	$14,666	$(140)	$4,368	$(373)	$19,034

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We do not believe any individual unrealized loss as of December 31, 2006 represents an other-than-temporary impairment. The $156 million unrealized losses reported for mortgage-backed securities relate primarily to securities issued by the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation and private issuers whose credit rating is AAA. The $25 million unrealized losses reported for commercial mortgage-backed securities relate primarily to fixed rate securities. The $9 million unrealized losses associated with asset-backed securities relate primarily to securities collateralized by home equity, automobile and credit card loans. The majority of the unrealized losses associated with both mortgage and asset-backed securities are attributable to changes in interest rates and not from the deterioration of the credit quality of the issuer.

Of those securities in an unrealized loss position for 12 months or more as of December 31, 2006, sixteen (eleven mortgage-backed and five state and municipal) positions with fair value totaling $333 million had an unrealized loss of more than 5% when compared with their amortized cost. The unrealized loss on these positions totaled $26 million and the unrealized loss amount on any individual position did not exceed $5 million. These mortgage-backed securities are primarily collateralized mortgage obligations where amortized cost approximates the par value of the security. These securities are all rated AAA. The aggregate unrealized loss on the state and municipal securities positions was not significant.

Information relating to securities sold is set forth in the following table.

Securities Sold

Year ended December 31 In millions	Proceeds	Gross Gains	Gross Losses	Net Gains (Losses)	Tax Expense (Benefit)
2006	**$11,102**	**$2**	**$209**	**$(207)**	**$(72)**
2005	13,304	19	60	(41)	(14)
2004	14,206	94	39	55	19

The fair value of securities pledged to secure public and trust deposits and repurchase agreements and for other purposes was $10.6 billion at December 31, 2006 and $10.8 billion at December 31, 2005. The pledged securities include positions held in our portfolio of securities available for sale, trading securities that are included in other short-term investments on our Consolidated Balance Sheet, and securities accepted as collateral from others that we are permitted by contract or custom to sell or repledge.

The fair value of securities accepted as collateral that we are permitted by contract or custom to sell or repledge was $1.4 billion at December 31, 2006 and $273 million at December 31, 2005 and is a component of federal funds sold and resale agreements on our Consolidated Balance Sheet. This change reflected an increase in securities sold short, included in other borrowed funds on our Consolidated Balance Sheet. Of the permitted amount, $1.3 billion was repledged to others at December 31, 2006 and all was repledged to others at December 31, 2005.

The following table presents, by remaining contractual maturity, the amortized cost, fair value and weighted-average yield of debt securities at December 31, 2006.

Contractual Maturity Of Debt Securities

December 31, 2006 Dollars in millions	1 Year or Less	After 1 Year through 5 Years	After 5 Years through 10 Years	After 10 Years	Total
SECURITIES AVAILABLE FOR SALE					

U.S. Treasury and government agencies	$452	$145	$1	$13	**$611**
Mortgage-backed	8	5	24	17,288	**17,325**
Commercial mortgage-backed				3,231	**3,231**
Asset-backed	12	84	86	1,433	**1,615**
State and municipal	6	60	71	3	**140**
Other debt	6	17	6	61	**90**
Total debt securities available for sale	$484	$311	$188	$22,029	**$23,012**
Fair value	$484	$307	$185	$21,894	**$22,870**
Weighted-average yield	4.57%	4.52%	4.95%	5.42%	**5.38%**

Based on current interest rates and expected prepayment speeds, the total weighted-average expected maturity of mortgage-backed securities was 3 years and 6 months, of commercial mortgage-backed securities was 5 years and 8 months and of asset-backed securities was 2 years and 5 months at December 31, 2006. Weighted-average yields are based on historical cost with effective yields weighted for the contractual maturity of each security.

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Note 7 Loans, Commitments To Extend Credit and Concentrations of Credit Risk

Loans outstanding were as follows:

December 31 - in millions	**2006**	2005
Commercial	**$ 20,584**	$ 19,325
Commercial real estate	**3,532**	3,162
Consumer	**16,515**	16,173
Residential mortgage	**6,337**	7,307
Lease financing	**3,556**	3,628
Other	**376**	341
Total loans	**50,900**	49,936
Unearned income	**(795)**	(835)
Total loans, net of unearned income	**$ 50,105**	$ 49,101

We realized net gains from sales of commercial mortgages of $55 million in 2006, $61 million in 2005 and $50 million in 2004. Gains on sales of education loans totaled $33 million in 2006, $19 million in 2005 and $30 million in 2004. Net gains in excess of valuation adjustments related to the liquidation of our institutional loans held for sale totaled $7 million in 2005 and $52 million in 2004.

Concentrations of credit risk exist when changes in economic, industry or geographic factors similarly affect groups of counterparties whose aggregate exposure is material in relation to our total credit exposure. Loans outstanding and related unfunded commitments are concentrated in our primary geographic markets. At December 31, 2006, no specific industry concentration exceeded 3% of total commercial loans outstanding and unfunded commitments.

In the normal course of business, we originate or purchase loan products whose contractual features, when concentrated, may increase our exposure as a holder and servicer of those loan products. Possible product terms and features that may create a concentration of credit risk would include loan products whose terms permit negative amortization, a high loan-to-value ratio, features that may expose the borrower to future increases in repayments above increases in market interest rates, below-market interest rates and interest-only loans, among others.

We originate interest-only loans to commercial borrowers. These products are standard in the financial services industry and the features of these products are considered during the underwriting process to mitigate the increased risk of this product feature that may result in borrowers not being able to make interest and principal payments when due. We do not believe that these product features create a concentration of credit risk.

We also originate home equity loans and lines of credit that result in a credit concentration of high loan-to-value ratio loan products at the time of origination. In addition, these loans are concentrated in our primary geographic markets as discussed above. At December 31, 2006, $5.8 billion of the $15.4 billion of home equity and other consumer loans (included in Consumer in the table above) had a loan-to-value ratio greater than 80%. These loans are collateralized primarily by 1-4 family residential properties. As part of our asset and liability management activities, we also periodically purchase residential mortgage loans that are collateralized by 1-4 family residential properties. At December 31, 2006, $2.6 billion of the $6.3 billion of residential mortgage loans were interest-only loans.

During the third quarter of 2006, we announced our plan to sell or securitize approximately $2.1 billion of loans from our residential mortgage portfolio. These transactions were substantially consummated during the fourth quarter of 2006. In accordance with GAAP, these loans were transferred to loans held for sale as of September 30, 2006. We recognized a pretax loss in the third quarter of 2006 of $48 million as a reduction of noninterest income, representing the mark to market valuation of these loans upon transfer to held for sale status. This loss, which is reported in the Other business segment, represented the decline in value of the loans almost entirely from the impact of increases in interest rates over the holding period.

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Net Unfunded Credit Commitments

December 31 - in millions	2006	2005
Commercial	**$ 31,009**	$ 27,774
Consumer	**10,495**	9,471
Commercial real estate	**2,752**	2,337
Other	**579**	596
Total	**$ 44,835**	$ 40,178

Commitments to extend credit represent arrangements to lend funds subject to specified contractual conditions. At December 31, 2006, commercial commitments are reported net of $8.3 billion of participations, assignments and syndications, primarily to financial services companies. The comparable amount at December 31, 2005 was $6.7 billion. Commitments generally have fixed expiration dates, may require payment of a fee, and contain termination clauses in the event the customer s credit quality deteriorates. Based on our historical experience, most commitments expire unfunded, and therefore cash requirements are substantially less than the total commitment. Consumer home equity lines of credit accounted for 74% of consumer unfunded credit commitments.

As a result of deconsolidating Market Street in October 2005, amounts related to Market Street were considered third party unfunded commitments at December 31, 2006 and 2005. These unfunded credit commitments totaled $5.6 billion at December 31, 2006 and $4.6 billion at December 31, 2005 and are included in the preceding table primarily within the Commercial and Consumer categories.

Net outstanding standby letters of credit totaled $4.4 billion at December 31, 2006 and $4.2 billion at December 31, 2005.

Standby letters of credit commit us to make payments on behalf of customers if certain specified future events occur. Such instruments are typically issued to support industrial revenue bonds, commercial paper, and bid-or-performance related contracts. Maturities for standby letters of credit ranged from 2007 to 2017. See Note 24 Commitments and Guarantees for additional information.

At December 31, 2006, the largest industry concentration was for general medical and surgical hospitals, which accounted for approximately 5% of the total letters of credit and bankers acceptances.

At December 31, 2006, we pledged $1.3 billion of loans to the FRB and $24.1 billion of loans to the Federal Home Loan Bank (FHLB) as collateral for the contingent ability to borrow, if necessary.

Certain directors and executive officers of PNC and its subsidiaries, as well as certain affiliated companies of these directors and officers, were customers of and had loans with subsidiary banks in the ordinary course of business. All such loans were on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other customers and did not involve more than a normal risk of collectibility or present other unfavorable features. The aggregate principal amounts of these loans were $18 million at December 31, 2006 and $21 million at December 31, 2005. During 2006, new loans of $58 million were funded and repayments totaled $61 million.

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Note 8 Asset Quality

The following table sets forth nonperforming assets and related information:

December 31 - dollars in millions	**2006**	2005
Nonaccrual loans		
Commercial	**$109**	$134
Commercial real estate	**12**	14
Consumer	**13**	10
Residential mortgage	**12**	15
Lease financing	**1**	17
Total nonaccrual loans	**$147**	$190
Total nonperforming loans	**147**	190
Nonperforming loans held for sale (a)		1
Foreclosed and other assets		
Lease	**12**	13
Residential mortgage	**10**	9
Other	**2**	3
Total foreclosed and other assets	**24**	25
Total nonperforming assets (b)	**$171**	$216
Nonperforming loans to total loans	**.29%**	.39%
Nonperforming assets to total loans, loans held for sale and foreclosed assets	**.33**	.42
Nonperforming assets to total assets	**.17**	.23
Interest on nonperforming loans		
Computed on original terms	**$15**	$16
Recognized	**4**	5
Past due loans		
Accruing loans past due 90 days or more	**$50**	$46
As a percentage of total loans	**.10%**	.09%
Past due loans held for sale		
Accruing loans held for sale past due 90 days or more	**$9**	$47
As a percentage of total loans held for sale	**.38%**	1.92%

(a) Includes $1 million of troubled debt restructured loans held for sale at December 31, 2005.

(b) Excludes equity management assets that are carried at estimated fair value of $11 million (including $4 million of troubled debt restructured assets) at December 31, 2006 and $25 million (including $7 million of troubled debt restructured assets) at December 31, 2005.

Changes in the allowance for loan and lease losses were as follows:

In millions	**2006**	2005	2004
January 1	**$596**	$607	$632
Charge-offs	**(180)**	(129)	(166)
Recoveries (a)	**40**	99	51
Net charge-offs (a)	**(140)**	(30)	(115)
Provision for credit losses	**124**	21	52
Acquired allowance (b)		23	22
Net change in allowance for unfunded loan commitments and letters of credit	**(20)**	(25)	16
December 31	**$560**	$596	$607

(a) Amounts for 2005 reflect the impact of a $53 million loan recovery in that year.

(b) Riggs in 2005 and United National Bancorp in 2004.

Changes in the allowance for unfunded loan commitments and letters of credit were as follows:

In millions	2006	2005	2004
Allowance at January 1	**$100**	$75	$91
Net change in allowance for unfunded loan commitments and letters of credit	**20**	25	(16)
December 31	**$120**	$100	$75

All nonperforming loans at December 31, 2006 and 2005 are considered impaired under SFAS 114. Of these totals, impaired loans amounting to $121 million at December 31, 2006 and $148 million at December 31, 2005 had a corresponding specific allowance for loan and lease losses of $32 million and $37 million, respectively. The average balance of impaired loans was $147 million in 2006, $106 million in 2005 and $141 million in 2004. We did not recognize any interest income on impaired loans in 2006, 2005 or 2004.

Loans that are not included in nonperforming or past due categories but cause us to be uncertain about the borrower s ability to comply with existing repayment terms over the next six months totaled $41 million at December 31, 2006 compared with $67 million at December 31, 2005. Approximately 59% of these loans are in the Corporate & Institutional Banking portfolio.

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NOTE 9 GOODWILL AND OTHER INTANGIBLE ASSETS

A summary of the changes in goodwill by business segment during 2006 follows:

Goodwill

In millions	Dec. 31 2005	Additions/ Adjustments	**Dec. 31 2006**
Retail Banking	$1,471	$(5)	**$1,466**
Corporate & Institutional Banking	935	3	**938**
BlackRock	190	(160)	**30**
PFPC	968		**968**
Other	55	(55)	
Total	$3,619	$(217)	**$3,402**

The gross carrying amount, accumulated amortization and net carrying amount of other intangible assets by major category consisted of the following:

Other Intangible Assets

December 31 - in millions	**2006**	2005
Customer-related and other intangibles		
Gross carrying amount (a)	**$342**	$646
Accumulated amortization	**(178)**	(143)
Net carrying amount	**$164**	$503
Mortgage and other loan servicing rights		
Gross carrying amount	**$689**	$511
Accumulated amortization	**(212)**	(167)
Net carrying amount	**$477**	$344
Total	**$641**	$847

(a) Amounts for 2006 were reduced by $305 million related to the BlackRock deconsolidation. See Note 2 Acquisitions for additional information regarding our deconsolidation of BlackRock effective September 29, 2006.

Most of our other intangible assets have finite lives and are amortized primarily on a straight-line basis or, in the case of mortgage and other loan servicing rights and certain core deposit intangibles, on an accelerated basis.

For customer-related intangibles, the estimated remaining useful lives range from less than one year to 11 years, with a weighted-average remaining useful life of approximately 5 years. Our mortgage and other loan servicing rights are amortized primarily over a period of five to 10 years in proportion to the estimated net servicing income from the related loans.

The changes in the carrying amount of goodwill and net other intangible assets during 2006 follows:

Changes in Goodwill and Other Intangibles

In millions	Goodwill	Customer-Related	Servicing Rights
December 31, 2005	$3,619	$503	$344

Additions/adjustments:			
BlackRock (a)	(190)	(305)	
BlackRock stock activity, net	(25)		
Retail Banking	(5)		2
Other			4
Corporate & Institutional Banking	3	1	172
Reduction in accumulated amortization			2
Amortization (b)		(35)	(47)
December 31, 2006	**$3,402**	**$164**	**$477**

(a) Reflects our deconsolidation of BlackRock. See also note (a) under the Other Intangible Assets table.

(b) Amount is net of $17 million of accumulated amortization that was eliminated during the third quarter of 2006 in connection with the deconsolidation of BlackRock.

Our investment in BlackRock changes when BlackRock repurchases its shares in the open market or issues shares for an acquisition or pursuant to its employee compensation plans. We recognize goodwill when BlackRock repurchases its shares at an amount greater than book value per share and this results in an increase in our percentage ownership interest.

We recognized a net reduction to goodwill of approximately $25 million related to BlackRock stock activity, primarily due to the decrease in our ownership interest in BlackRock from approximately 69% to approximately 34% as a result of the BlackRock/MLIM transaction in 2006. The reduction in goodwill reduced the gain realized by PNC from the transaction.

Servicing revenue from both commercial and residential mortgage servicing assets and liabilities generated contractually specified servicing fees, net interest income from servicing portfolio deposit balances and ancillary fees totaling $139 million for the year ended December 31, 2006. We also generate servicing revenue from fee-based activities provided to others.

Amortization expense on intangible assets for 2006, 2005 and 2004 was $99 million, $74 million and $52 million, respectively. Amortization expense on existing intangible assets for 2007 through 2011 is estimated to be as follows:

2007: $100 million,
2008: $91 million,
2009: $85 million,
2010: $67 million, and
2011: $53 million.

We conduct a goodwill impairment test on our reporting units at least annually or more frequently if any adverse triggering

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events occur. Based on this review, no adjustment for goodwill impairment was deemed necessary for 2006. The fair value of our reporting units is determined by using discounted cash flow and market comparability methodologies.

NOTE 10 PREMISES, EQUIPMENT AND LEASEHOLD IMPROVEMENTS

Premises, equipment and leasehold improvements, stated at cost less accumulated depreciation and amortization, were as follows:

December 31 - in millions	**2006**	2005
Land	**$187**	$186
Buildings	**937**	881
Equipment	**1,771**	1,735
Leasehold improvements	**385**	453
Total	**3,280**	3,255
Accumulated depreciation and amortization	**(1,578)**	(1,538)
Net book value	**$1,702**	$1,717

Depreciation expense on premises, equipment and leasehold improvements totaled $180 million in 2006, $192 million in 2005 and $159 million in 2004. Amortization expense, primarily for capitalized internally developed software, was $44 million in 2006 and $43 million for both 2005 and 2004.

We lease certain facilities and equipment under agreements expiring at various dates through the year 2071. We account for substantially all such leases as operating leases. Rental expense on such leases amounted to $193 million in 2006, $189 million in 2005 and $174 million in 2004.

Required minimum annual rentals that we owe on noncancelable leases having initial or remaining terms in excess of one year totaled $965 million at December 31, 2006 and $998 million at December 31, 2005. Minimum annual rentals for the years 2007 through 2012 and thereafter are as follows:

2007: $140 million,
2008: $125 million,
2009: $108 million,
2010: $94 million,
2011: $84 million, and
2012 and thereafter: $414 million.

NOTE 11 SECURITIZATIONS AND RETAINED INTERESTS

During 2006, 2005 and 2004, we sold commercial mortgage loans totaling $307 million, $284 million and $460 million, respectively, in securitization transactions through programs with the Government National Mortgage Association (GNMA). The transactions and resulting receipt and subsequent sale of securities qualify as sales under the appropriate accounting criteria and resulted in pretax gains of $8 million in 2006, $7 million in 2005 and $8 million in 2004. In addition to the cash proceeds from the sales transactions above, net cash flows between the securitization vehicles and

PNC, including servicing fees, in 2006, 2005 and 2004 related to those transactions were not significant.

Additionally, we sold commercial mortgage and commercial loans of $2.9 billion in 2006, $3.1 billion in 2005 and $1.6 billion in 2004 for cash in other loan sales transactions. These transactions resulted in pretax gains of $55 million in 2006, $54 million in 2005 and $42 million in 2004. See Note 9 Goodwill and Other Intangible Assets for additional information regarding servicing assets.

For the transactions above, we continue to perform servicing and recognized servicing assets of $26 million in 2006, $23 million in 2005 and $14 million in 2004. We also purchased servicing rights for commercial mortgage loans from third parties of approximately $150 million in 2006, $112 million in 2005 and $47 million in 2004.

During the fourth quarter of 2006, we sold residential mortgage loans totaling $358 million in securitization transactions through third party programs. Additionally, we sold residential mortgage loans of $26 million in the fourth quarter of 2006 for cash in other loan sales transactions.

For these transactions, we serve as the servicer of record and recognized servicing assets of $4 million in 2006. In accordance with SFAS 156, these servicing assets were initially measured at fair value and we have elected the fair value method to value these residential mortgage servicing assets. The changes in fair value during 2006 and the servicing fees received in 2006 were not significant.

Changes in the mortgage and other loan servicing assets were as follows:

Mortgage and Other Loan Servicing Assets

In millions	**2006**	2005
Balance at January 1	**$344**	$242
Additions	**180**	135
Retirements (a)		
Amortization expense	**(47)**	(33)
Balance at December 31	**$477**	$344

(a) 2006 and 2005 included $2 million and $25 million, respectively, of fully amortized retirements.

Assuming a prepayment speed of 7%-16% for the respective strata discounted at 8%-10%, the estimated fair value of commercial mortgage servicing rights was $546 million at December 31, 2006. A 10% and 20% adverse change in all assumptions used to determine fair value at December 31, 2006, results in a $33 million and $66 million decrease in fair value, respectively. No valuation allowance was necessary at December 31, 2006 or December 31, 2005.

Assuming a prepayment speed of 12% for the respective strata discounted at 9.5%-10%, the estimated fair value of commercial loan servicing rights was $2 million at December 31, 2006. A 10% and 20% adverse change in all assumptions used to determine fair value at December 31, 2006, results in an insignificant decrease in fair value. No valuation allowance was necessary at December 31, 2006.

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We also own an interest-only strip related to education loans totaling $59 million and $58 million, respectively, at December 31, 2006 and December 31, 2005. This strip was retained from the sales of education loans to a third party trust prior to 2003. Loans that are held by the trust supporting the value of the strip were $88 million and $123 million at December 31, 2006 and December 31, 2005, respectively. The principal of these loans is effectively guaranteed by the federal government. The trust related to the securitization will terminate in 2007.

NOTE 12 DEPOSITS

The aggregate amount of time deposits with a denomination of $100,000 or more was $8.7 billion at December 31, 2006 and $7.1 billion at December 31, 2005.

Contractual maturities of time deposits for the years 2007 through 2012 and thereafter are as follows:

2007: $16.5 billion,
2008: $.6 billion,
2009: $.4 billion,
2010: $.1 billion,
2011: $.1 billion, and
2012 and thereafter: $1.3 billion.

NOTE 13 BORROWED FUNDS

Bank notes at December 31, 2006 totaling $1.1 billion have interest rates ranging from 2.75% to 10.25% with approximately $575 million maturing in 2007. Senior and subordinated notes consisted of the following:

December 31, 2006

Dollars in millions		Outstanding	Stated Rate	Maturity
Senior				
Exchangeable	$	**1,000**	**4.96%**	**2036**
All other		**1,535**	**4.20% 5.34%**	**2008-2010**
Total senior		**2,535**		
Subordinated				
Junior		**1,074**	**5.94% 10.01%**	**2007-2033**
All other		**2,888**	**4.88% 9.65%**	**2007-2017**
Total subordinated		**3,962**		
Total senior and subordinated	$	**6,497**		

Included in outstandings for the senior and subordinated notes in the table above are basis adjustments of $13 million and $3 million, respectively, related to fair value accounting hedges as of December 31, 2006.

Total borrowed funds at December 31, 2006 have scheduled or anticipated repayments for the years 2007 through 2012 and thereafter as follows:

2007: $8.4 billion,
2008: $1.4 billion,
2009: $.8 billion,
2010: $.8 billion,
2011: $6 million, and
2012 and thereafter: $3.6 billion.

Included in borrowed funds at December 31, 2006 are $1 billion of Floating Rate Exchangeable Senior Notes (Exchangeable Notes) that were issued through PNC Funding Corp (Funding), a subsidiary of PNC. These notes commenced on December 20, 2006 and are due December 20, 2036. Interest will be paid at a floating rate equal to 3-month LIBOR, reset quarterly, minus 40 basis points, quarterly in arrears, provided that such interest rate will never be less than 0% per annum. The Exchangeable Notes are guaranteed by PNC.

Holders may exchange the Exchangeable Notes for, as specified by Funding, shares of PNC common stock, cash, or a combination of shares and cash at any time on or prior to maturity based on an initial exchange price per share of approximately $128.56, subject to adjustment. Holders have the right to require PNC to repurchase all or a portion of the Exchangeable Notes on December 20, 2007 and periodically thereafter for an amount equal to 100% of the principal plus accrued and unpaid interest. Beginning on December 26, 2007, PNC may redeem the Exchangeable Notes in whole at any time, or in part from time to time, for an amount equal to 100% of the principal plus accrued and unpaid interest.

In connection with the issuance of the Exchangeable Notes, PNC entered into a Registration Rights Agreement (Agreement) with the initial purchaser of the Exchangeable Notes. As part of the Agreement PNC agreed to file a registration statement with the SEC, as soon as practicable but in any event within 120 days after the issue date, to register for resale the Exchangeable Notes and the common stock deliverable upon exchange for the Exchangeable Notes. PNC also agreed, among other things, to use its best efforts to cause the registration statement to be declared effective as promptly as practicable but in any event within 240 days after the issue date and to keep the registration statement continuously effective until registration is no longer applicable.

If PNC does not meet these obligations, PNC will be subject to liquidated damages equal to 0.25% per annum of the principal amount of the Exchangeable Notes outstanding. Assuming the Exchangeable Notes remain outstanding through 2036 and PNC does not meet these obligations, the maximum consideration that PNC could be required to transfer under this Agreement is approximately $75 million. We have not recorded a liability for this Agreement at December 31, 2006.

See Note 14 Capital Securities of Subsidiary Trusts for information about the $1.1 billion of junior subordinated debt.

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During February 2007, in connection with our planned acquisition of Mercantile, we issued $1.9 billion of debt to fund the cash portion of this transaction, comprised of the following:

- On February 1, 2007, we issued $775 million of floating rate senior notes due January 2012. Interest will be reset quarterly to 3-month LIBOR plus 14 basis points and interest will be paid quarterly.
- Also on February 1, 2007, we issued $500 million of floating rate senior notes due January 2014. Interest will be reset quarterly to 3-month LIBOR plus 20 basis points and will be paid quarterly.
- On February 8, 2007, we issued $600 million of subordinated notes due February 2017. These notes pay interest semiannually at a fixed rate of 5.625%.

See Note 2 Acquisitions for additional information regarding Mercantile.

NOTE 14 CAPITAL SECURITIES OF SUBSIDIARY TRUSTS

In December 2006, we elected to redeem all of the underlying Capital Securities related to the PNC Institutional Capital Trust A, UNB Capital Statutory Trust II, and Riggs Capital Trust I. The total Capital Securities redeemed totaled $453 million.

At December 31, 2006, the following capital securities represent non-voting preferred beneficial interests in the assets of PNC Institutional Capital Trust B, PNC Capital Trusts C and D, UNB Capital Trust I, and the Riggs Capital Trust II (the Trusts). All of these Trusts are wholly owned finance subsidiaries of PNC. UNB Capital Trust I was acquired effective January 1, 2004 as part of the United National acquisition. Riggs Capital Trust II was acquired in May 2005 as part of the Riggs acquisition. In the event of certain changes or amendments to regulatory requirements or federal tax rules, the capital securities are redeemable in whole. The financial statements of the Trusts are not included in PNC s consolidated financial statements in accordance with GAAP.

- Trust B, formed in May 1997, issued $300 million of 8.315% capital securities due May 15, 2027, that are redeemable after May 15, 2007 at a premium that declines from 104.1575% to par on or after May 15, 2017.
- Trust C, formed in June 1998, issued $200 million of capital securities due June 1, 2028, bearing interest at a floating rate per annum equal to 3-month LIBOR plus 57 basis points. The rate in effect at December 31, 2006 was 5.94%. Trust C Capital Securities are redeemable on or after June 1, 2008 at par.
- Trust D, formed in December 2003, issued $300 million of 6.125% capital securities due December 15, 2033 that are redeemable on or after December 18, 2008 at par.
- UNB Capital Trust I, formed in March 1997 with $16 million outstanding of 10.01% capital securities due March 15, 2027, that are redeemable on or after March 15, 2007 at a premium that declines from 105.00% to par on or after March 15, 2017. PNC has delivered redemption notices to the related trustee to redeem all of these securities on March 15, 2007.
- Riggs Capital Trust II was formed in March 1997 when $200 million of 8 $^{7}/8$% capital securities were issued. These securities are due March 15, 2027, and are redeemable after March 15, 2007 at a premium that declines from 104.438% to par on or after March 15, 2017. Riggs had acquired less than 50% of the capital securities and, therefore, under FIN 46R PNC is not deemed to be the primary beneficiary. Accordingly, the financial statements of this Trust are not consolidated into PNC s financial results. Junior subordinated debt of $206 million owed by PNC to this Trust is included in PNC s balance sheet, with the related service cost included in interest expense. The $50 million of acquired capital securities are included as securities available for sale, with the related dividends included in interest income. PNC has delivered redemption notices to the related trustee to redeem all of these securities on March 15, 2007.

At December 31, 2006, PNC s junior subordinated debt of $1.1 billion represented debentures issued by PNC and purchased and held as assets by the Trusts.

The obligations of the respective parent of each Trust, when taken collectively, are the equivalent of a full and unconditional guarantee of the obligations of such Trust under the terms of the Capital Securities. Such guarantee is subordinate in right of payment in the same manner as other junior subordinated debt. There are certain restrictions on PNC s overall ability to obtain funds from its subsidiaries. For additional disclosure on these funding restrictions, including an explanation of dividend and intercompany loan limitations, see Note 4 Regulatory Matters.

NOTE 15 SHAREHOLDERS EQUITY

Information related to preferred stock is as follows:

Preferred Shares

December 31 Shares in thousands	Liquidation value per share	**2006**	2005
Authorized			
$1 par value		**17,012**	17,030
Issued and outstanding			
Series A	$40	**7**	7
Series B	40	**2**	2
Series C	20	**144**	152
Series D	20	**196**	206
Total issued and outstanding		**349**	367

Series A through D are cumulative and, except for Series B, are redeemable at our option. Annual dividends on Series A, B and D preferred stock total $1.80 per share and on Series C preferred stock total $1.60 per share. Holders of Series A

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through D preferred stock are entitled to a number of votes equal to the number of full shares of common stock into which such preferred stock is convertible. Series A through D preferred stock have the following conversion privileges: (i) one share of Series A or Series B is convertible into eight shares of PNC common stock; and (ii) 2.4 shares of Series C or Series D are convertible into four shares of PNC common stock.

During 2000, our Board of Directors adopted a shareholder rights plan providing for issuance of share purchase rights. The rights plan provided that, except as otherwise provided in the plan, if a person or group becomes beneficial owner of 10% or more of PNC outstanding common stock, all holders of the rights, other than such person or group, may purchase our common stock or equivalent preferred stock at half of market value. On February 14, 2007, our Board of Directors agreed to amend the existing rights agreement for the shareholder rights plan in order to accelerate the final expiration date of the outstanding share purchase rights issued under the plan from May 25, 2010 to February 28, 2007. The effect of this amendment is that the outstanding share purchase rights expired on February 28, 2007, and the shareholder rights plan pursuant to which the rights were issued is of no further force or effect after that date.

We have a dividend reinvestment and stock purchase plan. Holders of preferred stock and PNC common stock may participate in the plan, which provides that additional shares of common stock may be purchased at market value with reinvested dividends and voluntary cash payments. Common shares issued pursuant to this plan were: 535,394 shares in 2006, 688,665 shares in 2005 and 744,266 shares in 2004.

At December 31, 2006, we had reserved approximately 44.3 million common shares to be issued in connection with certain stock plans and the conversion of certain debt and equity securities.

In February 2005, our Board of Directors authorized the purchase of up to 20 million shares of our common stock in open market or privately negotiated transactions. The 2005 repurchase authorization was a replacement and continuation of the 2004 repurchase program. The 2005 program will remain in effect until fully utilized or until modified, superseded or terminated. During 2006, we purchased 5 million common shares at a total cost of $354 million under the 2005 program. During 2005, we purchased .5 million common shares at a total cost of $26 million under both the 2005 and 2004 common stock repurchase programs, all of which occurred during the first quarter.

NOTE 16 FINANCIAL DERIVATIVES

We use a variety of derivative financial instruments to help manage interest rate, market and credit risk and reduce the effects that changes in interest rates may have on net income, fair value of assets and liabilities, and cash flows. These instruments include interest rate swaps, interest rate caps and floors, futures contracts, and total return swaps.

Fair Value Hedging Strategies

We enter into interest rate and total return swaps, interest rate caps, floors and futures derivative contracts to hedge designated commercial mortgage loans held for sale, commercial loans, bank notes, senior debt and subordinated debt for changes in fair value primarily due to changes in interest rates. Adjustments related to the ineffective portion of fair value hedging instruments are recorded in interest income, interest expense or noninterest income depending on the hedged item.

Cash Flow Hedging Strategy

We enter into interest rate swap contracts to modify the interest rate characteristics of designated commercial loans from variable to fixed in order to reduce the impact of interest rate changes on future interest income. We are hedging our exposure to the variability of future cash flows for all forecasted transactions for a maximum of 10 years for hedges converting floating-rate commercial loans to fixed. The fair value of these derivatives is reported in other assets or other liabilities and offset in accumulated other comprehensive income (loss) for the effective portion of the derivatives. When the hedged transaction culminates, any unrealized gains or losses related to these swap contracts are reclassified from accumulated other comprehensive income (loss) into earnings in the same period or periods during which the hedged forecasted transaction affects earnings and are included in interest income. Ineffectiveness of the strategy, as defined by risk management policies and procedures, if any, is reported in interest income.

During the next twelve months, we expect to reclassify to earnings $30 million of pretax net losses, or $19 million after-tax, on cash flow hedge derivatives currently reported in accumulated other comprehensive income (loss). This amount could differ from amounts actually recognized due to changes in interest rates and the addition of other hedges subsequent to December 31, 2006. These net losses are anticipated to result from net cash flows on receive fixed interest rate swaps that would impact interest income recognized on the related floating rate commercial loans.

As of December 31, 2006 we have determined that there were no hedging positions where it was probable that certain forecasted transactions may not occur within the originally designated time period.

For those hedge relationships that require testing for ineffectiveness, any ineffectiveness present in the hedge relationship is recognized in current earnings. The ineffective portion of the change in value of these derivatives resulted in a $4 million net loss in 2006 compared with a net loss of $3 million in 2005.

During the third quarter of 2006, we recognized a $20 million pretax loss charged to other noninterest income associated with our application of the short-cut method of fair value hedge accounting for trust preferred securities.

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Free-Standing Derivatives

To accommodate customer needs, we also enter into financial derivative transactions primarily consisting of interest rate swaps, interest rate caps and floors, futures, swaptions, and foreign exchange and equity contracts. We primarily manage our market risk exposure from customer positions through transactions with third-party dealers. The credit risk associated with derivatives executed with customers is essentially the same as that involved in extending loans and is subject to normal credit policies. We may obtain collateral based on our assessment of the customer. For derivatives not designated as an accounting hedge, the gain or loss is recognized in trading noninterest income.

Also included in free-standing derivatives are transactions that we enter into for risk management and proprietary purposes that are not designated as accounting hedges, primarily interest rate and basis swaps, total return swaps, interest rate caps and floors, credit default swaps, option contracts and certain interest rate-locked loan origination commitments as well as commitments to buy or sell mortgage loans.

Basis swaps are agreements involving the exchange of payments, based on notional amounts, of two floating rate financial instruments denominated in the same currency, one pegged to one reference rate and the other tied to a second reference rate (e.g., swapping payments tied to one-month LIBOR for payments tied to three-month LIBOR). We use these contracts to mitigate the impact on earnings of exposure to a certain referenced interest rate.

We purchase and sell credit default swaps to mitigate the economic impact of credit losses on specifically identified existing lending relationships or to generate revenue from proprietary trading activities. The fair value of these derivatives typically is based on the change in value, due to changing credit spreads.

Interest rate lock commitments for, as well as commitments to buy or sell, mortgage loans that we intend to sell are considered free-standing derivatives. Our interest rate

exposure on certain commercial mortgage interest rate lock commitments is economically hedged with pay-fixed interest rate swaps and forward sales agreements. These contracts mitigate the impact on earnings of exposure to a certain referenced rate.

Free-standing derivatives also include positions we take based on market expectations or to benefit from price differentials between financial instruments and the market based on stated risk management objectives.

Derivative Counterparty Credit Risk

By purchasing and writing derivative contracts we are exposed to credit risk if the counterparties fail to perform. Our credit risk is equal to the fair value gain in the derivative contract. We minimize credit risk through credit approvals, limits, monitoring procedures and collateral requirements. We generally enter into transactions with counterparties that carry high quality credit ratings.

We enter into risk participation agreements to share some of the credit exposure with other counterparties related to interest rate derivative contracts or to take on credit exposure to generate revenue. We will make/receive payments under these guarantees if a customer defaults on its obligation to perform under certain credit agreements. Risk participation agreements entered into prior to July 1, 2003 were considered financial guarantees and therefore not included in derivatives. Agreements entered into subsequent to June 30, 2003 are included in the derivative table that follows. We determine that we meet our objective of reducing credit risk associated with certain counterparties to derivative contracts when the participation agreements share in their proportional credit losses of those counterparties.

We generally have established agreements with our major derivative dealer counterparties that provide for exchanges of marketable securities or cash to collateralize either party s positions. At December 31, 2006 we held cash and US government and mortgage-backed securities with a fair value of $109 million and pledged cash with a fair value of $151 million under these agreements.

The total notional or contractual amounts, estimated net fair value and credit risk for derivatives were as follows:

		December 31, 2006			December 31, 2005	
In millions			Credit risk	Notional/	Estimated net	Credit risk

	Notional/ Contract amount	Estimated net fair value		Contract amount	fair value	
Accounting hedges						
Fair value hedges	**$4,996**	**$(1)**	**$51**	$5,900	$78	$108
Cash flow hedges	**7,815**	**62**	**72**	2,926	(9)	5
Total	**$12,811**	**$61**	**$123**	$8,826	$69	$113
Free-standing derivatives						
Interest rate contracts	**$101,749**	**$21**	**$533**	$70,404	$39	$372
Equity contracts	**2,393**	**(63)**	**134**	2,744	(79)	347
Foreign exchange contracts	**7,203**		**61**	4,687	4	60
Credit derivatives	**3,626**	**(11)**	**5**	1,353		7
Options	**97,669**	**68**	**306**	51,383	32	168
Risk participation agreements	**786**			461		
Commitments related to mortgage-related assets	**2,723**	**10**	**15**	1,695	1	6
Other	**20**			254	5	9
Total	**$216,169**	**$25**	**$1,054**	$132,981	$2	$969

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NOTE 17 EMPLOYEE BENEFIT PLANS

PENSION AND POSTRETIREMENT PLANS

We have a noncontributory, qualified defined benefit pension plan covering eligible employees. Benefits are derived from a cash balance formula based on compensation levels, age and length of service. Pension contributions are based on an actuarially determined amount necessary to fund total benefits payable to plan participants.

We also maintain nonqualified supplemental retirement plans for certain employees. We also provide certain health care and life insurance benefits for qualifying retired employees (postretirement benefits) through various plans. The nonqualified pension and postretirement benefit plans are unfunded.

During the second quarter of 2005, we acquired a frozen defined benefit pension plan as a result of the Riggs acquisition. Plan assets and projected benefit obligations of the Riggs plan were approximately $107 million and $116 million, respectively, at acquisition date. The $9 million funding deficit was recognized as part of the Riggs acquisition purchase price allocation. For determining contribution amounts to the plan, deficits are calculated using ERISA-mandated rules, and on this basis we contributed approximately $16 million to the Riggs plan during the third quarter of 2005. We integrated the Riggs plan into the PNC plan on December 30, 2005.

We use a measurement date of December 31 for plan assets and benefit obligations. A reconciliation of the changes in the projected benefit obligation for qualified and nonqualified pension plans and postretirement benefit plans as well as the change in plan assets for the qualified pension plan is as follows:

	Qualified Pension		Nonqualified Pension		Postretirement Benefits	
December 31 (Measurement Date) in millions	**2006**	2005	**2006**	2005	**2006**	2005
Accumulated benefit obligation at end of year	**$1,186**	$1,232	**$73**	$69		
Projected benefit obligation at beginning of year	**$1,290**	$1,166	**$73**	$72	**$270**	$276
Riggs acquisition		116		1		26
Service cost	**34**	33	**1**	1	**2**	2
Interest cost	**68**	65	**4**	4	**13**	14
Amendments	**2**					1
Actuarial loss (gain) (including changes in assumptions)	**(47)**		**3**	2	**(30)**	(28)
Participant contributions					**7**	7
Federal Medicare subsidy on benefits paid					**2**	
Benefits paid	**(102)**	(90)	**(5)**	(7)	**(29)**	(28)
Projected benefit obligation at end of year	**$1,245**	$1,290	**$76**	$73	**$235**	$270
Fair value of plan assets at beginning of year	**$1,627**	$1,492				
Riggs acquisition		107				
Actual return on plan assets	**221**	102				
Employer contribution		16	**$5**	$7	**$20**	$21
Participant contributions					**7**	7
Federal Medicare subsidy on benefits paid					**2**	
Benefits paid	**(102)**	(90)	**(5)**	(7)	**(29)**	(28)
Fair value of plan assets at end of year	**$1,746**	$1,627				
Funded status	**$501**	$337	**$(76)**	$(73)	**$(235)**	$(270)
Unrecognized net actuarial loss		340		26		64
Unrecognized prior service cost (credit)		(1)		1		(38)
Net amount recognized on the balance sheet	**$501**	$676	**$(76)**	$(46)	**$(235)**	$(244)
Amounts recognized in the Consolidated Balance Sheet consist of:						

Other assets (Other liabilities)	**$501**		**$(76)**		**$(235)**	
Prepaid (accrued) pension cost		$676		$(46)		$(244)
Additional minimum liability				(23)		
Intangible asset				1		
Accumulated other comprehensive loss				22		
Net amount recognized in the Consolidated Balance Sheet	**$501**	$676	**$(76)**	$(46)	**$(235)**	$(244)
Amounts recognized in accumulated other comprehensive income consist of:						
Prior service cost (credit)	**2**				**(31)**	
Net actuarial loss	**184**		**28**		**33**	
Amount recognized in AOCI	**$186**		**$28**		**$2**	

The fair value of the qualified pension plan assets exceeds both the accumulated benefit obligation and the projected benefit obligation. The nonqualified pension plan, which contains several individual plans that are accounted for together, is unfunded. Contributions from us and, in the case of postretirement benefit plans, participant contributions cover all benefits paid under the nonqualified pension plan and postretirement benefit plans. The benefit obligations, asset values, funded status and balance sheet impacts are shown in the above table.

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Pension Plan Assets

Assets related to our qualified pension plan (the Plan) are held in trust (the Trust). The trustee is PNC Bank, N.A. The Trust is exempt from tax pursuant to section 501(a) of the Internal Revenue Code (the Code). The Plan is qualified under section 401(a) of the Code. Plan assets consist primarily of listed domestic and international equity securities and US government, agency, and corporate debt securities and real estate investments. Plan assets do not include common or preferred stock or any debt of PNC.

The Pension Plan Administrative Committee (the Committee) adopted the current Pension Plan Investment Policy Statement, including the updated target allocations and allowable ranges shown below, on November 29, 2005.

The long-term investment strategy for pension plan assets is to:

- Meet present and future benefit obligations to all participants and beneficiaries,
- Cover reasonable expenses incurred to provide such benefits, including expense incurred in the administration of the Trust and the Plan,
- Provide sufficient liquidity to meet benefit and expense payment requirements on a timely basis, and
- Provide a total return that, over the long term, maximizes the ratio of trust assets to liabilities by maximizing investment return, at an appropriate level of risk.

The Plan s specific investment objective is to meet or exceed the investment policy benchmark over the long term. The investment policy benchmark compares actual performance to a weighted market index, and measures the contribution of active investment management and policy implementation. This investment objective is expected to be achieved over the long term (one or more market cycles) and is measured over rolling five-year periods. Total return calculations are time-weighted and are net of investment-related fees and expenses.

The asset allocations for the Trust at the end of 2006 and 2005, and the target allocation for 2007, by asset category, are as follows:

	Target Allocation 2007	Allowable Range	Percentage of Plan Assets at December 31 **2006**	2005
Asset Category				
Domestic Equity	35%	32-38%	**39.3%**	39.0%
International Equity	20%	17-23%	**21.3%**	19.6%
Private Equity	5%	0-8%	**1.5%**	.9%
Total Equity	60%		**62.1%**	59.5%
Domestic Fixed Income	30%	27-33%	**28%**	30.7%
High Yield Fixed Income	5%	0-8%	**4.9%**	6.7%
Total Fixed Income	35%		**32.9%**	37.4%
Real Estate	5%	0-8%	**4.8%**	2.5%
Other	0%	0-1%	**.2%**	.6%
Total	100%		**100%**	100%

The Asset Category represents the allocation of Plan assets in accordance with the investment objective of each of the Plan s investment managers. Certain domestic equity investment managers utilize derivatives and fixed income securities as described in their investment management agreements to achieve their investment objective under the Investment Policy Statement.

The slight overweight in domestic equity at year-end 2005 and 2006 was attributable to the targeted allocation in Private Equity, which continues to be committed but which is funded over time as suitable opportunities for private equity investment are identified and as calls for funding are made. The Investment Policy Statement provides that, from time to time, domestic equity may serve as a proxy (substitute) for private equity. Additionally, target allocation changes, which were effective November 29, 2005, included reducing the High Yield Fixed Income allocation from 10% to 5% and creating a new Real Estate allocation of 5%. This transition was completed during 2006.

We believe that, over the long term, asset allocation is the single greatest determinant of risk. Asset allocation will deviate from the target percentages due to market movement, cash flows, and investment manager performance. Material deviations from the asset allocation targets can alter the expected return and risk of the Trust. On the other hand, frequent rebalancing to the asset allocation targets may result in significant transaction costs, which can impair the Trust s ability to meet its investment objective. Accordingly, the Trust portfolio is periodically rebalanced to maintain asset allocation within the target ranges described above.

In addition to being diversified across asset classes, the Trust is diversified within each asset class. Secondary diversification provides a reasonable basis for the expectation that no single security or class of securities will have a disproportionate impact on the total risk and return of the Trust.

The Committee selects investment managers for the Trust based on the contributions that their respective investment styles and processes are expected to make to the investment performance of the overall portfolio. The managers Investment Objectives and Guidelines, which are a part of each manager s Investment Management Agreement, document performance expectations and each manager s role in the portfolio. The Committee uses the Investment Objectives and Guidelines to establish, guide, control and measure the strategy and performance for each manager.

The purpose of investment manager guidelines is to:

- Establish the investment objective and performance standards for each manager,
- Provide the manager with the capability to evaluate the risks of all financial instruments or other assets in which the manager s account is invested, and
- Prevent the manager from exposing its account to excessive levels of risk, undesired or inappropriate risk, or disproportionate concentration of risk.

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The guidelines also indicate which investments and strategies the manager is permitted to use to achieve its performance objectives, and which investments and strategies it is prohibited from using.

Where public market investment strategies may include the use of derivatives and/or currency management, language is incorporated in the managers guidelines to define allowable and prohibited transactions and/or strategies. Derivatives are typically employed by investment managers to modify risk/return characteristics of their portfolio(s), implement asset allocation changes in a cost-effective manner, or reduce transaction costs. Under the managers investment guidelines, derivatives may not be used solely for speculation or leverage. Derivatives are used only in circumstances where they offer the most efficient economic means of improving the risk/reward profile of the portfolio.

BlackRock, PFPC and our Retail Banking business segment receive compensation for providing investment management, trustee and custodial services for the majority of the Trust portfolio. Compensation for such services is paid by PNC. Non-affiliate service providers for the Trust are compensated from plan assets.

The following table provides information regarding our estimated future cash flows related to our various plans:

Estimated Cash Flows

			Postretirement Benefits	
In millions	Qualified Pension	Nonqualified Pension	Gross PNC Benefit Payments	Reduction in PNC Benefit Payments Due to Medicare Part D Subsidy
Estimated 2007 employer contributions	None	$8	$24	$2
Estimated future benefit payments				
2007	$107	$8	$24	$2
2008	111	9	24	2
2009	117	9	24	2
2010	116	10	24	2
2011	121	9	24	2
2012 2016	589	34	113	9

The qualified pension plan contributions are deposited into the Trust, and the qualified pension plan benefit payments are paid from the Trust. For the other plans, total contributions and the benefit payments are the same and represent expected benefit amounts, which are paid from general assets. Postretirement benefits are net of participant contributions.

The components of net periodic pension and postretirement benefit cost/(income) were as follows:

	Qualified Pension Plan			Nonqualified Pension Plan			Postretirement Benefits		
Year ended December 31 in millions	**2006**	2005	2004	**2006**	2005	2004	**2006**	2005	2004
Service cost	**$34**	$33	$35	**$1**	$1	$1	**$2**	$2	$3
Interest cost	**68**	65	65	**4**	4	4	**13**	14	17
Expected return on plan assets	**(129)**	(128)	(112)						
Amortization of prior service cost	**(1)**	(1)	(1)				**(6)**	(7)	(6)
Amortization of actuarial losses (gains)	**16**	23	23	**3**	3	3	**1**	4	5
Curtailment (gain)			(1)						

Net periodic cost	**$(12)**	$(8)	$9	**$8**	$8	$8	**$10**	$13	$19

The weighted-average assumptions used (as of the beginning of each year) to determine net periodic costs shown above were as follows:

	Net Periodic Cost Determination		
Year ended December 31	**2006**	2005	2004
Discount rate			
Qualified pension	**5.50%**	5.25%	6.00%
Nonqualified pension	**5.40**	5.25	6.00
Postretirement benefits	**5.60**	5.25	6.00
Rate of compensation increase (average)	**4.00**	4.00	4.00
Assumed health care cost trend rate			
Initial trend	**10.00**	10.00	11.00
Ultimate trend	**5.00**	5.00	5.00
Year ultimate reached	**2011**	2010	2010
Expected long-term return on plan assets	**8.25**	8.50	8.50

The weighted-average assumptions used (as of the end of each year) to determine year-end obligations for both pension and postretirement benefits were as follows:

	At December 31	
	2006	2005
Discount rate		
Qualified pension	**5.70%**	5.50%
Nonqualified pension	**5.60**	5.40
Postretirement benefits	**5.80**	5.60
Rate of compensation increase	**4.00**	4.00
Assumed health care cost trend rate		
Initial trend	**10.00**	10.00
Ultimate trend	**5.00**	5.00
Year to reach ultimate	**2012**	2011

As of December 31, 2006 and December 31, 2005, the discount rate assumptions were determined independently for each plan reflecting the duration of each plan s obligations.

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Specifically, a yield curve was produced for a universe containing the majority of US-issued Aa grade corporate bonds, all of which were non-callable (or callable with make-whole provisions).

Excluded from this yield curve were the 10% of the bonds with the highest yields and the 10% with the lowest yields. For each plan, the discount rate was determined as the level equivalent rate that would produce the same present value obligation as that using spot rates aligned with the projected benefit payments.

The health care cost trend rate assumptions shown in the preceding tables relate only to the postretirement benefit plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

Year ended December 31, 2006 In millions	Increase	Decrease
Effect on total service and interest cost	**$1**	**$(1)**
Effect on year-end benefit obligation	**11**	**(9)**

As discussed in Note 1 Accounting Policies, we adopted SFAS 158 at December 31, 2006. Under SFAS 158, beginning December 31, 2006, unamortized actuarial gains and losses and prior service costs and credits are recognized in AOCI each December 31, while amortization of these amounts through net periodic benefit cost will occur in accordance with FAS 87 and 106. The estimated amounts that will be amortized in 2007 are as follows:

	2007 Estimate		
Year ended December 31 In millions	Qualified Pension	Nonqualified Pension	Postretirement Benefits
Prior service cost (credit)			$(7)
Net actuarial loss (gain)	$1	$2	1
Total	$1	$2	$(6)

MEDICARE REFORM

In December 2003, the Medicare Prescription Drug Improvement and Modernization Act of 2003 (the Act) was enacted. The Act established a prescription drug benefit under Medicare, known as Medicare Part D, and a federal subsidy to sponsors of postretirement plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. Our actuaries have attested that the benefits we provide to certain participants are at least actuarially equivalent to Medicare Part D, and, accordingly, we will be entitled to a subsidy.

DEFINED CONTRIBUTION PLANS

We have a contributory, qualified defined contribution plan that covers substantially all employees except those covered by other plans as identified below. Under this plan, employee contributions up to 6% of eligible compensation as defined by the plan are matched 100%, subject to Code limitations. The plan is a 401(k) plan and includes an employee stock ownership (ESOP) feature. Employee contributions are

invested in a number of investment options available under the plan, including a PNC common stock fund and several BlackRock mutual funds, at the direction of the employee. All shares of PNC common stock held by the plan are part of the ESOP. Employee contributions to the plan for 2006, 2005 and 2004 were matched primarily by shares of PNC common stock held in treasury, except in the case of those participants who have exercised their diversification election rights to have their matching portion in other investments available within the plan. Effective November 22, 2005, we amended the plan to provide all participants the ability to diversify the matching portion of their plan account invested in shares of PNC common stock into other investments available within the plan. Prior to this amendment, only participants age 50 or older were permitted to exercise this diversification option. Employee benefits expense related to this plan was $52 million in 2006, $47 million in 2005 and $48 million in 2004. We measured employee benefits expense as the fair value of the shares and cash contributed to the plan by PNC.

In conjunction with the BlackRock deconsolidation, BlackRock employees ceased participating in the plan September 30, 2006. On October 3, 2006, approximately $127 million in plan assets were transferred from the plan.

Additionally, Hilliard Lyons sponsors a contributory, qualified defined contribution plan that covers substantially all of its employees who are not covered by the plan described above. Contributions to this plan are made in cash and include a base contribution for those participants employed at December 31, a matching of employee contributions, and a discretionary profit sharing contribution as determined by Hilliard Lyons Executive Compensation Committee. Employee benefits expense for this plan was $5 million in 2006, $6 million in 2005 and $5 million in 2004.

Effective July 1, 2004, we adopted a separate qualified defined contribution plan that covers substantially all US-based PFPC employees not covered by our plan. The plan is a 401(k) plan and includes an ESOP feature. Under this plan, employee contributions of up to 6% of eligible compensation as defined by the plan may be matched annually based on PFPC performance levels. Participants must be employed as of December 31 of each year to receive this annual contribution. The performance-based employer matching contribution will be made primarily in shares of PNC common stock held in treasury, except in the case of those participants who have exercised their diversification election rights to have their matching portion in other investments available within the plan. Mandatory employer contributions to this plan are made in cash and include employer basic and transitional contributions. Employee-directed contributions are invested in a number of investment options available under the plan, including a PNC common stock fund and several BlackRock mutual funds, at the direction of the employee. Effective November 22, 2005, we amended the plan to provide all participants the ability to

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diversify the matching portion of their plan account invested in shares of PNC common stock into other investments available within the plan. Prior to this amendment, only participants age 50 or older were permitted to exercise this diversification option. Employee benefits expense for this plan, which was effective July 1, 2004, was $9 million in 2006, $12 million in 2005 and $5 million for 2004. We measured employee benefits expense as the fair value of the shares and cash contributed to the plan.

We also maintain a nonqualified supplemental savings plan for certain employees.

NOTE 18 STOCK-BASED COMPENSATION PLANS

We have long-term incentive award plans (Incentive Plans) that provide for the granting of incentive stock options, nonqualified stock options, stock appreciation rights, incentive shares/performance units, restricted stock, other share-based awards and dollar-denominated awards to executives and, other than incentive stock options, to non-employee directors. As of December 31, 2006, no incentive stock options or stock appreciation rights were outstanding.

NONQUALIFIED STOCK OPTIONS

Options are granted at exercise prices not less than the market value of common stock on the grant date. Generally, options granted since 1999 become exercisable in installments after the grant date. Options granted prior to 1999 are mainly

exercisable 12 months after the grant date. No option may be exercisable after 10 years from its grant date. Payment of the option exercise price may be in cash or previously owned shares of common stock at market value on the exercise date.

Generally, options granted under the Incentive Plans vest ratably over a three-year period as long as the grantee remains an employee or, in certain cases, retires from PNC. For all options granted prior to the adoption of SFAS 123R, we recognized compensation expense over the three-year vesting period. If an employee retired prior to the end of the three-year vesting period, we accelerated the expensing of all unrecognized compensation costs at the retirement date. As required under SFAS 123R, we recognize compensation expense for options granted to retirement-eligible employees after January 1, 2006 in the period granted, in accordance with the service period provisions of the options.

A summary of stock option activity follows:

Options outstanding at December 31 Shares in thousands	Per Option Exercise Price		Weighted-Average Exercise Price	Shares
December 31, 2005	$31.13	$76.00	$55.30	18,292
Granted	**62.71**	**71.38**	**67.83**	**2,410**
Exercised	**31.13**	**66.97**	**49.32**	**(5,462)**
Forfeited	**43.41**	**74.59**	**66.49**	**(290)**
December 31, 2006	**$37.43**	**$76.00**	**$59.29**	**14,950**

Information about stock options outstanding at December 31, 2006 follows:

Options Outstanding Options Exercisable

December 31, 2006

Shares in thousands

Range of exercise prices		Shares	Weighted-average exercise price	Weighted-average remaining contractual life (in years)	Shares	Weighted-average exercise price
$37.43	**$42.99**	**680**	**$ 41.60**	**3.5**	**680**	**$ 41.60**
43.00	**52.99**	**2,003**	**46.70**	**4.9**	**1,949**	**46.55**
53.00	**59.99**	**6,555**	**55.07**	**6.1**	**4,765**	**55.58**
60.00	**76.00**	**5,712**	**70.64**	**5.5**	**3,349**	**72.65**
Total		**14,950**	**$ 59.29**	**5.6**	**10,743**	**$ 58.38**

At December 31, 2006, there were approximately 14,304,000 options in total that were vested and are expected to vest. The weighted-average grant-date fair value of such options was $59.19 per share, the weighted-average remaining contractual life was approximately 5.5 years, and the aggregate intrinsic value at December 31, 2006 was approximately $219 million.

Options granted in 2005 and 2004 include options for 30,000 shares that were granted to non-employee directors in each year. No such options were granted in 2006.

The weighted-average grant-date fair value of options granted in 2006, 2005 and 2004 was $9.94, $8.72 and $9.64 per option, respectively. At December 31, 2005 and 2004 options for 13,582,000 and 12,693,000 shares of common stock,

respectively, were exercisable at a weighted-average price of $56.58 and $56.41, respectively. The total intrinsic value of options exercised during 2006, 2005 and 2004 was $111 million, $31 million and $17 million, respectively. At December 31, 2006 the aggregate intrinsic value of all options outstanding and exercisable was $227 million and $173 million, respectively.

Cash received from option exercises under all Incentive Plans for 2006, 2005 and 2004 was approximately $233 million, $98 million and $42 million, respectively. The actual tax benefit realized for tax deduction purposes from option exercises under all Incentive Plans for 2006, 2005 and 2004 was approximately $82 million, $34 million and $15 million, respectively.

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There were no options granted in excess of market value in 2006, 2005 or 2004. Shares of common stock available during the next year for the granting of options and other awards under the Incentive Plans were 42,767,760 at December 31, 2006.

During 2006, we issued approximately 4.9 million shares from treasury stock in connection with stock option exercise activity. As with past exercise activity, we intend to utilize treasury stock for future stock option exercises.

As discussed in Note 1 Accounting Policies, we adopted the fair value recognition provisions of SFAS 123 prospectively to all employee awards including stock options granted, modified or settled after January 1, 2003. As permitted under SFAS 123, we recognized compensation expense for stock options on a straight-line basis over the pro rata vesting period. Total compensation expense recognized related to PNC stock options in 2006 was $31 million compared with $29 million in 2005 and $21 million in 2004.

Pro Forma Effects

A table is included in Note 1 Accounting Policies that sets forth pro forma net income and basic and diluted earnings per share as if compensation expense had been recognized under SFAS 123 and 123R, as amended, for stock options for 2006, 2005 and 2004.

For purposes of computing stock option expense and pro forma results, we estimated the fair value of stock options using the Black-Scholes option pricing model. The model requires the use of numerous assumptions, many of which are very subjective. Therefore, the pro forma results are estimates of results of operations as if compensation expense had been recognized for all stock-based compensation awards and are not indicative of the impact on future periods.

We used the following assumptions in the option pricing model for purposes of estimating pro forma results as well as to determine actual stock option expense:

- The risk-free interest rate is based on the US Treasury yield curve,
- The dividend yield represents average yields over the previous three-year period,
- Volatility is measured using the fluctuation in month-end closing stock prices over a five-year period, and
- The expected life assumption represents the period of time that options granted are expected to be outstanding and is based on a weighted-average of historical option activity.

Option Pricing Assumptions

Weighted-average for the year ended December 31	**2006**	2005	2004
Risk-free interest rate	**4.5%**	3.8%	3.4%
Dividend yield	**3.7**	3.8	3.6
Volatility	**20.5**	25.7	28.9
Expected life	**5.1 yrs.**	4.8 yrs.	4.9 yrs.

Incentive/Performance Unit Share and Restricted Stock Awards

The fair value of nonvested incentive/performance unit shares and restricted stock awards is initially determined based on the average of the high and low of our common stock price on the date of grant. Incentive/performance unit shares are subsequently valued subject to the achievement of one or more financial and other performance goals over a three-year period. The Personnel and Compensation Committee of the Board of Directors approves the final award of incentive/performance unit shares. Restricted stock awards have various vesting periods ranging from 36 months to 60 months. There are no financial or performance goals associated with any of our restricted stock awards.

The weighted-average grant-date fair value of incentive share and restricted stock awards granted in 2006, 2005 and 2004 was $67.36, $53.81 and $54.46 per share, respectively. We recognize compensation expense for incentive/performance unit shares and restricted stock awards ratably over the corresponding vesting and/or performance periods for each type of program. Total compensation expense recognized related to PNC incentive/performance unit share and restricted stock awards during 2006 was approximately $45 million compared with $44 million in 2005 and $25 million in 2004.

A summary of nonvested incentive/performance unit shares and restricted stock award activity follows:

Shares in thousands	Nonvested Incentive/ Performance Unit Shares	Weighted-Average Grant Date Fair Value	Nonvested Restricted Shares	Weighted-Average Grant Date Fair Value
Dec. 31, 2005	660	$ 41.01	2,209	$ 50.84
Granted	**186**	**69.58**	**595**	**64.19**
Awarded as restricted	**(649)**	**41.02**	**649**	**66.95**
Vested			**(917)**	**53.14**
Forfeited	**(11)**	**40.51**	**(111)**	**53.06**
Dec. 31, 2006	**186**	**$ 69.58**	**2,425**	**$ 57.45**

At December 31, 2006, there was $47 million of unrecognized deferred compensation expense related to nonvested share-based compensation arrangements granted under the Incentive Plans. This cost is expected to be recognized as expense over a period of no longer than five years. The total fair value of incentive/performance unit share and restricted stock awards vested during 2006, 2005 and 2004 was approximately $63 million, $3 million and $5 million, respectively.

Additionally in 2006, we granted a performance unit incentive award to a certain senior executive. The grant is share-denominated with an initial specified target number of 30,000 share units. The potential award is dependent on the achievement of certain performance criteria over a three-year period ending December 31, 2008. Final awarded performance units will be paid only in cash. Total compensation expense recognized related to this incentive award during 2006 was approximately $1 million.

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Employee Stock Purchase Plan

Our ESPP has approximately 1.4 million shares available for issuance. Full-time employees with six months and part-time employees with 12 months of continuous employment with us are eligible to participate in the ESPP at the commencement of the next six-month offering period. Eligible participants may purchase our common stock at 95% of the fair market value on the last day of each six-month offering period. No charge to earnings is recorded with respect to the ESPP.

Shares issued pursuant to the ESPP were as follows:

Year ended December 31	Shares		Price Per Share
2006	**105,041**	**$**	**66.66 and $70.34**
2005	138,754		51.74 and 58.74
2004	156,753		50.43 and 54.57

BlackRock LTIP Programs

BlackRock adopted the 2002 LTIP program to help attract and retain qualified professionals. At that time, we agreed to transfer 4 million of the shares of BlackRock common stock then held by us to fund the 2002 and future programs approved by BlackRock s board of directors, subject to certain conditions and limitations. Prior to 2006, BlackRock granted awards under the 2002 LTIP program of approximately $230 million, of which approximately $210 million was paid on January 30, 2007. The awards were paid approximately 17%

in cash by BlackRock and the remainder in BlackRock common stock transferred by us to the LTIP participants (approximately 1 million shares). As permitted under the award agreements, employees elected to put approximately 95% of the stock portion of the awards back to BlackRock. These shares were retained by BlackRock as treasury stock.

BlackRock granted additional restricted stock unit awards in January 2007, all of which are subject to achieving earnings performance goals prior to the vesting date of September 29, 2011. Of the shares of BlackRock common stock that we have agreed to transfer to fund their LTIP programs, approximately 1.6 million shares have been committed to fund the restricted stock unit awards vesting in 2011 and the amount remaining would then be available for future awards.

We reported noninterest expense of $33 million, $64 million and $110 million for the years ended December 31, 2006, 2005 and 2004, respectively, related to the BlackRock LTIP awards. Additionally, noninterest income in the fourth quarter of 2006 included a $12 million charge related to our commitment to fund the BlackRock LTIP programs. This charge represents the mark-to-market of our BlackRock LTIP obligation as of December 31, 2006 and is a result of the fourth quarter increase in the market value of BlackRock common shares.

Note 19 Earnings Per Share

The following table sets forth basic and diluted earnings per common share calculations:

Year ended December 31 - in millions, except share and per share data	**2006**	2005	2004
Calculation Of Basic Earnings Per Common Share			
Net income	**$2,595**	$1,325	$1,197
Less: Preferred dividends declared	**1**	1	1
Net income applicable to basic earnings per common share	**$2,594**	$1,324	$1,196
Basic weighted-average common shares outstanding (in thousands)	**291,758**	286,276	281,248
Basic earnings per common share	**$8.89**	$4.63	$4.25
Calculation Of Diluted Earnings Per Common Share (a)			
Net income	**$2,595**	$1,325	$1,197

Less: BlackRock adjustment for common stock equivalents	**6**	7	4
Net income applicable to diluted earnings per common share	**$2,589**	$1,318	$1,193
Basic weighted-average common shares outstanding (in thousands)	**291,758**	286,276	281,248
Weighted-average common shares to be issued using average market price and assuming:			
Conversion of preferred stock Series A and B	**70**	78	85
Conversion of preferred stock Series C and D	**584**	618	663
Conversion of debentures	**2**	2	10
Exercise of stock options	**2,178**	1,178	992
Incentive share awards	**1,930**	1,688	634
Diluted weighted-average common shares outstanding (in thousands)	**296,522**	289,840	283,632
Diluted earnings per common share	**$8.73**	$4.55	$4.21
(a) Excludes stock options considered to be anti-dilutive (in thousands)	**4,230**	10,532	10,762

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NOTE 20 INCOME TAXES

The components of income taxes are as follows:

Year ended December 31 In millions	**2006**	2005	2004
Current			
Federal	**$565**	$550	$720
State	**46**	53	12
Total current	**611**	603	732
Deferred			
Federal	**752**	(12)	(192)
State		13	(2)
Total deferred	**752**	1	(194)
Total	**$1,363**	$604	$538

Significant components of deferred tax assets and liabilities are as follows:

December 31 - in millions	**2006**	2005
Deferred tax assets		
Allowance for loan and lease losses	**$258**	$311
Net unrealized securities losses	**52**	135
Compensation and benefits	**296**	56
Loan valuation	**6**	10
Other	**277**	240
Total deferred tax assets	**889**	752
Deferred tax liabilities		
Leasing	**1,025**	1,078
Depreciation	**75**	103
Goodwill	**205**	206
BlackRock basis difference	**1,166**	6
Other	**56**	15
Total deferred tax liabilities	**2,527**	1,408
Net deferred tax liability	**$1,638**	$656

A reconciliation between the statutory and effective tax rates follows:

Year ended December 31	**2006**	2005	2004
Statutory tax rate	**35.0%**	35.0%	35.0%
Increases (decreases) resulting from			
State taxes	**.8**	2.1	.4
Tax-exempt interest	**(.3)**	(1.1)	(.7)
Life insurance	**(.6)**	(1.0)	(1.1)
Tax credits	**(.9)**	(1.8)	(2.3)
Reversal of deferred tax liabilities BlackRock basis allocation		(2.3)	
Other		(.7)	(1.0)
Effective tax rate	**34.0%**	30.2%	30.3%

At December 31, 2006 we had available $104 million of federal and $221 million of state income tax net operating loss carryforwards originating from acquired companies and $73 million in other state net operating losses which will expire from 2007 through 2026.

No deferred US income taxes have been provided on certain undistributed earnings of non-US subsidiaries, which amounted to $39 million at December 31, 2006. As of September 30, 2006, these earnings are considered to be reinvested for an indefinite period of time or will be repatriated when it is tax effective to do so. It is not practicable to determine the deferred tax liability on these earnings.

See Note 1 Accounting Policies for a discussion of FIN 48.

NOTE 21 SEGMENT REPORTING

We have four major businesses engaged in providing banking, asset management and global fund processing products and services:

Retail Banking,
Corporate & Institutional Banking,
BlackRock, and
PFPC.

Results of individual businesses are presented based on our management accounting practices and our management structure. There is no comprehensive, authoritative body of guidance for management accounting equivalent to GAAP; therefore, the financial results of individual businesses are not necessarily comparable with similar information for any other company. We refine our methodologies from time to time as our management accounting practices are enhanced and our businesses and management structure change. Financial results are presented, to the extent practicable, as if each business, with the exception of our BlackRock segment, operated on a stand-alone basis. As permitted under GAAP, we have aggregated the business results for certain operating segments for financial reporting purposes.

Assets receive a funding charge and liabilities and capital receive a funding credit based on a transfer pricing methodology that incorporates product maturities, duration and other factors. Capital is intended to cover unexpected losses and is assigned to the banking and processing businesses using our risk-based economic capital model. We have increased the capital assigned to Retail Banking to 6% of funds to reflect the capital required for well-capitalized banks and to approximate market comparables for this business. The capital for PFPC has been increased to reflect its legal entity shareholders equity.

BlackRock business segment results for the nine months ended September 30, 2006 and full years 2005 and 2004 reflected our majority ownership in BlackRock during those periods. Subsequent to the September 29, 2006 BlackRock/MLIM transaction closing, which had the effect of reducing our ownership interest to approximately 34%, our investment in BlackRock was accounted for under the equity method but continues to be a separate reportable business segment of PNC. The fair value of our investment in BlackRock at December 31, 2006 was approximately $6.7 billion. Our prior period business segment information included in this Note 21 for BlackRock was not restated. See Note 2 Acquisitions regarding the BlackRock/MLIM transaction.

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We have allocated the allowances for loan and lease losses and unfunded loan commitments and letters of credit based on our assessment of risk inherent in the loan portfolios. Our allocation of the costs incurred by operations and other support areas not directly aligned with the businesses is primarily based on the use of services.

Total business segment financial results differ from total consolidated results. The impact of these differences is reflected in the Intercompany Eliminations and Other categories. Intercompany Eliminations reflects activities conducted among our businesses that are eliminated in the consolidated results. Other includes residual activities that do not meet the criteria for disclosure as a separate reportable business, such as gains or losses related to BlackRock, 2006 BlackRock/MLIM integration costs, One PNC implementation costs, asset and liability management activities, related net securities gains or losses, certain trading activities, equity management activities and minority interest in income of BlackRock up to September 29, 2006, differences between business segment performance reporting and financial statement reporting (GAAP), and most corporate overhead.

Assets, revenue and earnings attributable to foreign activities were not material in the periods presented.

Business Segment Products And Services

Retail Banking provides deposit, lending, brokerage, trust, investment management, and cash management services to approximately 2.5 million consumer and small business customers within our primary geographic area. Our customers are serviced through approximately 850 offices in our branch network, the call center located in Pittsburgh and the Internet *www.pncbank.com*. The branch network is located primarily in Pennsylvania; New Jersey; the greater Washington, DC area, including Maryland and Virginia; Ohio; Kentucky; and Delaware. Brokerage services are provided through PNC Investments, LLC, and J.J.B. Hilliard, W.L. Lyons, Inc. Retail Banking also serves as investment manager and trustee for employee benefit plans and charitable and endowment assets and provides nondiscretionary defined contribution plan services and investment options through its *Vested Interest*® product. These services are provided to individuals and corporations primarily within our primary geographic markets.

Corporate & Institutional Banking provides lending, treasury management, and capital markets products and services to mid-sized corporations, government entities, and selectively to large corporations. Lending products include secured and unsecured loans, letters of credit and equipment leases. Treasury management services include cash and investment management, receivables management, disbursement services, funds transfer services, information reporting, and global trade services. Capital markets-related products and services include foreign exchange, derivatives, loan syndications, mergers and acquisitions advisory and related services to middle-market companies, securities underwriting, and securities sales and trading. Corporate & Institutional Banking also provides commercial loan servicing, real estate advisory and technology solutions for the commercial real estate finance industry. Corporate & Institutional Banking provides products and services generally within our primary geographic markets, with certain products and services provided nationally.

BlackRock is one of the world s largest publicly traded investment management firms. As of December 31, 2006, BlackRock s assets under management were approximately $1.1 trillion. The firm manages assets on behalf of institutions and individuals worldwide through a variety of equity, fixed income, cash management and alternative investment products. In addition, BlackRock provides BlackRock Solutions® investment system, risk management, and financial advisory services to a growing number of institutional investors. The firm has a major presence in key global markets, including the United States, Europe, Asia, Australia and the Middle East.

See Note 2 Acquisitions regarding the BlackRock/MLIM transaction.

PFPC is a leading full service provider of processing, technology and business solutions for the global investment industry. Securities services include custody, securities lending, and accounting and administration for funds registered under the 1940 Act and alternative investments. Investor services include transfer agency, managed accounts, subaccounting, and distribution. PFPC serviced $2.2 trillion in total assets and 68 million shareholder accounts as of December 31, 2006 both domestically and internationally through its Ireland and Luxembourg operations.

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Results Of Businesses

Year ended December 31 In millions	Retail Banking	Corporate & Institutional Banking	BlackRock	PFPC	Other	Intercompany Eliminations	Consolidated
2006							
INCOME STATEMENT							
Net interest income (expense)	**$1,673**	**$711**	**$20**	**$(38)**	**$(121)**		**$2,245**
Noninterest income	**1,447**	**752**	**1,135**	**917**	**2,137**	**$(61)**	**6,327**
Total revenue	**3,120**	**1,463**	**1,155**	**879**	**2,016**	**(61)**	**8,572**
Provision for credit losses	**81**	**42**			**1**		**124**
Depreciation and amortization	**67**	**23**	**29**	**57**	**99**		**275**
Other noninterest expense	**1,760**	**726**	**828**	**646**	**266**	**(58)**	**4,168**
Earnings before minority interests in BlackRock and income taxes	**1,212**	**672**	**298**	**176**	**1,650**	**(3)**	**4,005**
Minority interests in BlackRock					**47**		**47**
Income taxes	**447**	**209**	**104**	**52**	**552**	**(1)**	**1,363**
Earnings	**$765**	**$463**	**$194**	**$124**	**$1,051**	**$(2)**	**$2,595**
Inter-segment revenue	**$13**	**$9**	**$28**	**$12**	**$(1)**	**$(61)**	
AVERAGE ASSETS (a)	**$29,248**	**$26,548**	**$3,937**	**$2,204**	**$35,611**	**$(2,536)**	**$95,012**
2005							
INCOME STATEMENT							
Net interest income (expense)	$1,588	$729	$35	$(33)	$(165)		$2,154
Noninterest income	1,275	596	1,191	879	312	$(80)	4,173
Total revenue	2,863	1,325	1,226	846	147	(80)	6,327
Provision for (recoveries of) credit losses	52	(30)			(1)		21
Depreciation and amortization	62	20	31	56	107		276
Other noninterest expense	1,664	638	822	629	329	(52)	4,030
Earnings before minority interests in BlackRock and income taxes	1,085	697	373	161	(288)	(28)	2,000
Minority interests in BlackRock					71		71
Income taxes	403	217	139	57	(202)	(10)	604
Earnings	$682	$480	$234	$104	$(157)	$(18)	$1,325
Inter-segment revenue	$13	$7	$32	$3	$25	$(80)	
AVERAGE ASSETS (a)	$27,618	$25,309	$1,848	$2,128	$33,315	$(1,670)	$88,548
2004							
INCOME STATEMENT							
Net interest income (expense)	$1,479	$701	$34	$(47)	$(198)		$1,969
Noninterest income	1,223	552	725	810	324	$(62)	3,572
Total revenue	2,702	1,253	759	763	126	(62)	5,541
Provision for (recoveries of) credit losses	61	5			(14)		52
Depreciation and amortization	53	17	21	45	80		216
Other noninterest expense	1,630	598	543	601	184	(60)	3,496
Earnings before minority interests in BlackRock and income taxes	958	633	195	117	(124)	(2)	1,777
Minority interests in BlackRock					42		42
Income taxes	348	190	52	47	(98)	(1)	538
Earnings	$610	$443	$143	$70	$(68)	$(1)	$1,197
Inter-segment revenue	$12	$7	$33		$10	$(62)	
AVERAGE ASSETS (a)	$24,261	$21,589	$1,145	$2,572	$27,582	$(1,883)	$75,266

(a) Period-end balances for BlackRock and PFPC.

BlackRock income classified as net interest income in the preceding table represents the net of investment income and interest expense as presented in the Business Segments Review Section. PFPC income classified as net interest income (expense) in the preceding table represents the interest components of nonoperating income (net of nonoperating expense) and debt financing as disclosed in the Business Segments Review Section.

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NOTE 22 OTHER COMPREHENSIVE INCOME

Details of other comprehensive income (loss) are as follows (in millions):

	Pretax	Tax	After-tax
Net unrealized securities gains (losses)			
Balance at January 1, 2004			$3
2004 activity			
Increase in net unrealized losses for securities held at year-end	$(56)	$20	(36)
Less: net gains realized in net income (a)	50	(17)	33
Net unrealized securities losses	(106)	37	(69)
Balance at December 31, 2004			(66)
2005 activity			
Increase in net unrealized losses for securities held at year-end	(312)	109	(203)
Less: net losses realized in net income (a)	(44)	15	(29)
Net unrealized securities losses	(268)	94	(174)
Balance at December 31, 2005			(240)
2006 activity			
Increase in net unrealized gains for securities held at year-end	**129**	**(46)**	**83**
Less: net losses realized in net income (a)	**(101)**	**35**	**(66)**
Net unrealized securities gains	**230**	**(81)**	**149**
Balance at December 31, 2006			**$(91)**

(a) Pretax amounts represent net unrealized gains (losses) as of the prior year-end date that were realized in the subsequent year when the related securities were sold. These amounts differ from net securities gains included in the Consolidated Income Statement primarily because they do not include gains or losses realized on securities that were purchased and then sold during the same year.

	Pretax	Tax	After-tax
Net unrealized gains (losses) on cash flow hedge derivatives			
Balance at January 1, 2004			$48
2004 activity			
Increase in net unrealized losses on cash flow hedge derivatives	$(30)	$11	(19)
Less: net gains realized in net income	35	(12)	23
Net unrealized losses on cash flow hedge derivatives	(65)	23	(42)
Balance at December 31, 2004			6
2005 activity			
Increase in net unrealized losses on cash flow hedge derivatives	(49)	17	(32)
Less: net gains realized in net income			
Net unrealized losses on cash flow hedge derivatives	(49)	17	(32)
Balance at December 31, 2005			(26)
2006 activity			
Increase in net unrealized gains on cash flow hedge derivatives	**13**	**(5)**	**8**
Less: net gains realized in net income	**(7)**	**2**	**(5)**
Net unrealized losses on cash flow hedge derivatives	**20**	**(7)**	**13**
Balance at December 31, 2006			**$(13)**
Pension, other postretirement and postemployment benefit plan adjustments			
Balance at January 1, 2004			$(14)
2004 activity	$(2)	$1	(1)
Balance at December 31, 2004			(15)
2005 activity			
Balance at December 31, 2005			(15)
2006 Activity			
SFAS 87 adjustment	**(2)**	**1**	**(1)**
SFAS 158 adjustment, net	**(203)**	**71**	**(132)**
Total 2006 activity	**(205)**	**72**	**(133)**

Balance at December 31, 2006			**$(148)**
***Other* (b)**			
Balance at January 1, 2004			$23
2004 activity	$(3)	$1	(2)
Balance at December 31, 2004			21
2005 activity	(11)	4	(7)
Balance at December 31, 2005			14
2006 Activity	**6**	**(3)**	**3**
Balance at December 31, 2006			**$17**

(b) Consists of interest-only strip valuation adjustments and foreign currency translation adjustments.

The accumulated balances related to each component of other comprehensive income (loss) are as follows:

December 31 in millions	**2006**	2005
Net unrealized securities gains (losses)	**$(91)**	$(240)
Net unrealized gains (losses) on cash flow hedge derivatives	**(13)**	(26)
Pension, other postretirement and postemployment benefit plan adjustments	**(148)**	(15)
Other	**17**	14
Accumulated other comprehensive income (loss)	**$(235)**	$(267)

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NOTE 23 FAIR VALUE OF FINANCIAL INSTRUMENTS

December 31 - in millions	2006 Carrying Amount	2006 Fair Value	2005 Carrying Amount	2005 Fair Value
Assets				
Cash and short-term assets	**$ 9,016**	**$ 9,016**	$ 6,957	$ 6,957
Securities	**23,191**	**23,191**	20,710	20,710
Loans held for sale	**2,366**	**2,366**	2,449	2,449
Net loans (excludes leases)	**46,757**	**46,878**	45,713	45,883
Other assets	**892**	**892**	965	965
Mortgage and other loan servicing rights	**477**	**552**	344	403
Financial derivatives				
Fair value hedges	**51**	**51**	108	108
Cash flow hedges	**72**	**72**	5	5
Free-standing derivatives	**1,054**	**1,054**	969	969
Liabilities				
Demand, savings and money market deposits	**47,277**	**47,277**	43,914	43,914
Time deposits	**19,024**	**18,959**	16,361	16,215
Borrowed funds	**15,310**	**15,496**	17,186	17,323
Financial derivatives				
Fair value hedges	**52**	**52**	30	30
Cash flow hedges	**10**	**10**	14	14
Free-standing derivatives	**1,029**	**1,029**	967	967
Unfunded loan commitments and letters of credit	**101**	**122**	77	98

The aggregate fair values in the table above do not represent our underlying market value as the table excludes the following:

- real and personal property,
- lease financing,
- loan customer relationships,
- deposit customer intangibles,
- retail branch networks,
- fee-based businesses, such as asset management and brokerage, and
- trademarks and brand names.

Fair value is defined as the estimated amount at which a financial instrument could be exchanged in a current transaction between willing parties, or other than in a forced or liquidation sale. However, it is not our intention to immediately dispose of a significant portion of such financial instruments, and unrealized gains or losses should not be interpreted as a forecast of future earnings and cash flows. The derived fair values are subjective in nature and involve uncertainties and significant judgment. Therefore, they cannot be determined with precision. Changes in our assumptions could significantly impact the derived fair value estimates.

We used the following methods and assumptions to estimate fair value amounts for financial instruments.

GENERAL

For short-term financial instruments realizable in three months or less, the carrying amount reported in the consolidated

balance sheet approximates fair value. Unless otherwise stated, the rates used in discounted cash flow analyses are based on market yield curves.

CASH AND SHORT-TERM ASSETS

The carrying amounts reported in the consolidated balance sheet for cash and short-term investments approximate fair values primarily due to their short-term nature. For purposes of this disclosure only, short-term assets include the following:

- due from banks,
- interest-earning deposits with banks,
- federal funds sold and resale agreements,
- trading securities,
- cash collateral,
- customers acceptance liability, and
- accrued interest receivable.

SECURITIES

The fair value of securities is based on quoted market prices, where available. If quoted market prices are not available, fair value is estimated using the quoted market prices of comparable instruments.

NET LOANS AND LOANS HELD FOR SALE

Fair values are estimated based on the discounted value of expected net cash flows incorporating assumptions about prepayment rates, credit losses and servicing fees and costs. For revolving home equity loans, this fair value does not include any amount for new loans or the related fees that will

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be generated from the existing customer relationships. In the case of nonaccrual loans, scheduled cash flows exclude interest payments. The carrying value of loans held for sale approximates fair value.

Loans are presented above net of the allowance for loan and lease losses.

Other Assets

Other assets as shown in the accompanying table include the following:

- noncertificated interest-only strips,
- FHLB and FRB stock,
- equity investments carried at cost and fair value, and
- private equity investments carried at fair value.

Investments accounted for under the equity method, including our investment in BlackRock, are not included in the accompanying table.

The carrying amounts of private equity investments are recorded at fair value. Fair value of the noncertificated interest-only strips is estimated based on the discounted value of expected net cash flows. The equity investments carried at cost, including the FHLB and FRB stock, have a carrying value of approximately $365 million as of December 31, 2006, and $321 million as of December 31, 2005, both of which approximate fair value at each date.

Mortgage And Other Loan Servicing Assets

Fair value is based on the present value of the future cash flows, including assumptions as to prepayment speeds, discount rates, interest rates, cost to service and other factors.

Deposits

The carrying amounts of noninterest-bearing demand and interest-bearing money market and savings deposits approximate fair values. For time deposits, which include foreign deposits, fair values are estimated based on the discounted value of expected net cash flows assuming current interest rates.

Borrowed Funds

The carrying amounts of federal funds purchased, commercial paper, acceptances outstanding and accrued interest payable are considered to be their fair value because of their short-term nature. For all other borrowed funds, fair values are estimated based on the discounted value of expected net cash flows assuming current interest rates.

Unfunded Loan Commitments And Letters Of Credit

The fair value of unfunded loan commitments and letters of credit is our estimate of the cost to terminate them. For purposes of this disclosure, this fair value is the sum of the deferred fees currently recorded by us on these facilities and the liability established on these facilities related to their creditworthiness.

Financial Derivatives

For exchange-traded contracts, fair value is based on quoted market prices. For nonexchange-traded contracts, fair value is based on dealer quotes, pricing models or quoted prices for instruments with similar characteristics.

Note 24 Commitments and Guarantees

Equity Funding Commitments

We had commitments to make additional equity investments in certain equity management entities of $123 million and affordable housing limited partnerships of $71 million at December 31, 2006.

Additionally, in October 2005, we committed $200 million to PNC Mezzanine Partners III, L.P., a $350 million mezzanine fund, that invests principally in subordinated debt securities with an equity component. Funding of this investment is expected to occur over a five-year period. The remaining unfunded commitment on December 31, 2006 was $155 million. The limited partnership is consolidated for financial reporting purposes as PNC has a 57% ownership interest.

Standby Letters of Credit

We issue standby letters of credit and have risk participations in standby letters of credit and bankers acceptances issued by other financial institutions, in each case to support obligations of our customers to third parties. If the customer fails to meet its financial or performance obligation to the third party under the terms of the contract, then upon the request of the guaranteed party, we would be obligated to make payment to them. The standby letters of credit and risk participations in standby letters of credit and bankers acceptances outstanding on December 31, 2006 had terms ranging from less than one year to 10 years. The aggregate maximum amount of future payments we could be required to make under outstanding standby letters of credit and risk participations in standby letters of credit and bankers acceptances was $6.6 billion at December 31, 2006.

Assets valued as of December 31, 2006 of approximately $.9 billion secured certain specifically identified standby letters of credit. Approximately $2.2 billion in recourse provisions from third parties was also available for this purpose as of December 31, 2006. In addition, a portion of the remaining standby letters of credit and letter of credit risk participations issued on behalf of specific customers is also secured by collateral or guarantees that secure the customers other obligations to us. The carrying amount of the liability for our obligations related to standby letters of credit and risk participations in standby letters of credit and bankers acceptances was $57 million at December 31, 2006.

Standby Bond Purchase Agreements and Other Liquidity Facilities

We enter into standby bond purchase agreements to support municipal bond obligations. At December 31, 2006, the

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aggregate of PNC s commitments under these facilities was $240 million. PNC also enters into certain other liquidity facilities to support individual pools of receivables acquired by commercial paper conduits including Market Street. At December 31, 2006, our total commitments under these facilities were $5.7 billion, of which $5.6 billion was related to Market Street.

INDEMNIFICATIONS

We are a party to numerous acquisition or divestiture agreements under which we have purchased or sold, or agreed to purchase or sell, various types of assets. These agreements can cover the purchase or sale of:

- Entire businesses,
- Loan portfolios,
- Branch banks,
- Partial interests in companies, or
- Other types of assets.

These agreements generally include indemnification provisions under which we indemnify the third parties to these agreements against a variety of risks to the indemnified parties as a result of the transaction in question. When PNC is the seller, the indemnification provisions will generally also provide the buyer with protection relating to the quality of the assets we are selling and the extent of any liabilities being assumed by the buyer. Due to the nature of these indemnification provisions, we cannot quantify the total potential exposure to us resulting from them.

We provide indemnification in connection with securities offering transactions in which we are involved. When we are the issuer of the securities, we provide indemnification to the underwriters or placement agents analogous to the indemnification provided to the purchasers of businesses from us, as described above. When we are an underwriter or placement agent, we provide a limited indemnification to the issuer related to our actions in connection with the offering and, if there are other underwriters, indemnification to the other underwriters intended to result in an appropriate sharing of the risk of participating in the offering. Due to the nature of these indemnification provisions, we cannot quantify the total potential exposure to us resulting from them.

We enter into certain types of agreements that include provisions for indemnifying third parties, such as:

- Agreements relating to providing various servicing and processing functions to third parties,
- Agreements relating to the creation of trusts or other legal entities to facilitate leasing transactions, commercial mortgage-backed securities transactions (loan securitizations) and certain other off-balance sheet transactions,
- Confidentiality agreements,
- Syndicated credit agreements, as a syndicate member,
- Sales of individual loans and equipment leases,
- Arrangements with brokers to facilitate the hedging of derivative and convertible arbitrage activities, and
- Litigation settlement agreements.

Due to the nature of these indemnification provisions, we cannot calculate our aggregate potential exposure under them.

We enter into certain types of agreements, including leases, assignments of leases, and subleases, in which we agree to indemnify third parties for acts by our agents, assignees and/or sublessees, and employees. While we do not believe these indemnification liabilities are material, either individually or in total, we cannot calculate our potential exposure.

We enter into contracts for the delivery of technology service in which we indemnify the other party against claims of patent and copyright infringement by third parties. Due to the nature of these indemnification provisions, we cannot calculate our aggregate potential exposure under this type of indemnification.

We engage in certain insurance activities which require our employees to be bonded. We satisfy this bonding requirement by issuing letters of credit in a total amount of approximately $5 million.

In the ordinary course of business, we enter into contracts with third parties under which the third parties provide services on behalf of PNC. In many of these contracts, we agree to indemnify the third party service provider under certain circumstances. The terms of the indemnity vary from contract to contract and the amount of the indemnification liability, if any, cannot be determined.

We are a general or limited partner in certain asset management and investment limited partnerships, many of which contain indemnification provisions that would require us to make payments in excess of our remaining funding commitments. While in certain of these partnerships the maximum liability to us is limited to the sum of our unfunded commitments and partnership distributions received by us, in the others the indemnification liability is unlimited. As a result, we cannot determine our aggregate potential exposure for these indemnifications.

Pursuant to their bylaws, PNC and its subsidiaries provide indemnification to directors, officers and, in some cases, employees and agents against certain liabilities incurred as a result of their service on behalf of or at the request of PNC and its subsidiaries. PNC and its subsidiaries also advance on behalf of covered individuals costs incurred in connection with certain claims or proceedings, subject to written undertakings by each such individual to repay all amounts so advanced if it is ultimately determined that the individual is not entitled to indemnification. We generally are responsible for similar indemnifications and advancement obligations that companies we acquire, including Riggs, had to their officers, directors and sometimes employees and agents at the time of acquisition. We advanced such costs on behalf of several such individuals (including some from Riggs) with respect to pending litigation or investigations during 2006. It is not possible for us to determine the aggregate potential exposure resulting from the obligation to provide this indemnity or to advance such costs.

In connection with the lending of securities held by PFPC as an intermediary on behalf of certain of its clients, we provide indemnification to those clients against the failure of the borrowers to return the securities. The market value of the securities lent is fully secured on a daily basis; therefore, the exposure to us is limited to temporary shortfalls in the collateral as a result of short-term fluctuations in trading prices of the loaned securities. At December 31, 2006, the total maximum potential exposure as a result of these indemnity obligations was approximately $13.0 billion, although we held collateral at the time in excess of that amount.

Other Guarantees

We write caps and floors for customers, risk management and proprietary trading purposes. At December 31, 2006, the fair value of the written caps and floors liability on our Consolidated Balance Sheet was $53 million. Our ultimate obligation under written options is based on future market conditions and is only quantifiable at settlement. We manage our market risk exposure from customer positions through transactions with third-party dealers.

We also enter into credit default swaps under which we buy loss protection from or sell loss protection to a counterparty for the occurrence of a credit event of a reference entity. The fair value of the contracts sold on our Consolidated Balance Sheet was a net asset of $4 million at December 31, 2006. The maximum amount we would be required to pay under the credit default swaps in which we sold protection, assuming all reference obligations experience a credit event at a total loss, without recoveries, was $933 million at December 31, 2006. We purchased $827 million notional of credit default swaps to mitigate the exposure of certain written credit default swaps at December 31, 2006.

We have entered into various contingent performance guarantees through credit risk participation arrangements with terms ranging from less than one year to 11 years. We will be required to make payments under these guarantees if a customer defaults on its obligation to perform under certain credit agreements with third parties. Our exposure under these agreements is approximately $372 million at December 31, 2006.

Contingent Payments In Connection With Certain Acquisitions

A number of the acquisition agreements to which we are a party and under which we have purchased various types of assets, including the purchase of entire businesses, partial interests in companies, or other types of assets, require us to make additional payments in future years if certain

predetermined goals are achieved or not achieved within a specific time period. Due to the nature of the contract provisions, we cannot quantify our total exposure that may result from these agreements.

Note 25 Parent Company

Summarized financial information of the parent company is as follows:

Income Statement

Year ended December 31 - in millions	**2006**	2005	2004
Operating Revenue			
Dividends from:			
Bank subsidiaries and bank holding company	**$710**	$717	$895
Non-bank subsidiaries	**69**	72	187
Interest income	**16**	8	4
Noninterest income	**9**	6	
Total operating revenue	**804**	803	1,086
Operating Expense			
Interest expense	**93**	71	42
Other expense	**46**	11	5

Total operating expense	**139**	82	47
Income before income taxes and equity in undistributed net income of subsidiaries	**665**	721	1,039
Income tax benefits	**(60)**	(24)	(17)
Income before equity in undistributed net income of subsidiaries	**725**	745	1,056
Equity in undistributed net income of subsidiaries:			
Bank subsidiaries and bank holding company	**1,653**	396	98
Non-bank subsidiaries	**217**	184	43
Net income	**$2,595**	$1,325	$1,197

Balance Sheet

December 31 - in millions	**2006**	2005
Assets		
Cash and due from banks	**$2**	$3
Short-term investments with subsidiary bank	**3**	
Securities available for sale	**290**	293
Investments in:		
Bank subsidiaries and bank holding company	**9,294**	7,140
Non-bank subsidiaries	**2,038**	2,504
Other assets	**559**	237
Total assets	**$12,186**	$10,177
Liabilities		
Subordinated debt	**$1,147**	$1,326
Accrued expenses and other liabilities	**251**	288
Total liabilities	**1,398**	1,614
Shareholders Equity	**10,788**	8,563
Total liabilities and shareholders equity	**$12,186**	$10,177

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Commercial paper and all other debt issued by PNC Funding Corp, a wholly owned finance subsidiary, is fully and unconditionally guaranteed by the parent company. In addition, in connection with certain affiliates commercial mortgage servicing operations, the parent company has committed to maintain such affiliates net worth above minimum requirements.

The parent company received net income tax refunds of $35 million in 2006 and $19 million in 2005. Such refunds represent the parent company s portion of consolidated income taxes. The parent company made income tax payments of $9 million in 2004. The parent company paid interest of $113 million in 2006, $94 million in 2005 and $62 million in 2004.

Statement Of Cash Flows

Year ended December 31 - in millions	**2006**	2005	2004
Operating Activities			
Net income	**$2,595**	$1,325	$1,197