BANK OF NEW YORK CO INC
Form 10-K
March 01, 2006
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THE BANK OF NEW YORK COMPANY, INC.

FINANCIAL REVIEW

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S ELECTED FINANCIAL DATA

(Dollars in millions, except per share amounts)	2005	2004	2003*	2002	2001**
Revenue (tax equivalent basis)	$ 8,341	$ 7,133	$ 6,361	$ 5,789	$ 7,241
Net Interest Income	1,909	1,645	1,609	1,665	1,681
Noninterest Income	4,956	4,650	3,996	3,133	3,561
Provision for Credit Losses	15	15	155	685	375
Noninterest Expense	4,483	4,122	3,698	2,751	2,819
Net Income	1,571	1,440	1,157	902	1,343
Net Income Available to Common Shareholders	1,571	1,440	1,157	902	1,343
Return on Average Assets	1.55%	1.45%	1.27%	1.13%	1.64%
Return on Average Common Shareholders Equity	16.59	16.37	15.12	13.96	21.58
Common Dividend Payout Ratio	41.00	42.22	48.83	60.78	39.21
Efficiency Ratio	65.7	66.0	66.0	55.4	55.2
Per Common Share					
Basic Earnings	$ 2.05	$ 1.87	$ 1.54	$ 1.25	$ 1.84
Diluted Earnings	2.03	1.85	1.52	1.24	1.81
Cash Dividends Paid	0.82	0.79	0.76	0.76	0.72
Market Value at Year-End	31.85	33.42	33.12	23.96	40.80
Averages					
Securities	$ 28,751	$ 25,046	$ 24,455	$ 22,970	$ 18,559
Loans	39,682	37,778	35,623	34,305	38,770
Total Assets	101,435	99,340	91,467	79,830	81,700
Deposits	62,215	61,056	58,615	53,795	56,278
Long-Term Debt	7,312	6,152	6,103	5,338	4,609
Common Shareholders Equity	9,473	8,797	7,654	6,465	6,224
At Year-End					
Allowance for Loan Losses as a Percent of Total Loans	1.01%	1.65%	1.89%	2.09%	1.16%
Allowance for Loan Losses as a Percent of Non-Margin Loans	1.19	1.99	2.26	2.12	1.18
Allowance for Credit Losses as a Percent of Total Loans	1.39	2.06	2.28	2.65	1.72
Allowance for Credit Losses as a Percent of Non-Margin Loans	1.63	2.48	2.72	2.68	1.75
Tier 1 Capital Ratio	8.38	8.31	7.44	7.58	8.11
Total Capital Ratio	12.48	12.21	11.49	11.96	11.57
Leverage Ratio	6.60	6.41	5.82	6.48	6.70
Common Equity to Assets Ratio	9.67	9.83	9.12	8.60	7.80
Total Equity to Assets Ratio	9.67	9.83	9.12	8.60	7.80
Common Shares Outstanding (In millions)	771.129	778.121	775.192	725.971	729.500
Employees	23,451	23,363	22,901	19,437	19,181
Assets Under Custody (In trillions) Estimated					
Total Assets Under Custody	$ 10.9	$ 9.7	$ 8.3	$ 6.8	$ 6.9
Equity Securities	32%	35%	34%	26%	36%
Fixed Income Securities	68	65	66	74	64
Cross-border Assets Under Custody	$ 3.4	$ 2.7	$ 2.3	$ 1.9	$ 1.9
Assets Under Management (In billions) Estimated					
Total Assets Under Management	$ 155	$ 137	$ 112	$ 80	$ 72
Asset Management Sector	69%	75%	79%	95%	93%
Equity Securities	24%	27%	27%	27%	33%
Fixed Income Securities	14	16	17	24	18
Alternative Investments	10	11	8	8	7
Liquid Assets	21	21	27	36	35
Foreign Exchange Overlay	6	6	5	5	7
Securities Lending Short-term Investment Funds	25	19	16		

* The 2003 results reflect $96 million of merger and integration costs associated with the Pershing acquisition as well as a $78 million expense related to the settlement of a claim by General Motors Acceptance Corporation (GMAC) related to the 1999 sale of BNY Financial Corporation (BNYFC).

** The 2001 results reflect the estimated $242 million impact of the World Trade Center disaster, the related $175 million initial insurance recovery, and the $190 million special provision on the accelerated disposition of emerging telecommunications loans.

All amounts in the above notes are pre-tax.

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M ANAGEMENT S DISCUSSION AND ANALYSIS OF THE COMPANY S FINANCIAL CONDITION AND RESULTS OF OPERATIONS (MD&A)

INTRODUCTION

The Bank of New York Company, Inc. s (the Company) actual results of future operations may differ from those estimated or anticipated in certain forward-looking statements contained herein for reasons which are discussed below and under the heading Forward Looking Statements and Risk Factors That Could Affect Future Results. When used in this report, the words estimate, forecast, project, anticipate, expect, inte believe, plan, goal, should, may, strategy, target, and words of similar meaning are intended to identify forward looking statements in statements specifically identified as forward looking statements.

OVERVIEW

The Company s Businesses

The Bank of New York Company, Inc. (NYSE: BK) is a global leader in providing a comprehensive array of services that enable institutions and individuals to move and manage their financial assets in more than 100 markets worldwide. The Company has a long tradition of collaborating with clients to deliver innovative solutions through its core competencies: securities servicing, treasury management, investment management, and individual & regional banking services. The Company s extensive global client base includes a broad range of leading financial institutions, corporations, government entities, endowments and foundations. Its principal subsidiary, The Bank of New York, founded in 1784, is the oldest bank in the United States and has consistently played a prominent role in the evolution of financial markets worldwide.

The Company s strategy over the past decade has been to focus on highly scalable, fee-based securities servicing and fiduciary businesses, and it has achieved top three market share in most of its major product lines. The Company distinguishes itself competitively by offering the broadest array of products and services around the investment lifecycle. These include:

- advisory and asset management services to support the investment decision;
- extensive trade execution, clearance and settlement capabilities;
- custody, securities lending, accounting, and administrative services for investment portfolios;
- sophisticated risk and performance measurement tools for analyzing portfolios; and
- services for issuers of both equity and debt securities.

By providing integrated solutions for clients needs, the Company strives to be the preferred partner in helping its clients succeed in the world s rapidly evolving financial markets.

The Company s key objectives include:

- achieving positive operating leverage on an annual basis and
- sustaining top-line growth by expanding client relationships and winning new ones

To achieve its key objectives, the Company has grown both through internal reinvestment as well as execution of strategic acquisitions to expand product offerings and increase market share in its scale businesses. Internal reinvestment occurs through increased technology spending, staffing levels, marketing/branding initiatives, quality programs, and product development. The Company consistently invests in technology to improve the breadth and quality of its product offerings, and to increase economies of scale. The Company has acquired over 90 businesses over the past ten years, almost exclusively in its securities servicing and asset management areas. The acquisition of Pershing in 2003 for $2 billion was the largest of these acquisitions.

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As part of the transformation to a leading securities servicing provider, the Company has also de-emphasized or exited several of its slower growth traditional banking businesses over the past decade. The Company s more significant actions include selling its credit card business in 1997 and its factoring business in 1999, and most recently, significantly reducing non-financial corporate credit exposures by 41% from December 31, 2001 to December 31, 2005. Capital generated by these actions has been reallocated to the Company s higher-growth businesses.

The Company s business model is well positioned to benefit from a number of long-term secular trends. These include:

- growth of worldwide financial assets,
- globalization of investment activity,
- structural market changes, and
- increased outsourcing.

These trends benefit the Company by driving higher levels of financial asset trading volume and other transactional activity, as well as higher asset price levels and growth in client assets, all factors by which the Company prices its services. In addition, international markets offer excellent growth opportunities.

Current Business Trends

In 2005 the operating environment was somewhat mixed relative to the Company s assumptions at the beginning of the year. The equity markets showed lower price appreciation and volumes than assumed. The fixed income markets remained strong and cross-border investment and trading activity increased. Volatility in foreign exchange markets was in line with expectations. The Federal Reserve raised rates more than the Company anticipated at the start of 2005. Given the Company s diversified business model, the Company achieved double-digit growth in many of its key business lines.

With respect to fee income growth, execution and clearing was lower than expected given the weaker equity markets, but the Company achieved solid growth in ADRs, corporate trust, and investor and broker-dealer services, which resulted in servicing fee growth of 10%.

Private client services and asset management, as well as foreign exchange and other trading, also had solid results. This offset weaker performance in the global payments business, corporate lending activities, and retail banking. Overall, core noninterest income growth for the year was 8%.

The Company has been positioned to benefit from rising interest rates, and with the Federal Reserve raising the federal funds rate from 2.25% at the start of the year to 4.25% at the end, core net interest income was up 11%. Strong liquidity generated from its core businesses, widening spreads on deposits, and sound asset positioning all contributed to this strong performance.

Expense control was effective as the Company s staff count increased over 2005 by just 1% to 23,451, well below the pace of revenue growth. This reflects the Company s continued progress on reengineering for labor efficiencies. The Company is also relocating staff to lower cost locations. Expense growth overall was up 9%, reflecting higher costs for pensions and options, construction of an out-of-region data center, and legal and regulatory costs. These factors should have a lesser impact on expense growth prospectively.

For 2006, the Company based its budget planning process on expectations of moderate economic growth and continued growth in the capital markets. The Company expects equity markets to strengthen slightly versus 2005 and rise 5-7%. U.S. non-program equity volumes are forecast to be up 4-6% with equity capital raising holding steady. Moderate growth in M&A volumes is expected. The Company assumes the federal funds rate

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will rise to 4.5% with only a slight steepening of the yield curve. GDP growth is expected to be slightly over 3%. The Company projects fixed income activity to be moderate, given the expectation of a leveling-off in short interest rates.

This presents an overall backdrop which is comparable to 2005, although with a somewhat different composition and a slightly less favorable environment for net interest income. In the aggregate, the Company expects to grow revenues faster than the markets by focusing on faster-growing market segments, gaining market share, and providing a high level of service to its existing clients.

Several other factors will have an impact on 2006 results, including:

- higher pension expense given relatively poor investment returns over the past four years and further changes in prospective assumptions partly offset by changes to the Company s primary domestic plan;
- higher costs related to completing relocation projects;
- an anticipated lower level of securities gains; and
- potentially higher credit loss provisioning given the very favorable credit costs in 2005.

After considering the above, the Company is targeting positive operating leverage of 100+ basis points in 2006. The Company will seek to control overall expense growth through continued cost discipline and reengineering efforts, without sacrificing the investments necessary both to innovate and to enhance service quality. The Company continues to focus on key programs to attain greater straight-through processing of transactions, to reengineer labor costs, and to move activity to lower cost locations.

In January 2006, a significant customer ended its clearing relationship with Pershing following its acquisition by a major broker-dealer. Pershing currently is in discussions seeking compensation for the termination of the relationship.

FINANCIAL HIGHLIGHTS

2005

In 2005, the Company reported net income of $1,571 million and diluted earnings per share of $2.03 compared with net income of $1,440 million and diluted earnings per share of $1.85 in 2004, and net income of $1,157 million and diluted earnings per share of $1.52 in 2003. Reported EPS reflects a reduction of 3 cents in 2004 due to items detailed in Other 2004 Developments .

Additional 2005 highlights include:

- Positive operating leverage on a core basis for the third and fourth quarters versus 2004;
- Securities servicing fees up 10% from 2004;
- Net interest income up 16% versus 2004;
- Private client services and asset management fees up 9%;

Foreign exchange and other trading revenues up 7% from 2004; and

Active capital management, as the Company repurchased 5 million net shares.

The Company s 2005 earnings reflect significant progress toward its key objectives. New business wins and revenues from new and innovative products drove double-digit revenue growth in many of the Company s key business lines. In 2005, the Company focused on generating positive operating leverage and began to deliver on that objective as well. A number of outstanding regulatory issues were resolved. The Company launched its branding initiative in January 2005 and continued to expand it throughout the year. Finally, the Company s earnings per share of $2.03 was in the midpoint of the guidance range the Company provided early in 2005.

During 2005, the Company formed strategic alliances to penetrate faster-growing markets in France, Germany, the Nordic and Baltic region, Japan, Australia, and India. The Company also continued to expand its market presence in high-growth areas such as hedge fund servicing and collateral management, while extending its capabilities in the rapidly growing area of alternative investments.

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The Company continued to improve its credit risk portfolio, and it funded further long-term investment spending for technology, business continuity, quality, and branding programs.

In 2005, the Company continued to invest in enhancing its service offerings, critical to sustaining top-line growth through all types of markets, while maintaining its commitment to expense discipline to ensure a competitive cost base. Service offerings enhancements were the result of both internal development and acquisitions.

The Company announced three strategic transactions:

- Lynch, Jones & Ryan, Inc. a market leader in commission recapture, the acquisition complements the Company s execution business. The acquisition brings in 1,400 pension fund clients, which offer cross-sell opportunities for the Company s transition management services.

- Alcentra an international asset management group focused on funds that invest in non-investment grade debt. The acquisition adds structured credit to the Company s asset management offering and $6 billion to assets under management.

- Urdang Capital Management a real estate investment firm that manages approximately $3.0 billion in direct investments and portfolios of REIT securities. Expected to close in the first quarter of 2006, the acquisition expands the Company s alternative investment platform by adding real estate investment management.

The acquisitions of Alcentra and Urdang bring asset classes that are in demand by core customer segments such as pension funds, endowments and foundations, international investors, and private clients. Going forward, the Company plans to continue building out its asset management capabilities and to capitalize on the Company s inherent distribution strengths, as well as favorable secular trends for growth in investable assets.

2004

In 2004, the Company reported net income of $1,440 million and diluted earnings per share of $1.85. In 2004, the Company recorded several gains and charges that in the aggregate reduced reported earnings by 3 cents per share. These items are detailed in Other 2004 Developments .

In 2004, the growth in earnings was paced by securities servicing growth of 18% (9% adjusted for full-year impact of Pershing) to $2,857 million, core net interest income growth of 6%, strong credit performance, and higher than expected securities gains. Performance was strong across nearly all the Company s securities servicing businesses. Investor and issuer services increased by 11% and 12%, respectively. The growth in investor services was driven largely by new business wins and improvements year-over-year in asset values and volumes. Issuer services benefited from increased cross-border activity in depositary receipts and improving market share in global products within corporate trust. Broker-dealer services were up 17% primarily due to strong growth in collateral management.

The Company s asset management business continued to perform well, responding to growing institutional investor interest in alternative investments. Private client services and asset management fees increased $64 million, or 17%, primarily due to exceptional growth at the Company s fund of funds manager, Ivy Asset Management (Ivy). In addition, foreign exchange results continued to benefit from currency volatility and increased cross-border investing. Foreign exchange and other trading revenues remained at historically high levels, up 11% versus a year ago. The provision for credit losses declined to $15 million from $155 million in 2003.

This strength in revenue was partially offset by upward pressure on the Company s expense base. Higher employee stock option and pension expenses, business continuity spending, costs associated with legal and regulatory matters, and costs associated with converting new business opportunities in investor services all contributed to higher expense levels.

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2003

In 2003, the Company reported net income was $1,157 million and diluted earnings per share of $1.52. Merger and integration costs associated with the Pershing acquisition of 8 cents per share and the settlement with General Motors Acceptance Corporation (GMAC) of 7 cents per share impacted earnings in 2003. In 2003, securities servicing fees were $2,412 million, a 27% increase compared with $1,896 million in 2002, reflecting the Pershing acquisition and growth in investor and broker-dealer services. Global payment services fees increased 6% for the full year, which is attributable to improved multi-currency funds transfer product capabilities and new business wins. For the year 2003, private client services and asset management fees were up 12% from the previous year, reflecting higher equity price levels as well as strong growth at Ivy. In addition, the year-over-year comparison also benefited from the full-year impact of several 2002 acquisitions. Foreign exchange and other trading revenues were up 40% over 2002, resulting from increased client-driven foreign exchange, interest rate hedging activity, and the Pershing acquisition. The provision for credit losses was $155 million. Although expenses increased significantly due to the Pershing acquisition, stock option expensing, a lower pension credit, technology investment, and business continuity, the Company was able to attain positive leverage in the second half of the year.

CONSOLIDATED INCOME STATEMENT REVIEW

Noninterest Income

				Percent Inc/(Dec)	
(In millions)	**2005**	**2004**	**2003**	**2005 vs. 2004**	**2004 vs. 2003**
Noninterest Income					
Servicing Fees					
Securities	$ 3,148	$ 2,857	$ 2,412	10%	18%
Global Payment Services	294	319	314	(8)	2
	3,442	3,176	2,726	8	17
Private Client Services and Asset Management Fees	490	448	384	9	17
Service Charges and Fees	382	384	375	(1)	2
Foreign Exchange and Other Trading Activities	391	364	327	7	11
Securities Gains/(Losses)	68	78	35	(13)	123
Other	183	200	149	(9)	34
Total Noninterest Income	$ 4,956	$ 4,650	$ 3,996	7	16

Noninterest income is provided by a wide range of securities servicing, global payment services, private client services and asset management, trading activities, and other fee-based services. Revenues from these activities were $4,956 million in 2005, compared with $4,650 million in 2004 and $3,996 million in 2003. As a percentage of revenues, total noninterest income was 72% in 2005, compared with 74% in 2004 and 71% in 2003. The growth in revenue in 2005 primarily reflects broadly stronger performance in securities servicing, private client services and asset management fees, and foreign exchange and other trading revenue.

The increase in 2004 primarily reflects strong performance across nearly all the Company s securities servicing businesses and the full-year impact of the Pershing acquisition, as well as higher foreign exchange and other trading revenue, private client services and asset management fees, and securities gains. The 2004 increase also includes the $48 million pre-tax gain on the sale of a portion of the Company s investment in Wing Hang Bank Limited and the $19 million gain on four sponsor fund investments recorded in 2004.

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The following table provides the breakdown of securities servicing fees for 2005, 2004, and 2003.

Securities Servicing Fees

(In millions)	2005	2004	2003	Percent Inc/(Dec) 2005 vs. 2004	Percent Inc/(Dec) 2004 vs. 2003
Execution and Clearing Services	$ 1,222	$ 1,145	$ 885	7%	29%
Investor Services	1,060	924	830	15	11
Issuer Services	639	583	522	10	12
Broker-Dealer Services	227	205	175	11	17
Securities Servicing Fees	$ 3,148	$ 2,857	$ 2,412	10	18

Securities servicing fees were $3,148 million, $2,857 million, and $2,412 million, in 2005, 2004, and 2003, respectively. The 10% increase in securities servicing fees from 2004 primarily reflects solid growth across all businesses. In 2004, the 18% increase in securities servicing fees from 2003 reflects the full-year impact of the Pershing acquisition and good organic growth in investor and issuer services, which were up 11% and 12%. For additional details on Securities Servicing Fees, refer to the Business Segment Review section.

Global payment services fees, principally funds transfer, cash management, and trade services, were $294 million in 2005, $319 million in 2004, and $314 million in 2003. The decline in global payment services fees in 2005 reflects customers choosing to pay with higher compensatory balances, which benefits net interest income. On an invoiced services basis total revenue was up 5% over 2004. The small 2004 increase in global payment services fees from 2003 is attributable to customers starting to leave higher compensatory balances to cover the cost of services rather than pay fees as a result of the rising rate environment.

Private client services and asset management fees were $490 million in 2005, $448 million in 2004, and $384 million in 2003. The 9% increase over 2004 reflects strong growth in asset management fees as well as higher fees in private banking. Asset management was driven by another strong performance at Ivy and double-digit growth in fixed income asset management and separate account services. The 17% increase in fees in 2004 from 2003 reflects strong growth in Ivy, higher fees from fixed income asset management, and higher equity price levels.

Service charges and fees were $382 million in 2005, compared with $384 million in 2004 and $375 million in 2003. The decrease in 2005 from 2004 reflects lower retail checking account fees. The increase in 2004 from 2003 reflects higher syndication and advisory fees.

Foreign exchange and other trading revenues were a record $391 million in 2005, $364 million in 2004, and $327 million in 2003. Foreign exchange trading grew strongly in 2005 reflecting increased volume due to new business wins and greater business from existing clients. Other trading grew in 2005 reflecting higher interest rate and equity derivatives trading partially offset by a decline in trading revenue at Pershing. The 11% increase in 2004 from 2003 resulted from new business wins and an increased level of client activity, tied to cross-border investing and hedging against currency volatility. Pershing contributed $44 million to foreign exchange and other trading revenue in 2005, compared with $51 million in 2004 and $35 million in 2003.

Securities gains were $68 million in 2005, compared with a $78 million in 2004 and a $35 million in 2003. The securities gains in 2005 and 2004 were primarily attributable to the Company s private equity portfolio. In 2004, the Company s private equity portfolio generated $19 million of realized gains on four sponsor investments. Half of the 2003 gains arose from repositioning actions in the Company s fixed income securities portfolio.

Other noninterest income is attributable to asset-related gains, equity investments, and other transactions. Asset-related gains include gains on lease residuals, as well as loan and real estate dispositions. Equity investment income primarily reflects the Company s proportionate share of the income from its investment in

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Wing Hang Bank Limited, AIB/BNY Securities Services (Ireland) Limited, and RBSI Securities Services (Holdings) Limited. Other income primarily includes income or loss from insurance contracts, low income housing and other investments as well as various miscellaneous revenues. The breakdown among these three categories is shown below:

Other Noninterest Income

(In millions)	2005	2004	2003
Asset-Related Gains	$ 97	$ 82	$ 36
Equity Investment Income	44	43	34
Other	42	75	79
Total Other Noninterest Income	$ 183	$ 200	$ 149

Other noninterest income was $183 million in 2005, $200 million in 2004, and $149 million in 2003. In 2005, asset-related gains included a $17 million gain on the sale of the Company s interest in Financial Models Companies, Inc. (FMC), a $12 million gain on the sale of certain Community Reinvestment Act (CRA) investments, a $12 million gain on sale of eight New York Stock Exchange seats, and a $10 million gain on the sale of a building. The increase in asset-related gains in 2004 from 2003 reflected a pre-tax gain of $48 million from the sale of a portion of the Company s investment in Wing Hang Bank Limited. The higher level of asset-related gains in 2005 and 2004 has helped to offset higher legal and regulatory costs and the impact of the 2004 SFAS 13 lease income adjustment. The 2005 decline in other in the above table reflects fewer government grants and lower insurance-related income.

Net Interest Income

					Percent Inc/(Dec)	
	2005	2004		2003	2005 vs. 2004	2004 vs. 2003
(Dollars in millions)	Reported	Reported	Core*	Reported	Reported	Reported
Net Interest Income	$ 1,909	$ 1,645	$ 1,711	$ 1,609	16%	2%
Tax Equivalent Adjustment	29	30	30	35		
Net Interest Income on a Tax Equivalent Basis	$ 1,938	$ 1,675	$ 1,741	$ 1,644	16%	2%
Net Interest Rate Spread	1.83%	1.78%	1.86%	1.97%		
Net Yield on Interest Earning Assets	2.36	2.07	2.15	2.22		

* Excludes SFAS 13 adjustments

For 2005, net interest income on a tax equivalent basis amounted to $1,938 million compared with $1,675 million in 2004. In 2005, the increase in net interest income reflects the Company s sound interest rate positioning for a rising rate environment, continued expansion of deposit spreads, and increased liquidity generated by servicing activities. The Company also benefited from customers greater use of compensating balances in a rising rate environment. On a reported basis, net interest income on a tax equivalent basis was up 16% while on a core basis it was up 11%.

Net interest income in 2004 was affected by three cumulative adjustments to the leasing portfolio, which were triggered under SFAS 13. See Other 2004 Developments .

Excluding the impact of the SFAS 13 leasing adjustments on the leveraged lease portfolio, net interest income on a tax equivalent basis was $1,741 million in 2004, up 6% from $1,644 million in 2003. This increase was attributable to the full-year impact of Pershing and the benefit of rising interest rates. Rising rates reduced compression on deposit product spreads, increased the value of free funds and caused the Company s global payment services customers to leave additional compensatory balances rather than pay for services with fees.

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The increase in net interest income in 2005 and 2004 also reflects an increase in average earning assets. Average earning assets were $82.1 billion in 2005 compared with $81.1 billion in 2004 and $74.1 billion in 2003. The increase in 2004 from 2003 reflects the inclusion of Pershing for the full year 2004. Average loans were $39.7 billion in 2005 compared with $37.8 billion in 2004 and $35.6 billion in 2003. Average securities were $28.8 billion in 2005, up from $25.0 billion in 2004 and $24.5 billion in 2003.

The net interest rate spread was 1.83% in 2005 compared with 1.78% in 2004, while the net yield on interest-earning assets was 2.36% in 2005 and 2.07% in 2004. Excluding the leasing adjustments of $66 million in 2004, the net interest rate spread was 1.86% and the net yield was 2.15%. The Company estimates that if Pershing had been owned for the full-year of 2003, the spread and yield in 2003 would have been reduced to 1.89% and 2.13%, respectively.

In this report a number of amounts related to net interest income are presented on a tax equivalent basis. The Company believes that this presentation provides comparability of net interest income arising from both taxable and tax-exempt sources and is consistent with industry practice.

Provision for Credit Losses

The provision for credit losses was $15 million in 2005, compared with $15 million in 2004 and $155 million in 2003. Asset quality remained high in 2005. The 2004 provision includes a credit of $7 million for the reduction in exposure associated with the restructuring of aircraft leases. The lower provision in 2004 from 2003 reflects the Company s improved asset quality and a stronger credit environment.

Noninterest Expense

				Percent Inc/(Dec)	
(In millions)	**2005**	**2004**	**2003**	**2005 vs. 2004**	**2004 vs. 2003**
Salaries and Employee Benefits	$ 2,549	$ 2,324	$ 2,002	10%	16%
Net Occupancy	323	305	261	6	17
Furniture and Equipment	208	204	185	2	10
Clearing	187	176	154	6	14
Sub-custodian Expenses	96	87	74	10	18
Software	215	193	170	11	14
Communications	95	93	92	2	1
Amortization of Intangibles	40	34	25	18	36
Pershing Merger and Acquisition Costs			96		
Other	770	706	639	9	10
Total Noninterest Expense	$ 4,483	$ 4,122	$ 3,698	9%	11%

Total noninterest expense was $4,483 million in 2005, $4,122 million in 2004, and $3,698 million in 2003. The 2005 increase in expenses primarily reflects increased staffing and clearing costs associated with new business and acquisitions, higher stock option and pension expense, expanded occupancy costs associated with business continuity, as well as higher technology and legal costs. The 2004 increase in expenses primarily reflects the full-year impact of the Pershing acquisition, higher stock option expense, a lower pension credit, the upfront expenses associated with the implementation of cost reduction initiatives, higher volume related sub-custodian and clearing expenses and higher technology and business continuity spending. In 2003, noninterest expense included merger and acquisition costs relating to Pershing of $96 million and the settlement with GMAC of $78 million.

Salaries and employee benefits were $2,549 million in 2005, compared with $2,324 million in 2004 and $2,002 million in 2003. In 2005, salaries rose 7% as tight headcount control and reengineering and relocation projects partially offset the impact of business wins, acquisitions and additional legal and compliance personnel. Benefit expense rose significantly in 2005 reflecting higher expenses for pensions, stock options, medical benefits, and incentive payments. In 2004, the increase in salaries and employee benefits reflects higher performance related incentives and benefits, higher stock option and defined contribution plan expense, a higher pension expense as well as higher variable expenses associated with revenue growth. The number of employees at December 31, 2005, was 23,451, up from 23,363 and 22,901 in 2004 and 2003, respectively. Severance expense was $17 million in 2005, $16 million in 2004 and $10 million in 2003.

Net occupancy and furniture and fixture expenses were $531 million in 2005, compared with $509 million in 2004 and $446 million in 2003. Net occupancy increased by $18 million, primarily reflecting the costs associated with the Company s new out-of-region data center in the mid-south region of the U.S. and the growth center in Manchester, England, as well as higher energy costs.

Clearing expenses were $187 million in 2005, compared with $176 million in 2004 and $154 million in 2003. The increase in 2005 reflects higher expenses associated with acquisitions within the execution business. Sub-custodian expenses increased 10% in 2005 to $96 million, reflecting higher level of business activity.

Software expenses increased in 2005 and 2004, reflecting the Company s continued investment in technology capabilities supporting its servicing activities as well as spending and development to support business growth.

Amortization of intangibles increased to $40 million in 2005 from $34 million in 2004 and $25 million in 2003. In 2005 and 2004, the Pershing acquisition added $20 million in intangibles amortization.

Other noninterest expense is attributable to vendor services, business development, legal expenses, settlements and claims, other, and the GMAC settlement. Vendor services include professional fees, computer services, market data, courier, and other services. Business development includes advertising, charitable contributions, travel, and entertainment expenses. The breakdown among these five categories is shown below:

Other Noninterest Expense

(In millions)	**2005**	**2004**	**2003**
Vendor Services	$ 336	$ 307	$ 259
Business Development	124	108	84
Legal Fees, Settlements and Claims	125	96	43
Other	185	195	175
GMAC Settlement			78
Total Other Noninterest Expense	$ 770	$ 706	$ 639

Other expenses in 2005 were $770 million, compared with $706 million in 2004 and $639 million in 2003. Since the Company owned Pershing for 8 months in 2003, $67 million of the 2004 increase relates to the full- year impact of owning Pershing. The increase in vendor services in 2005 primarily reflects higher consulting and pricing services expenses. Growth in business development expenses over the period reflects higher travel and entertainment and advertising related to the Company s branding initiatives. Legal fees, settlement and claims in 2005 included $24 million associated with the Russian Funds transfer matter and other regulatory matters, as well as an increase in legal fees. In 2004, noninterest expense included expenses associated with the RW Matter of $30 million.

In 2003, the Company and GMAC settled claims relating to the Company s 1999 sale to GMAC of BNY Financial Corporation, the Company s factoring and asset-based finance business. The settlement resolved all claims between the parties with a payment of $110 million by the Company to GMAC. After accounting for a

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previously established reserve for this matter, the net impact of the settlement was approximately $78 million, or 7 cents per fully diluted share. The Company sold BNY Financial Corporation to GMAC for $1.8 billion in cash in 1999.

The Company continues to increase its investment in technology focusing on key items such as delivering positive operating leverage, driving product innovation and enhancing the client experience. Software development has been an increasing component of technology expense in 2005, 2004, and 2003. The rate of infrastructure investment is slowing. Approximately 80% of the data center capacity is two years old or less. In the fourth quarter of 2005, the Company s new data center in the mid-south region of the U.S. became operational. The new data center will improve the geographic diversification and resilience of the Company s operations and will support the processing needs of the Company s institutional and retail customers. In 2006, the Company expects to benefit from the new data center as redundant locations are beginning to be shut down. Print center consolidation was completed in 2005. Core investor services applications were recently developed and engineered with technologies that should be durable over time.

The Company has a number of programs to control expense growth. These programs include day-to-day profitability programs, reengineering processes, and moving jobs to lower cost environs. Day-to-day profitability programs focus on stringent control of headcount and discretionary expenses, as well as enhanced vendor management.

Reengineering focuses on business process reviews throughout the Company. Projects commenced in 2005 are expected to have a $40 million impact in 2006. In 2004, the Company reviewed 15 areas and developed action steps to lower expenses by $90 million, with a $40 million impact in 2004 and a $50 million incremental for 2005. These savings have lowered the Company s growth rate of expenses by approximately 1% over the past two years. The savings are partly offset by consulting costs.

In January 2004, the Company began a three-year effort to move 1,500 jobs to lower cost areas. In 2005, the Company moved 516 positions out of higher-cost locations, up from 419 moves in 2004. In 2006, the Company anticipates further expansion of the job relocation program to 1,800 jobs given the success of the program to date. As a result, the Company will incur higher expense in 2006 for severance and lease termination, but will achieve net benefits in 2007 and 2008.

The Company adopted fair value accounting for stock compensation on January 1, 2003, using the prospective method. The Company s grants of stock options typically vest over two to four years. The year 2005 was the third and final year the adoption of expensing stock options impacted year-over-year expense comparisons. The Company expects stock options expense to be somewhat less expensive in 2006 since the Company is issuing fewer options than it has in the past.

Income Taxes

The Company s consolidated effective tax rates for 2005, 2004, and 2003 were 33.6%, 33.3%, and 34.0%, respectively. The increase in the effective tax rate in 2005 primarily reflects higher state and local taxes. The decline in the effective tax rate in 2004 from 2003 primarily reflects the increase in the tax reserve related to LILO exposures which was offset by the SFAS 13 leasing adjustments. The Company anticipates the tax rate for the year 2006 to increase slightly to 33.7%.

The Company invests in synthetic fuel (Section 29) and low income housing (Section 42) investments generating tax credits, which have the effect of permanently reducing the Company s tax expense. The effective tax rates in all periods reflect a reclassification related to Section 42 tax credits. See Accounting Changes and New Accounting Pronouncements in the Notes to Consolidated Financial Statements. The Company also invests in leveraged leases which, through accelerated depreciation, postpone the payment of taxes to future years. For financial statement purposes, deferred taxes are recorded as a liability for future payment.

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BUSINESS SEGMENT REVIEW

Segment Data

The Company has an internal information system that produces performance data for its four business segments along product and service lines.

Business Segments Accounting Principles

The Company s segment data has been determined on an internal management basis of accounting, rather than the generally accepted accounting principles used for consolidated financial reporting. These measurement principles are designed so that reported results of the segments will track their economic performance. Segment results are subject to restatement whenever improvements are made in the measurement principles or when organizational changes are made.

In 2005, the Company has determined that it is appropriate to modify its segment presentation in order to provide more transparency into its results of operations and to better reflect modifications in the management structure that the Company implemented during the fourth quarter of 2005. As such, the Company has identified four major business segments for assessing its overall performance, with the Institutional Services segment being further subdivided into four business groupings. These segments are shown below:

- Institutional Services Segment
  - Investor & Broker-Dealer Services Business
  - Execution & Clearing Services Business
  - Issuer Services Business
  - Treasury Services Business
- Private Bank & BNY Asset Management Segment
- Retail & Middle Market Banking Segment
- Corporate and Other Segment

All prior periods have been restated to reflect this realignment. Other specific accounting principles employed include:

- The measure of revenues and profit or loss by a segment has been adjusted to present segment data on a tax equivalent basis.
- The provision for credit losses allocated to each segment is based on management s judgment as to average credit losses that will be incurred in the operations of the segment over a credit cycle of a period of years. Management s judgment includes the following factors among others: historical charge-off experience and the volume, composition, and size of the credit portfolio. This method is

different from that required under generally accepted accounting principles as it anticipates future losses which are not yet probable and therefore not recognizable under generally accepted accounting principles.

Balance sheet assets and liabilities and their related income or expense are specifically assigned to each segment.

Net interest income is allocated to segments based on the yields on the assets and liabilities generated by each segment. Assets and liabilities generated by credit-related activities are allocated to businesses based on borrower usage of that businesses products or services. Credit-only relationships and borrowers using both credit and payment services remain in Treasury Services. Segments with a net liability position are allocated assets primarily from the securities portfolio.

Noninterest income associated with Treasury-related services is similarly allocated back to those businesses.

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Revenues and expenses associated with specific client bases are included in those segments. For example, foreign exchange activity associated with clients using custody products is allocated to Investor & Broker-Dealer Services.

Support and other indirect expenses are allocated to segments based on internally-developed methodologies.

Description of Business Segments

The activities within each business segment are described below.

Institutional Services Segment

Investor & Broker-Dealer Services Business

Investor & Broker-Dealer Services includes global custody, global fund services, securities lending, global liquidity services, outsourcing, government securities clearance, collateral management, credit-related services, and other linked revenues, principally foreign exchange and execution and clearing revenues.

In Investor Services, the Company is one of the leading custodians with $10.9 trillion of assets under custody at December 31, 2005. The Company is one of the largest mutual fund custodians for U.S. funds and one of the largest providers of fund services in the world with over $1.6 trillion in total assets. The Company, also services more than 17% of the total industry assets for exchange-traded funds, and is a leading U.K. custodian. In securities lending, the Company is the largest lender of U.S. Treasury securities and depositary receipts with a lending pool of approximately $1.5 trillion in 27 markets around the world.

The Company s Broker-Dealer Services business clears approximately 50% of U.S. Government securities. The Company is the leader in global clearance, clearing equity and fixed income transactions in 101 markets. With over $1.1 trillion in tri-party balances worldwide, the Company is the world s largest collateral management agent.

Execution & Clearing Services Business

The Company provides execution, clearing and financial services outsourcing solutions in over 80 global markets, executing trades for 575 million shares and clearing 930,000 trades daily. In Execution Services, the Company conducts institutional agency brokerage, electronic trading, transition management services, and independent research. The Company s Execution Services business is one of the largest global institutional agency brokerage organizations. In addition, it is one of the leading institutional electronic brokers for non-U.S. dollar equity execution.

Pershing s clearing business provides clearing, execution, financing, and custody for introducing broker-dealers and registered investment advisors. Pershing services more than 1,100 institutional and retail financial organizations and independent investment advisors who collectively represent nearly 6 million individual investors.

Issuer Services Business

Issuer Services includes corporate trust, depositary receipts, employee investment plan services, stock transfer, and credit-related services.

In Issuer Services, the Company is depositary for more than 1,200 American and global depositary receipt programs, a 64% market share, acting in partnership with leading companies from 60 countries. As a trustee, the

Company provides diverse services for corporate, municipal, structured, and international debt securities. Over 90,000 appointments for more than 30,000 worldwide clients have resulted in the Company being trustee for more than $3 trillion in outstanding debt securities. The Company is the third largest stock transfer agent, servicing more than 16 million shareowners. Employee Investment Plan Services has more than 124 clients with 650,000 employees in over 54 countries.

Treasury Services Business

Treasury Services includes global payment services for corporate customers as well as lending and credit-related services.

Corporate global payment services offers leading-edge technology, innovative products, and industry expertise to help its clients optimize cash flow, manage liquidity, and make payments around the world in more than 90 different countries. The Company maintains a global network of branches, representative offices and correspondent banks to provide comprehensive payment services including funds transfer, cash management, trade services and liquidity management. The Company is one of the largest funds transfer banks in the U.S. transferring over $1.18 trillion daily via more than 135,500 wire transfers.

The Company provides lending and credit-related services to large public and private corporations nationwide. Special industry groups focus on industry segments such as media, telecommunications, cable, energy, real estate, retailing, and healthcare. Credit-related revenues are allocated to businesses other than Treasury Services to the extent the borrower uses that businesses products or services. Credit-only relationships and borrowers using both credit and payment services remain in Treasury Services. Through BNY Capital Markets, Inc., the Company provides a broad range of capital markets and investment banking services including syndicated loans, bond underwriting, private placements of corporate debt and equity securities, and merger, acquisition, and advisory services. The Company is a leading arranger of syndicated financings for clients with 151 transactions totaling in excess of $59 billion in 2005.

For its credit services business overall, the Company s corporate lending strategy is to focus on those clients and industries that are major users of securities servicing and global payment services.

Private Bank and BNY Asset Management

The Private Bank & BNY Asset Management segment includes traditional banking and trust services to wealthy clients and investment management services for institutional and high-net-worth clients. In private banking, the Company offers a full array of wealth management services to help individuals plan, invest and transition and includes financial and estate planning, trust and fiduciary services, customized banking services, brokerage and investment solutions.

BNY Asset Management provides investment solutions for some of the wealthiest individuals, largest corporate and most prestigious organizations around the world applying a broad spectrum of investment strategies and wealth management solutions. BNY Asset Management s alternative strategies have expanded to include hedge fund of funds, private equity, alternative fixed income and real estate.

The Company s asset management subsidiaries include:

Ivy Asset Management Corporation, one of the country s leading hedge fund of fund firms, offers a comprehensive range of multi-manager hedge fund products and customized portfolio solutions.

Alcentra Group, acquired in January 2006, offers sophisticated alternative credit investments, including leveraged loans and subordinated and distressed debt.

Urdang Capital, a real estate investment firm, which the Company has agreed to acquire, offers the opportunity to invest in real estate through separate accounts, a closed-end commingled fund that invests directly in properties, and a separate account that invests in publicly-traded REITs.

Estabrook Capital Management LLC offers value-oriented investment management strategies, including socially responsible investing.

Gannett Welsh & Kotler specializes in tax-exempt management and equity portfolio strategies.

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The Company also provides investment management services directly to institutions and manages the Hamilton family of mutual funds.

Retail & Middle Market Banking Segment

The Retail Bank includes branch banking, consumer, small business, residential mortgage and asset management activities conducted through the Company s investment centers. The Company s retail franchise includes more than 600,000 consumer relationships and 100,000 business relationships. The Company operates 342 branches in 23 counties in the New York tri-state region. The Company has 241 branches in New York, 93 in New Jersey and 8 in Connecticut. The New York branches are primarily suburban-based with 118 in upstate New York, 85 on Long Island and 38 in New York City. The retail network is a significant source of low-cost funding and provides a platform to cross-sell core services to both individuals and small businesses in the New York metropolitan area. The branches are a meaningful source of private client referrals. Small business and investment centers are set up in the largest 100 branches.

Investment centers provide personalized professional investment counseling to individuals. Products include mutual funds, annuities, and discount brokerage services.

In middle market lending, the Company s regional commercial banking and regional commercial real estate divisions provide financing for a variety of businesses based in the New York metropolitan area. The types of financing include lines of credit, term loans, global trade services, and commercial mortgages.

Corporate and Other Segment

The Corporate and Other segment primarily includes the Company s leasing operations and corporate overhead. Net interest income in this segment primarily reflects the funding cost of goodwill and intangibles. The tax equivalent adjustment on net interest income is eliminated in this segment. Provision for credit losses reflects the difference between the aggregate of the credit provision over a credit cycle for the other three reportable segments and the Company s recorded provision. The Company s approach to acquisitions is highly centralized and controlled by senior management. Accordingly, the resulting goodwill and other intangible assets are included in this segment for average assets. Noninterest expense includes the related amortization. Noninterest income primarily reflects leasing, securities gains, and income from the sale of other corporate assets. Noninterest expenses include direct expenses supporting the leasing activities as well as certain corporate overhead not directly attributable to the operations of the other segments.

Business Review

Institutional Services Segment

				Inc/(Dec)	
(In millions)	**2005**	**2004**	**2003**	**2005 vs. 2004**	**2004 vs. 2003**
Net Interest Income	$ 1,186	$ 1,064	$ 971	$ 122	$ 93
Noninterest Income	4,182	3,830	3,337	352	493
Total Revenue	5,368	4,894	4,308	474	586
Provision for Credit Losses	59	59	101		(42)
Noninterest Expense	3,444	3,140	2,691	304	449
Income Before Taxes	1,865	1,695	1,516	170	179
Average Assets	75,682	72,286	63,952	3,396	8,334
Average Deposits	44,833	42,533	40,683	2,300	1,850

The Company s Institutional Services business is conducted in four business groupings: Investor & Broker-Dealer Services, Execution & Clearing Services, Issuer Services, and Treasury Services. Income before taxes was up 10% to $1,865 million in 2005 from $1,695 million in 2004, which was up 12% versus $1,516 million in 2003.

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Market Data

	2005	2004	2003	Percent Inc/(Dec) 2005 vs. 2004	2004 vs. 2003
S&P 500® Index	1,248	1,212	1,112	3%	9%
NASDAQ® Index	2,205	2,175	2,003	1	9
Lehman Brothers					
Aggregate Bond[sm] Index	206.2	220.6	193.4	(7)	14
MSCI® EAFE	1,680.1	1,515.5	1,288.8	11	18
NYSE Volume (In billions)	403.8	367.1	352.4	10	4
NASDAQ® Volume (In billions)	449.2	453.9	424.6	(1)	7

The S&P 500® Index was up 3% for the year, with average daily price levels up 7% from 2004. Performance for the NASDAQ® Index was up 1% for the year, with average daily prices up by 6%. Globally, the MSCI® EAFE index was up 11%. Combined NYSE and NASDAQ® non-program trading volumes were down an estimated 1% during the year. As the Company s business model is more volume than price sensitive, this created a drag on the Company s equity-linked businesses. The Lehman Brothers Aggregate Bond[sm] index was down 7%. Average fixed-income trading volume was up 14% offsetting some of the weakness in equities.

As of December 31, 2005, assets under custody rose to $10.9 trillion, from $9.7 trillion at December 31, 2004. The increase in assets under custody primarily reflects rising equity prices and new business wins. Equity securities composed 32% of the assets under custody at December 31, 2005 compared with 35% at December 31, 2004, while fixed income securities were 68% compared with 65% last year. Assets under custody in 2005 consisted of assets related to the custody and mutual funds businesses of $7.3 trillion, broker-dealer services assets of $2.2 trillion, and all other assets of $1.4 trillion.

The results for the businesses in the Institutional Service segment are discussed below.

Investor & Broker-Dealer Services Business

(In millions)	2005	2004	2003	Inc/(Dec) 2005 vs. 2004	2004 vs. 2003
Net Interest Income	$ 564	$ 518	$ 501	$ 46	$ 17
Noninterest Income	1,826	1,627	1,474	199	153
Total Revenue	2,390	2,145	1,975	245	170
Provision for Credit Losses	7	7	13		(6)
Noninterest Expense	1,636	1,441	1,316	195	125
Income Before Taxes	747	697	646	50	51
Average Assets	36,233	35,225	33,123	1,008	2,102
Average Deposits	28,316	26,231	24,671	2,085	1,560
Nonperforming Assets	5	28	55	(23)	(27)
Net Charge-offs		4	24	(4)	(20)

In 2005, income before taxes in the Investor & Broker-Dealer Services business increased to $747 million from $697 million in 2004 and $646 million in 2003. The increase in 2005 reflects improvements in net interest income and noninterest income.

Noninterest income was $1,826 million in 2005, compared with $1,627 million in 2004 and $1,474 million in 2003. The increase in noninterest income in 2005 is attributable to an increase in both investor and broker-dealer service fees as well as foreign exchange and other trading revenue generated by clients in this segment.

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Investor services fees were up in both 2005 and 2004. The increase over 2004 reflects strength in global and domestic fund services and custody, as well as new business wins and strong organic growth. Securities lending fees showed good growth in 2005 benefiting from higher loan volumes, driven by new business wins as well as a favorable spread environment. In 2004, investor services fee growth resulted from good organic growth in most areas.

Broker-dealer services fees were up compared with 2004 and 2003. The increase in 2005 reflects higher volumes due to new business wins in the collateral management business and greater volumes in government securities clearance. The Company now handles approximately $1.1 trillion of financing for the Company s broker-dealer clients daily through tri-party collateralized financing agreements, up 18% from a year ago. In 2004, increased broker-dealer services fees reflected higher volumes due to new business wins in the collateral management business and higher levels of mortgage-backed and government trading activity.

Net interest income in the Investor & Broker-Dealer Services business was $564 million in 2005, compared with $518 million in 2004 and $501 million in 2003. Net interest income growth in 2005 reflects increased deposit flows from customers in both businesses. The increase in net interest income in 2004 also reflected growth in deposits, primarily in investor services. Average deposits generated by the Investor & Broker-Dealer Services business were $28.3 billion in 2005, compared with $26.2 billion in 2004 and $24.7 billion in 2003. Average assets in the business were $36.2 billion in 2005, compared with $35.2 billion in 2004 and $33.1 billion in 2003.

Noninterest expense was $1,636 million in 2005, compared with $1,441 million in 2004 and $1,316 million in 2003. The rise in noninterest expense in 2005 was attributable primarily to higher salaries, benefits and sub-custody expenses tied to business growth, increased costs related to business continuity, and higher stock option and pension expenses. The increase in noninterest expense in 2004 was due to higher costs tied to increased activity levels, as well as the upfront expenses associated with the implementation of cost reduction initiatives and higher pension and option expense.

Net charge-offs were zero in 2005, compared with $4 million in 2004 and $24 million in 2003. Nonperforming assets were $5 million in 2005, compared with $28 million in 2004 and $55 million in 2003.

Execution & Clearing Services Business

				Inc/(Dec)	
(In millions)	**2005**	**2004**	**2003**	**2005 vs. 2004**	**2004 vs. 2003**
Net Interest Income	$ 211	$ 170	$ 108	$ 41	$ 62
Noninterest Income	1,327	1,242	959	85	283
Total Revenue	1,538	1,412	1,067	126	345
Provision for Credit Losses	1	1	1		
Noninterest Expense	1,151	1,087	809	64	278
Income Before Taxes	386	324	257	62	67
Average Assets	15,478	15,122	11,022	356	4,100
Average Payables to Customers and Broker-Dealers	6,014	6,361	3,945	(347)	2,416
Nonperforming Assets		2	3	(2)	(1)
Net Charge-offs	8	10	1	(2)	9

In 2005, income before taxes in the Execution & Clearing Services Business increased to $386 million from $324 million and $257 million in 2004 and 2003. The increase in 2005 reflects strong growth in net interest income and higher value added fees at Pershing as well as incremental revenues and earnings contribution from the LJR acquisition in the execution business.

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Noninterest income was $1,327 million in 2005, compared with $1,242 million in 2004 and $959 million in 2003. The execution business benefited in 2005 from increased client activity, strong growth in transition management and incremental revenues from the LJR acquisition. These factors offset the relatively weak market environment, in which non-program trading volumes were down 1%.

Pershing s 2005 noninterest income was up reflecting organic growth from value added fees, partially offset by business lost through client consolidation. The majority of Pershing s revenues are generated from non-transactional activities, such as asset gathering, administration and other services. Pershing s assets under administration were $749 billion at year-end 2005, compared with $706 billion at December 31, 2004. At year-end 2005, margin loans remained flat at $6.1 billion. In 2004, clearing services fees benefited from the full-year impact of Pershing and increased client activity.

In January 2006, a significant customer ended its clearing relationship with Pershing following its acquisition by a major broker-dealer. Pershing currently is in discussions seeking compensation for the termination of the relationship.

Execution and clearing service fees were $1,145 million in 2004, compared with $885 million in 2003. These businesses benefited from the full-year impact of Pershing, as well as increased client activity and strong growth in transition management.

Net interest income in the Execution and Clearing Services business was $211 million in 2005, compared with $170 million in 2004, and $108 million in 2003. Net interest income growth in 2005 and 2004 reflects the benefit of rising interest rates on spreads at Pershing. The year 2004 also benefited from the full-year impact of the Pershing acquisition. Average assets in the business were $15.5 billion in 2005, compared with $15.1 billion in 2004 and $11.0 billion in 2003.

Noninterest expense was $1,151 million in 2005, compared with $1,087 million in 2004 and $809 million in 2003. The rise in noninterest expense in 2005 was attributable to higher salaries, benefits and clearing expenses tied to both higher business activity overall as well as the LJR acquisition. The increase in noninterest expense in 2004 was due to stronger business activity and the full-year impact of the Pershing acquisition.

Net charge-offs were $8 million, $10 million, and $1 million in 2005, 2004, and 2003, respectively. The increase in charge-offs in 2004 is attributable to a credit loss in Pershing s UK clearing business as a result of an alleged deceptive scheme perpetrated on Pershing. Nonperforming assets were zero in 2005, compared with $2 million in 2004 and $3 million in 2003.

Issuer Services Business

				Inc/(Dec)	
(In millions)	**2005**	**2004**	**2003**	**2005 vs. 2004**	**2004 vs. 2003**
Net Interest Income	$ 238	$ 214	$ 208	$ 24	$ 6
Noninterest Income	757	696	636	61	60
Total Revenue	995	910	844	85	66
Provision for Credit Losses	11	11	18		(7)
Noninterest Expense	458	426	393	32	33
Income Before Taxes	526	473	433	53	40
Average Assets	13,349	11,776	11,310	1,573	466
Average Deposits	8,357	7,396	7,124	961	272
Nonperforming Assets	5	30	56	(25)	(26)
Net Charge-offs		4	25	(4)	(21)

In 2005, income before taxes in the Issuer Services Business increased to $526 million from $473 million in 2004 and $433 million in 2003. The increase in 2005 reflects growth in net interest income tied primarily to corporate trust, and higher fees in both depositary receipts and corporate trust.

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Noninterest income was $757 million in 2005, compared with $696 million in 2004 and $636 million in 2003. In 2005, the increase reflects higher levels of trading activity and greater corporate actions in depositary receipts, as well as continued strength in international issuance and structured products in corporate trust. The European corporate trust market is growing rapidly and the Company was able to attract significant amounts of new business. In 2004, the increase reflects strong growth in depositary receipts and solid results in corporate trust.

The overall environment for depositary receipts has improved steadily from 2003 to 2005, with trading volumes increasing at a compound rate of 9%. The trend in net issuance has been strong, fueled by increased cross-border activity. The value of foreign equities held by U.S. investors has increased from 13% in 2003 to 16% in 2005. In addition, the increase in cross-border merger and acquisitions and capital raisings has been strong, particularly in 2005.

The growth in corporate trust fees has been solid over the period. The principal growth drivers have been the structured and international product areas, where the markets are growing more rapidly and the Company is gaining market share.

Net interest income in the Issuer Services business was $238 million in 2005, compared with $214 million in 2004 and $208 million in 2003. Net interest income growth in 2005 reflects the positive impact of rising rates on spreads and increased deposit levels generated by the corporate trust business. The increase in net interest income in 2004 was also driven by the increase in interest rates during the period. Average deposits generated by the Issuer Services business were $8.4 billion in 2005, compared with $7.4 billion in 2004 and $7.1 billion in 2003. Average assets in the business were $13.3 billion in 2005, compared with $11.8 billion in 2004 and $11.3 billion in 2003.

Noninterest expense was $458 million in 2005, compared with $426 million in 2004 and $393 million in 2003. The rise in noninterest expense in 2005 and 2004 was attributable to increased client activity as well as higher technology, stock option and pension expenses.

Net charge-offs were zero in 2005, compared with $4 million in 2004 and $25 million in 2003. Nonperforming assets were $5 million in 2005, compared with $30 million in 2004 and $56 million in 2003.

Treasury Services Business

(In millions)	**2005**	**2004**	**2003**	**Inc/(Dec) 2005 vs. 2004**	**Inc/(Dec) 2004 vs. 2003**
Net Interest Income	$ 173	$ 162	$ 154	$ 11	$ 8
Noninterest Income	272	265	268	7	(3)
Total Revenue	445	427	422	18	5
Provision for Credit Losses	40	40	69		(29)
Noninterest Expense	199	186	173	13	13
Income Before Taxes	206	201	180	5	21
Average Assets	10,622	10,163	8,497	459	1,666
Average Deposits	7,914	8,793	8,810	(879)	(17)
Nonperforming Assets	16	95	177	(79)	(82)
Net Charge-offs	2	14	79	(12)	(65)

In 2005, income before taxes in the Treasury Services Business was $206 million, compared with $201 million in 2004 and $180 million in 2003. The moderate growth rate of this segment reflects both the Company s overall strategy to reduce corporate credit exposures as part of its risk reduction efforts, as well as specific initiatives to reduce the number and size of credit relationships with clients that do not use other securities servicing products. The results in 2005 reflect the continued strong credit environment. The improvement in 2004 over 2003 is primarily attributable to lower credit costs resulting from the reduction in credit risk as well as favorable conditions in credit markets.

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The increase in noninterest income to $272 million in the current year from $265 million in 2004 was due to higher capital market fees associated with clients in this segment, partially offset by lower fees from global payments as more clients used compensating balances to pay for services.

The Treasury Services business s net interest income was $173 million in 2005, compared with $162 million in 2004 and $154 million in 2003. The increase in 2005 reflects customers increased use of compensating balances to pay for global payment services, partially offset by the impact of the credit reduction program. Credit spreads were lower, reflecting the higher asset quality of the portfolio. Average assets for 2005 were $10.6 billion, compared with $10.2 billion in 2004 and $8.5 billion in 2003. Average deposits were $7.9 billion versus $8.8 billion in 2004 and $8.8 billion in 2003.

The provision for credit losses, which is assessed on a long-term credit cycle basis (see Business Segment Accounting Principles), was $40 million in 2005 compared with $40 million in 2004 and $69 million in 2003. The decrease in 2004 compared to 2003 principally reflects the benefits of the Company s corporate credit risk reduction program. Over the past several years, the Company has been seeking to improve its overall risk profile by reducing its credit exposures through elimination of non-strategic exposures, cutting back large individual exposures and avoiding outsized industry concentrations. Since 2001, the Company has reduced credit exposure to its corporate client base by 41%. In 2002, the Company set a goal of reducing corporate credit exposure to $24 billion by December 31, 2004. This goal was accomplished in early 2004 and exposures have since declined to $23.3 billion.

Net charge-offs in the Treasury Services business were $2 million, $14 million, and $79 million in 2005, 2004, and 2003. The charge-offs in 2004 primarily relate to loans to media, corporate, and foreign borrowers. The charge-offs in 2003 primarily relate to corporate borrowers. Nonperforming assets were $16 million in 2005, compared with $95 million in 2004 and $177 million in 2003. The decrease in nonperforming assets in 2005 primarily reflects loan sales, paydowns and charge-offs of commercial loans. The decrease in nonperforming assets in 2004 primarily reflects the sale of $43 million of loans to the operating subsidiaries of a major cable company as well as paydowns and charge-offs of domestic and foreign commercial loans.

Noninterest expense in 2005 was $199 million, compared to $186 million in 2004 and $173 million in 2003. The increase in noninterest expense in 2005 and 2004 was due in part to a higher pension expense, stock option expensing, and an increase in incentive compensation tied to revenues.

Private Bank and BNY Asset Management Segment

				Inc/(Dec)	
(In millions)	**2005**	**2004**	**2003**	**2005 vs. 2004**	**2004 vs. 2003**
Net Interest Income	$ 65	$ 61	$ 60	$ 4	$ 1
Noninterest Income	454	416	348	38	68
Total Revenue	519	477	408	42	69
Provision for Credit Losses	3	3			3
Noninterest Expense	317	288	233	29	55
Income Before Taxes	199	186	175	13	11
Average Assets	2,205	2,144	2,027	61	117
Average Deposits	1,673	1,616	1,765	57	(149)
Nonperforming Assets	1	1	8		(7)
Net Charge-offs		5	7	(5)	(2)

In 2005, income before taxes in the Private Bank and BNY Asset Management Segment was $199 million, compared with $186 million in 2004 and $175 million in 2003. The improvement over the period is primarily attributable to strong revenue growth at Ivy Asset Management.

Noninterest income was $454 million in 2005, compared with $416 million in 2004 and $348 million in 2003. Private Bank and BNY Asset Management revenues in 2005 were up compared with 2004 and 2003. The increase in 2005 reflects strong growth at Ivy, higher fees in private client services, and higher equity price levels. The S&P 500® Index was up 3% for the year, with average daily price levels up 7% from 2004. Performance for the NASDAQ® Index was up 1% for the year, with average daily prices up by 6%. In 2004, the increase reflects strong growth at Ivy, higher fees in private client services, and higher equity price. In 2004, Ivy opened an office in Tokyo to serve the expanding market for hedge fund products in Asia. Ivy successfully launched its London office in 2003.

Assets Under Management Asset Management Sector

(In billions) Estimated	**2005**	**2004**	**2003**
Total Assets Under Management	105	102	89
Equity Securities	35%	36%	34%
Fixed Income Securities	20	21	22
Alternative Investments	14	15	10
Liquid Assets	31	28	34

Assets under management (AUM) were $105 billion at December 31, 2005, compared with $102 billion at December 31, 2004 and $89 million at December 31, 2003. The increase in assets under management for 2005 reflects growth in Ivy, institutional equity products, and liquid assets as well as a rise in equity market values. Institutional clients represent 68% of AUM while individual clients equal 32%. AUM at December 31, 2005, are 35% invested in equities, 20% in fixed income, and 14% in alternative investments, with the remaining amount in liquid assets.

Net interest income in the Private Bank and BNY Asset Management segment was $65 million in 2005, compared with $61 million in 2004 and $60 million in 2003. Net interest income growth in 2005 and 2004 reflects wider spreads given higher interest rates. Average deposits generated by the Private Bank and BNY Asset Management segment were $1.7 billion in 2005, compared with $1.6 billion in 2004 and $1.8 billion in 2003. Average assets in the segment were $2.2 billion in 2005, compared with $2.1 billion in 2004 and $2.0 billion in 2003.

Noninterest expense was $317 million in 2005, compared with $288 million in 2004 and $233 million in 2003. The rise in noninterest expense in 2005 and 2004 was attributable to higher salaries, employee benefits, and technology costs.

Net charge-offs were zero, $5 million, and $7 million in 2005, 2004, and 2003. Nonperforming assets were $1 million in 2005, compared with $1 million and $8 million in 2004 and 2003.

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Retail & Middle Market Banking Segment

				Inc/(Dec)	
(In millions)	**2005**	**2004**	**2003**	**2005 vs. 2004**	**2004 vs. 2003**
Net Interest Income	$ 650	$ 616	$ 597	$ 34	$ 19
Noninterest Income	245	255	261	(10)	(6)
Total Revenue	895	871	858	24	13
Provision for Credit Losses	29	31	31	(2)	
Noninterest Expense	511	484	474	27	10
Income Before Taxes	355	356	353	(1)	3
Average Assets	13,778	15,166	15,996	(1,388)	(830)
Average Noninterest-Bearing Deposits	5,626	5,572	5,477	54	95
Average Deposits	15,709	16,907	16,167	(1,198)	740
Nonperforming Assets	34	52	42	(18)	10
Net Charge-offs	36	31	41	5	(10)
Number of Branches	342	341	341	1	
Number of ATMs	401	378	378	23	

In 2005, income before taxes was $355 million, compared with $356 million in 2004 and $353 million in 2003.

Net interest income in the Retail & Middle Market Banking Segment was $650 million in 2005, compared with $616 million in 2004 and $597 million in 2003. Net interest income growth in both 2005 and 2004 reflects the benefit of higher rates on interest spreads, growth in consumer loans, and the increasing number of small business customers use of compensating balances to pay for services.

Average deposits generated by the Retail & Middle Market Banking Segment were $15.7 billion in 2005, compared with $16.9 billion in 2004 and $16.2 billion in 2003. Average noninterest-bearing deposits were $5.6 billion in 2005, compared with $5.6 billion in 2004 and $5.5 billion in 2003. Average assets in the Retail & Middle Market Banking segment were $13.8 billion, compared with $15.2 billion in 2004 and $16.0 billion in 2003.

Noninterest income was $245 million in 2005, compared with $255 million in 2004 and $261 million in 2003. The decline in noninterest income in 2005 is attributable to lower monthly checking fees, lower gains from the sale of consumer loans given the Company s decision to retain more consumer loans, and small business customers using compensating balances rather than fees to pay for services.

Noninterest expense was $511 million in 2005, compared with $484 million in 2004 and $474 million in 2003. The rise in noninterest expense in 2005 and 2004 was primarily attributable to higher pension, option, marketing, occupancy, and consultant expenses.

Net charge-offs were $36 million, $31 million, and $41 million in 2005, 2004, and 2003. Nonperforming assets were $34 million in 2005, compared with $52 million in 2004 and $42 million in 2003.

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Corporate and Other

(In millions)	2005	2004	2003	Inc/(Dec) 2005 vs. 2004	Inc/(Dec) 2004 vs. 2003
Net Interest Income	$ 8	$ (96)	$ (19)	$ 104	$ (77)
Noninterest Income	75	149	50	(74)	99
Total Revenue	83	53	31	30	22
Provision for Credit Losses	(76)	(78)	23	2	(101)
Noninterest Expense	211	210	300	1	(90)
Income Before Taxes	(52)	(79)	(292)	27	213
Average Assets	9,770	9,744	9,492	26	252
Nonperforming Assets	18	6	8	12	(2)
Net Charge-offs	140	15	5	125	10

In 2005, income before taxes in the Corporate and Other Segment was a loss of $52 million, compared with a loss of $79 million and $292 million in 2004 and 2003.

Net interest income in the Corporate and Other Segment was $8 million in 2005, compared with a loss of $96 million in 2004 and a loss of $19 million in 2003. Net interest income in 2004 included the SFAS 13 cumulative adjustments to the leasing portfolio, which reduced net interest income by $66 million. Excluding the impact of this adjustment, the increase in net interest income in 2005 reflects lower earnings from the leasing portfolio, given the rising rate environment.

Noninterest income was $75 million in 2005, compared with $149 million in 2004 and $50 million in 2003. The decline in noninterest income in 2005 is attributable to both lower securities gains and lower gains from corporate asset sales in 2005 compared with 2004, given the $48 million gain on the sale of 5% of the Company s stake in Wing Hang Bank in 2004. Securities gains were $68 million in 2005, compared to $78 million in 2004 and $35 million in 2003. In 2004, securities gains included $19 million of higher than anticipated gains from four large sponsor funds.

Provision for credit losses was a credit of $76 million in 2005, compared with a $78 million credit in 2004 and a $23 million expense in 2003. The provision for credit losses reflects the difference between the aggregate of the credit provision over a credit cycle assigned to the other segments and the Company s recorded provision. The SFAS 13 aircraft adjustments lowered the provision by $7 million in 2004.

Noninterest expense, largely reflecting unallocated corporate overhead, amortization of goodwill, and nonrecurring items, was $211 million in 2005, compared with $210 million in 2004 and $300 million in 2003. The decrease in noninterest expense in 2004 versus 2003 was due to the $96 million of merger and integration costs associated with Pershing and the $78 million GMAC settlement in 2003, partially offset by growth in corporate overhead and goodwill amortization in 2004.

Net charge-offs were $140 million for 2005, compared to $15 million for 2004 and $5 million for 2003. The charge-offs in 2005 are attributable to the Company s airline leasing portfolio.

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Significant other items related to the Corporate and Other segment for the past three years are presented in the following table.

(In millions)	**2005**	**2004**	**2003**
Items impacting net interest income:			
Cost to Carry Goodwill	(99)	(105)	(95)
Tax Equivalent Basis	(29)	(30)	(35)
SFAS 13 Lease Adjustment		(66)	
Items impacting noninterest income:			
Gain on Sale of FMC	17		
Gain on Sale of Wing Hang		48	
Other Gains			16
Items impacting noninterest expense:			
Severance Costs	5	12	6
Goodwill and Intangibles Amortization	40	34	25
Pershing Integration Expenses			96
RW and Other Regulatory Matters	24	30	
GMAC Settlement			78
Lease Termination		8	

Other items Acquisitions are the responsibility of corporate management. Accordingly, goodwill and the funding cost of goodwill are assigned to the Corporate and Other segment. If the funding cost of goodwill was allocated to the other three segments, it would be assigned based on the goodwill attributable to each segment.

The tax equivalent adjustment is eliminated in the Corporate and Other Segment. Certain revenue and expense items have been driven by corporate decisions and have been included in the Corporate and Other Segment. In 2005, these include the $17 million gain on the sale of FMC and the $24 million charge for the Russian Funds transfer matter and other regulatory matters. Alternatively these items could be allocated to the Institutional Services Segment. In 2004, the $48 million gain on the sale of Wing Hang would be attributable to the Institutional Services Segment. The 2004 charge for the RW Matter would be attributable to the Retail & Middle Market Banking Segment.

Severance and lease termination costs in 2004 primarily relate to the Institutional Services Segment and to staff areas that cut across all business lines. Intangible amortization primarily relates to the Institutional Services Segment. In 2003, the GMAC settlement and the Pershing integration expenses are attributable to the Institutional Services Segment.

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The consolidating schedule below shows the contribution of the Company s businesses to its overall profitability.

(Dollars in millions) For the Year Ended December 31, 2005	Investor & Broker-Dealer Services	Execution & Clearing Services	Issuer Services	Treasury Services	Sub-total Institutional Services	Private Bank & BNY Asset Management	Retail & Middle Market	Corporate and Other	Total
Net Interest Income	$ 564	$ 211	$ 238	$ 173	$ 1,186	$ 65	$ 650	$ 8	$ 1,909
Noninterest Income	1,826	1,327	757	272	4,182	454	245	75	4,956
Total Revenue	2,390	1,538	995	445	5,368	519	895	83	6,865
Provision for Credit Losses	7	1	11	40	59	3	29	(76)	15
Noninterest Expense	1,636	1,151	458	199	3,444	317	511	211	4,483
Income Before Taxes	$ 747	$ 386	$ 526	$ 206	$ 1,865	$ 199	$ 355	$ (52)	$ 2,367
Contribution Percentage*	31%	16%	22%	8%	77%	8%	15%		
Average Assets	$ 36,233	$ 15,478	$ 13,349	$ 10,622	$ 75,682	$ 2,205	$ 13,778	$ 9,770	$ 101,435

(Dollars in millions) For the Year Ended December 31, 2004	Investor & Broker-Dealer Services	Execution & Clearing Services	Issuer Services	Treasury Services	Sub-total Institutional Services	Private Bank & BNY Asset Management	Retail & Middle Market	Corporate and Other	Total
Net Interest Income	$ 518	$ 170	$ 214	$ 162	$ 1,064	$ 61	$ 616	$ (96)	$ 1,645
Noninterest Income	1,627	1,242	696	265	3,830	416	255	149	4,650
Total Revenue	2,145	1,412	910	427	4,894	477	871	53	6,295
Provision for Credit Losses	7	1	11	40	59	3	31	(78)	15
Noninterest Expense	1,441	1,087	426	186	3,140	288	484	210	4,122
Income Before Taxes	$ 697	$ 324	$ 473	$ 201	$ 1,695	$ 186	$ 356	$ (79)	$ 2,158
Contribution Percentage*	31%	15%	21%	9%	76%	8%	16%		
Average Assets	$ 35,225	$ 15,122	$ 11,776	$ 10,163	$ 72,286	$ 2,144	$ 15,166	$ 9,744	$ 99,340

(Dollars in millions) For the Year Ended December 31, 2003	Investor & Broker-Dealer Services	Execution & Clearing Services	Issuer Services	Treasury Services	Sub-total Institutional Services	Private Bank & BNY Asset Management	Retail & Middle Market	Corporate and Other	Total
Net Interest Income	$ 501	$ 108	$ 208	$ 154	$ 971	$ 60	$ 597	$ (19)	$ 1,609
Noninterest Income	1,474	959	636	268	3,337	348	261	50	3,996
Total Revenue	1,975	1,067	844	422	4,308	408	858	31	5,605
Provision for Credit Losses	13	1	18	69	101		31	23	155
Noninterest Expense	1,316	809	393	173	2,691	233	474	300	3,698
Income Before Taxes	$ 646	$ 257	$ 433	$ 180	$ 1,516	$ 175	$ 353	$ (292)	$ 1,752
Contribution Percentage*	31%	13%	21%	9%	74%	9%	17%		
Average Assets	$ 33,123	$ 11,022	$ 11,310	$ 8,497	$ 63,952	$ 2,027	$ 15,996	$ 9,492	$ 91,467

*As a percent of total income before tax excluding Corporate and Other.

Foreign Operations

The Company s primary foreign activities consist of securities servicing and global payment services. Target customers include financial service companies, pension funds and securities issuers worldwide. The Company s international clearing business delivers clearing and financial services outsourcing solutions in 65 countries. In Execution, the Company provides institutional trade execution services in over 80 global markets, including 50 emerging markets.

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In Investor Services, the Company is a leading global custodian. In the United Kingdom the Company provides a full global and local product set. In Continental Europe a full global product set is provided with access to local markets through strategic partnerships. Off-shore mutual fund servicing capabilities for funds registered in Dublin, the Channel Islands, Luxembourg and Singapore are provided through operations in Luxembourg and Dublin.

In Issuer Services, the Company has been a leader in the ADR market, currently acting as the depositary receipts agent for 64% of all publicly sponsored listings by foreign companies. For debt issuance, the Company is one of the leading corporate trust providers for global debt issuance.

In the Asia-Pacific region, the Company has over 50 years experience providing trade and cash services to financial institutions and central banks. In addition, the Company offers a broad range of servicing and fiduciary products to financial institutions, corporations and central banks depending on the state of market development. In emerging markets, the Company leads with global payments and issuer services, introducing other products as the markets mature. For more established markets, the Company focus is on global, not local, investor services products and alternative investments.

The Company is also a leading provider and major market maker in the area of foreign exchange and interest-rate risk management services, dealing in over 100 currencies, and provides traditional trust and banking services to customers domiciled outside of the United States, principally in Europe and Asia. Ivy UK provides clients in Europe and the Middle East with hedge fund of funds investment advisory services.

Major operation centers are based in London, England; Brussels, Belgium; and Singapore with additional subsidiaries, branches, and representative offices in 33 countries.

International clients accounted for 25% of revenue and 18% of net income in 2005. The Company has approximately 3,699 employees in Europe and 1,693 in Asia. Foreign revenue, income before income taxes, net income and assets from foreign operations are shown in the table below.

	2005				2004				2003			
(In millions) Geographic Data	Revenues	Income Before Income Taxes	Net Income	Total Assets	Revenues	Income Before Income Taxes	Net Income	Total Assets	Revenues	Income Before Income Taxes	Net Income	Total Assets
Domestic	$ 5,177	$ 1,933	$ 1,283	$ 75,795	$ 4,703	$ 1,706	$ 1,139	$ 74,343	$ 4,367	$ 1,442	$ 952	$ 72,830
Europe	1,209	306	203	19,414	1,140	308	205	15,062	943	286	189	13,771
Asia	298	97	64	4,828	306	135	90	3,759	184	25	17	4,348
Other	181	31	21	2,037	146	9	6	1,365	111	(1)	(1)	1,448
Total	$ 6,865	$ 2,367	$ 1,571	$ 102,074	$ 6,295	$ 2,158	$ 1,440	$ 94,529	$ 5,605	$ 1,752	$ 1,157	$ 92,397

In 2005, revenues from Europe were $1,209 million, compared with $1,140 million in 2004 and $943 million in 2003. Excluding the 2004 impact of a SFAS 13 leasing adjustment, revenues in Europe were up 11% in 2005. The increase in 2005 reflects strong growth in investor and issuer service revenues. The increase in 2004 reflects the positive impact of a SFAS 13 leasing adjustment, full-year impact of the Pershing acquisition, new business growth, increased revenue from depositary receipts, and Ivy. Revenues from Asia were $298 million in 2005, compared with $306 million and $184 million in 2004 and 2003, respectively. The slight decrease in Asia in 2005 was primarily due to the large gain in 2004 related to Wing Hang Bank. Excluding the impact of the 2004 Wing Hang Bank sale, revenues in Asia were up 16% in 2005 reflecting strength in investor services, execution services and Ivy. Net income from Europe was $203 million in 2005, compared with $205 million and $189 million in 2004 and 2003, respectively. Net income from Asia was $64 million in 2005, compared with $90 million and $17 million in 2004 and 2003, respectively. Net income in Europe and Asia were driven by the same factors affecting revenue. In addition, in 2005 and 2004, net income in Europe was adversely impacted by the strength of the Euro and Sterling versus the dollar.

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Cross-Border Risk

Foreign assets are subject to general risks attendant to the conduct of business in each foreign country, including economic uncertainties and each foreign government s regulations. In addition, the Company s foreign assets may be affected by changes in demand or pricing resulting from fluctuations in currency exchange rates or other factors. Cross-border outstandings include loans, acceptances, interest-bearing deposits with other banks, other interest bearing investments, and other monetary assets which are denominated in dollars or other non-local currency. Also included are local currency outstandings not hedged or funded by local borrowings.

The tables below show the Company s cross-border outstandings for the last three years where cross-border exposure exceeds 1.00% of total assets (denoted with *) or 0.75% of total assets (denoted with **).

(In millions)

2005	Germany*	United Kingdom*	Netherlands*	France*	Belgium**	Switzerland**
Banks and other Financial Institutions	$ 2,216	$ 571	$ 1,010	$ 740	$ 634	$ 744
Public Sector	185			169	49	
Commercial, Industrial and Other	406	1,256	570	203	257	141
Total Cross-Border Outstandings	$ 2,807	$ 1,827	$ 1,580	$ 1,112	$ 940	$ 885

(In millions)

2004	Germany*	United Kingdom*	France*
Banks and other Financial Institutions	$ 2,586	$ 307	$ 850
Public Sector	176		128
Commercial, Industrial and Other	433	776	302
Total Cross-Border Outstandings	$ 3,195	$ 1,083	$ 1,280

(In millions)

2003	Germany*	United Kingdom*	Belgium*	Netherlands*	France**
Banks and other Financial Institutions	$ 1,988	$ 1,048	$ 815	$ 719	$ 473
Public Sector	169	1	217		143
Commercial, Industrial and Other	377	885	108	359	299
Total Cross-Border Outstandings	$ 2,534	$ 1,934	$ 1,140	$ 1,078	$ 915

CRITICAL ACCOUNTING POLICIES

The Company s significant accounting policies are described in the Notes to Consolidated Financial Statements under Summary of Significant Accounting and Reporting Policies . Four of the Company s more critical accounting policies are those related to the allowance for credit losses, the valuation of derivatives and securities where quoted market prices are not available, goodwill and other intangibles, and pension accounting.

In addition to the Summary of Significant Accounting and Reporting Policies footnote, further information on policies related to the allowance for credit losses can be found under Asset Quality and Allowance for Credit Losses in the MD&A. Further information on the valuation of derivatives and securities where quoted market prices are not available can be found under Market Risk Management and Trading Activities and Risk Management in the MD&A section and in Fair Value of Financial Instruments in the Notes to Consolidated Financial Statements. Further information on goodwill and intangible assets can be found in Goodwill and Intangibles in the Notes to Consolidated Financial Statements. Additional information on pensions can be found in Employee Benefit Plans in the Notes to the Consolidated Financial Statements.

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Allowance for Credit Losses

The allowance for credit losses and allowance for lending-related commitments consist of four elements: (1) an allowance for impaired credits; (2) an allowance for higher risk rated loans and exposures; (3) an allowance for pass rated loans and exposures; and (4) an unallocated allowance based on general economic conditions and certain risk factors in the Company s individual portfolio and markets. Further discussion on the four elements can be found under Asset Quality and Allowance for Credit Losses in the MD&A section.

The allowance for credit losses represents management s estimate of probable losses inherent in the Company s loan portfolio. This evaluation process is subject to numerous estimates and judgments. Probability of default ratings are assigned after analyzing the credit quality of each borrower/counterparty and the Company s internal rating are generally consistent with external ratings agency s default databases. Loss given default ratings are driven by the collateral, structure, and seniority of each individual asset and are consistent with external loss given default/recovery databases. The portion of the allowance related to impaired credits is based on the present value of future cash flows. Changes in the estimates of probability of default, risk ratings, loss given default/recovery rates, and cash flows could have a direct impact on the allocated allowance for loan losses.

To the extent actual results differ from forecasts or management s judgment, the allowance for credit losses may be greater or less than future charge-offs.

The Company considers it difficult to quantify the impact of changes in forecast on its allowance for credit losses. Nevertheless, the Company believes the following discussion may enable investors to better understand the variables that drive the allowance for credit losses.

A key variable in determining the allowance is management s judgment in determining the size of the unallocated allowance. At December 31, 2005, the unallocated allowance was 17% of the total allowance. If the unallocated allowance were five percent higher or lower, the allowance would have increased or decreased by $28 million, respectively.

The credit rating assigned to each credit is another significant variable in determining the allowance. If each credit were rated one grade better, the allowance would have decreased by $96 million, while if each credit were rated one grade worse, the allowance would have increased by $151 million.

Similarly, if the loss given default were one rating worse, the allowance would have increased by $62 million, while if the loss given default were one rating better, the allowance would have decreased by $56 million.

For impaired credits, if the fair value of the loans were 10% higher or lower, the allowance would have increased or decreased by $3 million, respectively.

Valuation of Derivatives and Securities Where Quoted Market Prices Are Not Available

When quoted market prices are not available for derivatives and securities values, such values are determined at estimated fair value, which is defined as the value at which positions could be closed out or sold in a transaction with a willing counterparty over a period of time consistent with the Company s trading or investment strategy. Fair value for these instruments is determined based on discounted cash flow analysis, comparison to similar instruments, and the use of financial models. Financial models use as their basis independently-sourced market parameters including, for example, interest rate yield curves, option volatilities, and currency rates. Discounted cash flow analysis is dependent upon estimated future cash flows and the level of interest rates. Model-based pricing uses inputs of observable prices for interest rates, foreign exchange rates, option volatilities and other factors. Models are benchmarked and validated by independent parties. The Company s valuation process takes into consideration factors such as counterparty credit quality, liquidity and

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concentration concerns. The Company applies judgment in the application of these factors. In addition, the Company must apply judgment when no external parameters exist. Finally, other factors can affect the Company s estimate of fair value, including market dislocations, incorrect model assumptions, and unexpected correlations.

These valuation methods could expose the Company to materially different results should the models used or underlying assumptions be inaccurate. See Use of Estimates in the Notes to Consolidated Financial Statements Summary of Significant Accounting and Reporting Policies .

To assist in assessing the impact of a change in valuation, at December 31, 2005, approximately $2.2 billion of the Company s portfolio of securities and derivatives is not priced based on quoted market prices. A change of 2.5% in the valuation of these securities and derivatives would result in a change in pre-tax income of $56 million.

Goodwill and Other Intangibles

The Company records all assets and liabilities acquired in purchase acquisitions, including goodwill, indefinite-lived intangibles, and other intangibles, at fair value as required by SFAS 141. Goodwill ($3,619 million at December 31, 2005) and indefinite-lived intangible assets ($370 million at December 31, 2005) are not amortized but are subject to annual tests for impairment or more often if events or circumstances indicate they may be impaired. Other intangible assets are amortized over their estimated useful lives and are subject to impairment if events or circumstances indicate a possible inability to realize the carrying amount. The initial recording of goodwill and other intangibles requires subjective judgments concerning estimates of the fair value of the acquired assets. The goodwill impairment test is performed in two phases. The first step compares the fair value of the reporting unit with its carrying amount, including goodwill. If the fair value of the reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not impaired; however, if the carrying amount of the reporting unit exceeds its fair value, an additional procedure must be performed. That additional procedure compares the implied fair value of the reporting unit s goodwill with the carrying amount of that goodwill. An impairment loss is recorded to the extent that the carrying amount of goodwill exceeds its implied fair value. Indefinite-lived intangible assets are evaluated for impairment at least annually by comparing their fair value to their carrying value.

Other identifiable intangible assets ($441 million at December 31, 2005) are evaluated for impairment if events and circumstances indicate a possible impairment. Such evaluation of other intangible assets is based on undiscounted cash flow projections. Fair value may be determined using: market prices, comparison to similar assets, market multiples, discounted cash flow analysis and other determinants. Estimated cash flows may extend far into the future and, by their nature, are difficult to determine over an extended timeframe. Factors that may significantly affect the estimates include, among others, competitive forces, customer behaviors and attrition, changes in revenue growth trends, cost structures and technology, and changes in discount rates and specific industry or market sector conditions. Other key judgments in accounting for intangibles include useful life and classification between goodwill and indefinite-lived intangibles or other intangibles which require amortization. See Goodwill and Intangibles in the Notes to Consolidated Financial Statements for additional information regarding intangible assets.

To assist in assessing the impact of a goodwill or intangible asset impairment charge, at December 31, 2005, the Company has $4.4 billion of goodwill and intangible assets. The impact of a 5% impairment charge would result in a reduction in pre-tax income of approximately $222 million.

Pension Accounting

The Company has defined benefit plans covering approximately 13,900 U.S. employees and approximately 3,175 non-US employees.

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The Company has three defined benefit pension plans in the U.S. and six overseas. The U.S. plans account for 82% of the projected benefit obligation. Pension expense was $26 million in 2005 while there were pension credits in 2004 and 2003 of $24 million and $39 million. In addition to its pension plans, the Company also has an Employee Stock Ownership Plan (ESOP) which may provide additional benefits to certain employees. Upon retirement, covered employees are entitled to the higher of their benefit under the ESOP or the defined benefit plan. If the benefit is higher under the defined benefit plan, the employees ESOP account is contributed to the pension plan.

A number of key assumption and measurement date values determine pension expense. The key elements include the long-term rate of return on plan assets, the discount rate, the market-related value of plan assets, and for the primary U.S. plan the price used to value stock in the ESOP. Since 2003, these key elements have varied as follows:

(Dollars in millions, except per share amounts)	2006	2005	2004	2003
Domestic Plans:				
Long-Term Rate of Return on Plan Assets	7.88%	8.25%	8.75%	9.00%
Discount Rate	5.88	6.00	6.25	6.50
Market-Related Value of Plan Assets[1]	$ 1,324	$ 1,502	$ 1,523	$ 1,483
ESOP Stock Price[1]	30.46	30.67	27.88	33.30
Net U.S Pension Credit/(Expense)		$ (17)	$ 31	$ 46
All other Pension Credit/(Expense)		(9)	(7)	(7)
Total Pension Credit/(Expense)		$ (26)	$ 24	$ 39

(1) Actuarially smoothed data. See Summary of Significant Accounting and Reporting Policies in Notes to the Consolidated Financial Statements.

The discount rate for U.S. pension plans was determined after reviewing a number of high quality long-term bond indices whose yields were adjusted to match the duration of the Company s pension liability. The Company also reviewed the results of several models that matched bonds to the Company s pension cash flows. The various indices and models produced discount rates ranging from 5.68% to 6.2%. After reviewing the various indices and models the Company selected a discount rate of 5.875%. The discount rates for foreign pension plans are based on high quality corporate bonds rates in countries that have an active corporate bond market. In those countries with no active corporate bond market, discount rates are based on local government bond rates plus a credit spread.

The Company s expected long-term rate of return on plan assets is based on anticipated returns for each asset class. At September 30, 2005 and 2004, the assumptions for the long-term rates of return on plan assets were 7.88% and 8.25%, respectively. Anticipated returns are weighted for the target allocation for each asset class. Anticipated returns are based on forecasts for prospective returns in the equity and fixed income markets, which should track the long-term historical returns for these markets. The Company also considers the growth outlook for U.S. and global economies, as well as current and prospective interest rates.

The market-related value of plan assets also influences the level of pension expense. Differences between expected and actual returns are recognized over five years to compute an actuarially derived market-related value of plan assets. In 2005, the market-related value of plan assets declined as the extraordinary actual return in 2000 was replaced with a more modest return.

Unrecognized actuarial gains and losses are amortized over the future service period (11 years) of active employees if they exceed a threshold amount. The Company currently has unrecognized losses which are being amortized.

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For 2005, U.S. pension expense increased by $48 million reflecting changes in assumptions, the amortization of unrecognized pension losses and a decline in the market-related value of plan assets. These same factors are expected to further increase pension expense in 2006. To reduce the impact of these factors, the Company changed certain of its domestic defined benefit pension plans during the third quarter of 2005. The primary change was to switch the computation of the benefits from final average pay to career average pay effective January 1, 2006. As a result U.S. pension expense is expected to increase by approximately $21 million.

The annual impacts on the primary U.S. plan of hypothetical changes in the key elements on the pension expense are shown in the tables below.

	Increase in			Decrease in	
(Dollars in millions)	**Pension Expense**		**2006 Base**	**Pension Expense**	
Long-Term Rate of Return on Plan Assets	6.88%	7.38%	7.88%	8.38%	8.88%
Change in Pension Expense	$ 16.0	$ 7.9	N/A	$ 7.9	$ 15.7
Discount Rate	5.38%	5.63%	5.88%	6.13%	6.38%
Change in Pension Expense	$ 14.9	$ 7.2	N/A	$ 6.9	$ 13.4
Market-Related Value of Plan Assets	-20.00%	-10.00%	$ 1,324	+10.00%	+20.00%
Change in Pension Expense	$ 50.8	$ 25.4	N/A	$ 25.4	$ 50.8
ESOP Stock Price	$ 20.46	$ 25.46	$ 30.46	$ 35.46	$ 40.46
Change in Pension Expense	$ 15.2	$ 7.3	N/A	$ 6.7	$ 12.9

CONSOLIDATED BALANCE SHEET REVIEW

The Company s assets were $102.1 billion at December 31, 2005, up from $94.5 billion in the prior year. The increase in 2005 from 2004 primarily reflects increased loans to financial institutions and growth in the securities portfolio. Investment securities as a percent of the Company s year-end assets were 27% in 2005 and 25% in 2004. Loans as a percent of assets was 39% and 37% of assets in 2005 and 2004, respectively. Total shareholders equity was $9.9 billion at December 31, 2005 compared with $9.3 billion in 2004. The major reason for the increase in shareholders equity was the retention of earnings.

Investment Securities

Total investment securities were $27.3 billion in 2005 compared with $23.8 billion in 2004 and $22.8 billion in 2003. The increases in 2005 and 2004 were primarily due to growth in the Company s portfolio of highly rated mortgage-backed securities. In 2005 and 2004, the Company added approximately $3.1 billion and $0.7 billion, respectively, of mortgage-backed securities to its investment portfolio. Average investment securities were $25.2 billion in 2005 compared with $23.0 billion in 2004 and $19.9 billion in 2003. At December 31, 2005, the fixed income portfolio composition was approximately 39% hybrid, 35% fixed rate, and 12% variable rate mortgage-backed securities while treasuries, government agencies, municipalities and short-term securities were 8% and other securities were 6%.

The Company s portfolio of mortgage-backed securities is 89% rated AAA, 8% AA, and 3% A. Mortgage-backed securities increased to $22.5 billion in 2005 from $19.4 billion in 2004. The primary risk in these securities is interest rate sensitivity. The Company seeks to reduce interest rate risk by investing in securities that convert to floating within three to five years or by investing in traunches of mortgage-backed securities that have rapid repayment characteristics. See Asset/Liability Management . The Company has been adding either adjustable or short life classes of structured mortgage-backed securities, both of which have short durations. The Company has maintained an effective duration of approximately 1.9 years on its mortgage portfolio to best match its liabilities and to reduce the adverse impact from a rise in interest rates.

Corporate debt securities declined in 2005. The primary risks in corporate debt securities are credit risk and interest rate risk. Almost all of the corporate securities are investment grade. Included in these securities are $0.9 billion of investment grade securities that are guaranteed by highly rated financial institutions.

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The short-term money market instruments and obligations of state and political subdivisions have a modest amount of credit risk. The U.S. Treasury and Agency securities and obligations of state and political subdivision are generally fixed rate securities so they expose the Company to interest rate risk.

The table below shows the distribution of the Company s securities portfolio:

Investment Securities (at Fair Value)

(In millions)	**December 31, 2005**	**December 31, 2004**
Fixed Income:		
Mortgage-Backed Securities	$ 22,483	$ 19,393
Asset-Backed Securities	305	
Corporate Debt	1,034	1,259
Short-Term Money Market Instruments	975	982
U.S. Treasury Securities	226	403
U.S. Government Agencies	620	505
State and Political Subdivisions	224	197
Emerging Market Debt (Collateralized by US Treasury Zero Coupon Obligations)	117	107
Other Foreign Debt	363	545
Subtotal Fixed Income	26,347	23,391
Equity Securities:		
Money Market Funds	922	388
Other	31	10
Subtotal Equity Securities	953	398
Total Securities	$ 27,300	$ 23,789

The net unrealized loss on securities available-for-sale was $108 million at December 31, 2005, compared with a gain of $75 million at December 31, 2004. The decline in unrealized gains reflects the rise in interest rates in 2005.

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The following table shows the maturity distribution by carrying amount and yield (not on a tax equivalent basis) of the Company s securities portfolio at December 31, 2005.

(Dollars in millions)	U.S. Government Amount	U.S. Government Yield*	U.S Government Agency Amount	U.S Government Agency Yield*	States and Political Subdivisions Amount	States and Political Subdivisions Yield*	Other Bonds, Notes and Debentures Amount	Other Bonds, Notes and Debentures Yield*	Mortgage/ Asset-Backed and Equity Securities Amount	Mortgage/ Asset-Backed and Equity Securities Yield*	Total
Securities Held-to-Maturity											
One Year or Less	$	%	$	%	$ 105	4.77%	$ 7	4.47%	$	%	$ 112
Over 1 through 5 Years	15	3.47	245	3.42							260
Over 5 through 10 Years	33	4.70									33
Over 10 years							121	6.25			121
Mortgage-Backed Securities									1,451	4.78	1,451
	$ 48	4.32%	$ 245	3.42%	$ 105	4.77%	$ 128	6.15%	$ 1,451	4.78%	$ 1,977
Securities Available-for-Sale											
One Year or Less	$ 178	3.31%	$ 221	3.35%	$ 8	5.58%	$ 1,799	4.03%	$	%	$ 2,206
Over 1 through 5 Years			163	4.03	36	6.07	4	5.90			203
Over 5 through 10 Years					43	5.86	4	6.46			47
Over 10 years					28	6.40	547	3.10			575
Mortgage-Backed Securities									21,162	4.67	21,162
Asset-Backed Securities									307	5.19	307
Equity Securities									957	4.03	957
	$ 178	3.31%	$ 384	3.64%	$ 115	6.04%	$ 2,354	3.96%	$ 22,426	4.65%	$ 25,457

* Yields are based upon the amortized cost of securities.

The Company also has equity investments categorized as other assets (bracketed amounts indicate carrying values). Included in other assets are strategic investments related to securities servicing ($73 million), venture capital investments ($341 million), an investment in Wing Hang Bank Ltd. ($215 million), tax advantaged low-income housing ($176 million), Federal Reserve Bank stock ($106 million), and other equity investments ($4 million).

The largest minority interest is Wing Hang with a fair value of $427 million (book value of $215 million) at December 31, 2005. An agreement with certain other shareholders of Wing Hang prohibits the sale of this interest without their permission. The Company received dividends from Wing Hang of $16 million, $12 million, and $17 million in 2005, 2004, and 2003, respectively. In 2004, the Company reduced its investment in Wing Hang from approximately 25% of Wing Hang s outstanding shares to 20%.

Venture capital activities consist of investments in private equity funds, mezzanine financings, and direct equity investments. The carrying and fair value of the Company s venture capital investments was $341 million at December 31, 2005, consisting of investments in private equity funds of $246 million, direct equity of $29 million, mezzanine financings of $39 million and leveraged bond funds of $27 million. Fair values for private equity funds are generally based upon information provided by fund sponsors and the Company s knowledge of the underlying portfolio while mezzanine financing and direct equity investments are based upon Company models.

In 2005, the Company had an average invested balance of $347 million in venture capital. Securities gains and interest income were $54 million, a pre-tax return of 16%. For 2006, the Company enters the year with a $341 million investment balance, and would expect returns to be somewhat lower.

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At December 31, 2005, the Company had $35 million of principal investment commitments to private equity funds and partnerships compared with $60 million at December 31, 2004. The timing of future cash requirements to fund such commitments is generally dependent on the investment cycle. This cycle, the period over which privately-held companies are funded by private equity investors and ultimately sold, merged, or taken public through an initial offering, can vary based on overall market conditions as well as the nature and type of industry in which the companies operate. If unused, the commitments expire as follows:

(In millions)	Commitments
2006	$ 25
2007	3
2008 - 2010	7
Total	$ 35

Commitments to venture capital limited partnerships may extend beyond expiration period shown to cover certain follow-on investments, claims and liabilities, and organizational and partnership expenses.

Consistent with the Company s policy to focus on its core activities, it continues to reduce its exposure to venture capital activities. At December 31, 2005, the Company had hedged approximately $39 million of its private equity fund investments. Hedge gains and losses are recorded at fair value in securities gains. Consistent with its objective to expand its asset management activities, the Company expects to start the $200 million BNY Mezzanine Fund LLP in 2006 and plans to commit up to $75 million to the fund, and it may make other commitments consistent with that strategy from time to time.

Loans

	December 31,			Annual Average		
(In billions)	Total	Non-Margin	Margin	Total	Non-Margin	Margin
2005	$ 40.7	$ 34.6	$ 6.1	$ 39.7	$ 33.3	$ 6.4
2004	35.8	29.7	6.1	37.8	31.5	6.3
2003	35.3	29.6	5.7	35.6	31.8	3.8

Total loans were $40.7 billion at December 31, 2005, compared with $35.8 billion in 2004. The increase in 2005 versus 2004 primarily reflects an increase in overdrafts, securities industry loans, and residential mortgages. The Company continues to focus on its strategy of reducing non-strategic and outsized corporate loan exposures to improve its credit risk profile. Average total loans were $39.7 billion in 2005, compared with $37.8 billion in 2004. The increase in average loans in 2005 primarily results from increased lending to financial institutions.

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The table below shows trends in the loans outstanding at year-end over the last five years based on a product analysis.

(In millions)	2005	2004	2003	2002	2001
Domestic					
Commercial and Industrial Loans	$ 6,271	$ 6,168	$ 6,611	$ 10,612	$ 11,633
Real Estate Loans:					
Construction and Land Development	324	284	304	480	434
Other, Principally Commercial Mortgages	1,694	2,040	2,335	2,420	2,501
Collateralized by Residential Properties	5,890	4,593	3,739	3,416	3,050
Banks and Other Financial Institutions	2,156	1,323	1,320	1,292	2,075
Loans for Purchasing or Carrying Securities	4,935	3,028	4,221	1,720	3,581
Lease Financings	3,262	3,595	3,727	3,529	3,576
Less:					
Unearned Income on Lease Financings	(938)	(1,072)	(1,063)	(944)	(1,026)
Consumer Loans	1,372	1,293	1,429	1,669	1,782
Margin loans	6,089	6,059	5,712	352	452
Other	946	548	431	238	427
Total Domestic	32,001	27,859	28,766	24,784	28,485
Foreign					
Commercial and Industrial Loans	1,456	793	1,305	1,780	2,390
Banks and Other Financial Institutions	3,924	3,939	2,045	1,624	2,060
Lease Financings	5,816	5,871	6,026	6,062	5,271
Less:					
Unearned Income on Lease Financings	(2,615)	(2,731)	(2,960)	(3,124)	(2,810)
Government and Official Institutions	101	42	93	205	224
Other	43	8	8	9	127
Total Foreign	8,725	7,922	6,517	6,556	7,262
Less: Allowance for Loan Losses	(411)	(591)	(668)	(656)	(415)
Net Loans	$ 40,315	$ 35,190	$ 34,615	$ 30,684	$ 35,332

Asset Quality and Allowance for Credit Losses

Over the past several years, the Company has improved its risk profile through greater focus on clients who are active users of the Company s non-credit services, with a de-emphasis on broad-based loan growth. The Company s primary exposure to credit risk of a customer consists of funded loans, unfunded formal contractual commitments to lend, counterparty risk associated with derivative transactions and overdrafts associated with clearing and settlement.

The role of credit has shifted to one that complements the Company s other services instead of as a lead product. Credit solidifies customer relationships and, through a disciplined allocation of capital, can earn acceptable rates of return as part of an overall relationship. The Company s credit risk management objectives are: (1) to eliminate non-strategic exposures; (2) to increase granularity in the portfolio by cutting back large individual borrower exposures; (3) to restructure the portfolio to avoid outsized industry concentrations; and (4) to limit exposures to non-investment grade counterparties. The goal of these objectives is to reduce volatility in the Company s credit provisioning and earnings. The Company regularly culls its loan portfolio of credit exposures that no longer meet risk/return criteria, including an assessment of overall relationship profitability. In addition, the Company makes use of credit derivatives and other risk mitigants to hedge portions of the credit risk in its portfolio. The effect of these transactions is to transfer credit risk to creditworthy, independent third parties.

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The Company continues to make progress towards improving its credit risk profile.

At December 31, 2005, corporate exposure was $23.3 billion.

The Company brought industry concentrations in line with reduced targets in areas such as telecom, retailing, and automotive. The largest single corporate industry exposure is now media at 13%.

The Company continued to eliminate non-strategic exposures that do not meet yield or cross-sell criteria.

At December 31, 2005, the Company has used credit default swaps to reduce exposure on $1,099 million of loans and commitments. At December 31, 2005, total exposures were $89.0 billion up from $82.5 billion in 2004 reflecting greater lending to financial institutions and increased residential mortgage lending.

The Company s largest absolute risk is lending to financial institutions and corporates, which make up 66% of the total and remained the same as 2004. The consumer and middle market portfolio increased by 13% reflecting increased residential mortgage lending. The business unit components of the loan portfolio are detailed below.

Loan Portfolio

	12/31/05		12/31/04		12/31/03		12/31/02	
(In billions)	**Loans**	**Exposure**	**Loans**	**Exposure**	**Loans**	**Exposure**	**Loans**	**Exposure**
Financial Institutions	$ 13.0	$ 35.5	$ 9.5	$ 31.1	$ 9.2	$ 31.0	$ 6.6	$ 30.7
Corporate	3.7	23.3	3.6	23.0	4.0	24.5	8.2	31.6
	16.7	58.8	13.1	54.1	13.2	55.5	14.8	62.3
Consumer & Middle Market	10.3	15.1	8.9	13.4	8.2	12.3	8.0	12.1
Lease Financings	5.5	5.5	5.6	5.6	5.8	5.8	5.6	5.7
Commercial Real Estate	2.1	3.5	2.1	3.3	2.4	3.2	2.5	3.3
Margin Loans	6.1	6.1	6.1	6.1	5.7	5.7	0.4	0.4
Total	$ 40.7	$ 89.0	$ 35.8	$ 82.5	$ 35.3	$ 82.5	$ 31.3	$ 83.8

Of the credits in the financial institutions and corporate segments with a rating equivalent to non-investment grade at December 31, 2005, 47% of these credits mature in less than one year.

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Financial Institutions

The financial institutions portfolio exposure was up from $30.7 billion in 2002 to $35.5 billion at year-end 2005. The financial institutions exposure fluctuates day to day based on the financing needs of the Company s broker-dealer customers and overdrafts relating to security settlements. These exposures are generally high quality, with 85% meeting the investment grade criteria of the Company s rating system. The exposures are short-term with 74% expiring within one year, and are frequently secured. For example, mortgage banking, securities industry, and investment managers often borrow against marketable securities held in custody at the Company. The diversity of the portfolio is shown in the accompanying table.

(In billions)	12/31/05					12/31/04			12/31/03	
Lending Division	**Loans**	**Unfunded Commitments**	**Total Exposures**	**% Inv Grade**	**% due <1 Yr**	**Loans**	**Unfunded Commitments**	**Total Exposures**	**Loans**	**Unfunded Commitments**
Banks	$ 5.1	$ 3.8	$ 8.9	65%	87%	$ 4.2	$ 3.5	$ 7.7	$ 2.6	$ 3.1
Securities Industry	3.4	3.7	7.1	88	96	1.5	3.0	4.5	1.9	3.5
Insurance	0.4	4.9	5.3	96	44	0.5	4.8	5.3	0.3	5.0
Government	0.1	4.7	4.8	98	52		5.0	5.0	0.2	5.6
Asset Managers	3.8	3.6	7.4	89	80	3.0	3.8	6.8	3.6	3.5
Mortgage Banks	0.1	0.7	0.8	70	51	0.2	0.7	0.9	0.4	0.5
Endowments	0.1	1.1	1.2	99	55	0.1	0.8	0.9	0.2	0.6
Total	$ 13.0	$ 22.5	$ 35.5	85%	74%	$ 9.5	$ 21.6	$ 31.1	$ 9.2	$ 21.8

Corporate

The corporate portfolio exposure was reduced to $23.3 billion at December 31, 2005, from $31.6 billion at year-end 2002. Approximately 74% of the portfolio is investment grade based on the Company s rating system and 16% of the portfolio matures within one year. In 2004, the Company reached its goal of reducing corporate exposure below $24.0 billion. This represents a decline of over $9 billion since the Company announced its goal to reduce corporate exposure in 2002.

(In billions)	12/31/05					12/31/04			12/31/03	
Lending Division	**Loans**	**Unfunded Commitments**	**Total Exposures**	**% Inv Grade**	**% due <1 Yr**	**Loans**	**Unfunded Commitments**	**Total Exposures**	**Loans**	**Unfunded Commitments**
Media	$ 1.1	$ 2.0	$ 3.1	62%	10%	$ 0.9	$ 2.2	$ 3.1	$ 0.9	$ 2.3
Cable	0.4	0.5	0.9	41	18	0.6	0.4	1.0	0.7	0.7
Telecom	0.1	0.4	0.5	79	7	0.1	0.5	0.6	0.3	0.6
Subtotal	1.6	2.9	4.5	60	11	1.6	3.1	4.7	1.9	3.6
Energy	0.4	4.9	5.3	84	10	0.4	4.4	4.8	0.4	4.2
Retailing	0.1	2.1	2.2	75	23	0.1	2.1	2.2	0.1	2.3
Automotive*	0.1	1.2	1.3	55	38	0.1	1.7	1.8	0.1	2.1
Healthcare	0.3	1.7	2.0	82	11	0.3	1.5	1.8	0.2	1.3
Other**	1.2	6.8	8.0	77	18	1.1	6.6	7.7	1.3	7.0
Total	$ 3.7	$ 19.6	$ 23.3	74%	16%	$ 3.6	$ 19.4	$ 23.0	$ 4.0	$ 20.5

* In 2005, the Company reduced its automotive exposure, eliminated the Automotive division, and transferred the remaining customers to the other geographic lending divisions. The amounts in the table were reconstructed for comparison to prior years.

** Diversified portfolio of industries and geographies

Other Corporate Risks

Included in the Company s corporate exposures are automotive and airline exposures. The Company continues to selectively reduce automotive exposures given ongoing weakness in the domestic automotive industry. Total exposure previously reported in the Automotive Division was $1.3 billion at December 31, 2005, down $516 million from December 31, 2004. This broadly defined industry portfolio consists of $194 million to Big Three automotive manufacturing, $199 million to finance subsidiaries, $453 million to highly rated asset- backed securitizations, $311 million to suppliers, and $144 million of other.

The Company s exposure to the airline industry consists of a $337 million leasing portfolio, including a $16 million real estate lease exposure. The airline leasing portfolio consists of $141 million to major U.S. carriers, $133 million to foreign airlines, and $63 million to U.S. regionals. In 2005, the industry continued to face the dilemma of an increasingly uncompetitive cost structure, weak demand with further downward pressure. In addition, considerable excess capacity and higher oil prices continue to negatively impact the valuations of the industry s aircraft in the secondary market. Because of these factors, the Company continues to maintain a sizable allowance for loan losses against these exposures and to closely monitor the portfolio. In 2005, the Company charged-off $140 million of a $153 million exposure to two bankrupt domestic airlines.

Consumer and Middle Market

The Company s consumer loan exposure is concentrated in the New York Tri-State region and consists primarily of loans secured by real estate and small business loans, as well as unsecured closed-end and open-end loans to individual consumers. These loans are originated through the Company s Private Client Services and Retail Banking businesses. The Company s middle market loan portfolio is very granular, with an average loan size of less than $2.5 million. It consists of loans to midsize companies, and focuses on users of cash management, trade finance, capital markets, and private client services.

Lease Financings

The Company utilizes the leasing portfolio as part of its tax cash flow management strategy. This portfolio generates attractive after-tax risk-adjusted returns. Counterparties in the leasing transactions are generally highly rated. The leasing portfolio consists of non-airline exposures of $5.2 billion and $337 million of airline exposures.

The non-airline portion of the leasing portfolio is backed by well-diversified assets, primarily large-ticket transportation equipment. The largest component is rail, consisting of both passenger and freight trains. Assets are both domestic and foreign-based, with primary concentrations in the United States and European countries. Excluding airline leasing, counterparty rating equivalents are as follows: 43% AA or better, 34% single A, 17% BBB, and 6% non-investment grade.

Commercial Real Estate

The Company s commercial real estate loan portfolio totaled $3.6 billion of exposure at December 31, 2005. Over 72% of the portfolio is secured by mortgages on properties predominantly located in the Tri-State region. The portfolio is diverse by project type with approximately 19% secured by office buildings, 33% secured by residential buildings, approximately 8% secured by retail buildings, while approximately 20% are unsecured loans to real estate investment trusts (REIT s) and approximately 20% fall into other categories.

The Company avoids speculative development loans and concentrates its activities largely within its retail branch network footprint. Real estate credit facilities are focused on experienced owners and are structured with moderate leverage based on existing cash flows.

International Loans

The Company is active in the international markets, particularly in areas associated with securities servicing and trade finance. Excluding leasing, these activities result in outstanding loans to foreign institutions of $5.5 billion and $4.8 billion at December 31, 2005 and 2004, respectively.

At December 31, 2005, the Company s emerging markets exposures consisted of $96 million in medium-term loans, $1,267 million in short-term loans, primarily trade related, and a $215 million investment in Wing

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Hang. In addition, the Company has $117 million of Philippine bonds whose principal payments are collateralized by U.S. Treasury zero coupon obligations and whose interest payments are partially collateralized. Emerging market countries where the Company has exposure include Argentina, Brazil, Bulgaria, China, Colombia, Costa Rica, Dominican Republic, Ecuador, Egypt, Honduras, Indonesia, Jamaica, Malaysia, Mexico, Morocco, Panama, Peru, Philippines, Russia, Thailand, Uruguay, Venezuela, and Vietnam.

Further details of the Company s outstandings are detailed under Loans .

Counterparty Risk Ratings Profile

The table below summarizes the risk ratings of the Company s foreign exchange and interest rate derivative counterparty credit exposure for the past year.

	For the Quarter Ended				
Rating(1)	**12/31/05**	**9/30/05**	**6/30/05**	**3/31/05**	**12/31/04**
AAA to AA-	74%	71%	68%	74%	68%
A+ to A-	13	13	15	13	19
BBB+ to BBB-	9	13	14	10	10
Noninvestment Grade	4	3	3	3	3
Total	100%	100%	100%	100%	100%

(1) Represents credit rating agency equivalent of internal credit ratings.

For derivative counterparty credit exposure see Commitments and Contingent Liabilities in the Notes to the Company s Consolidated Financial Statements.

Nonperforming Assets

Nonperforming assets decreased by $135 million to $79 million at December 31, 2005. The decrease in nonperforming assets during 2005 is primarily attributable to sales of the Company s exposure to a cable operator that was categorized as nonperforming as well as paydowns and charge-offs of commercial loans. See Loans in the Notes to the Consolidated Financial Statements.

Activity in Nonperforming Assets

	Year ended December 31,	
(In millions)	**2005**	**2004**
Balance at beginning of year	$ 214	$ 349
Additions	45	118
Charge-offs	(25)	(58)
Paydowns/Sales	(155)	(179)
Other		(16)
Balance at end of year	$ 79	$ 214

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The following table shows the distribution of nonperforming assets at the end of each of the last five years:

(Dollars in millions)	2005	2004	2003	2002	2001
Category of Loans:					
Domestic:					
Other Commercial	$ 17	$ 132	$ 219	$ 321	$ 138
Regional Commercial	35	53	51	34	18
Foreign	14	28	79	84	64
Total Nonperforming Loans	66	213	349	439	220
Other Assets Owned	13	1		1	2
Total Nonperforming Assets	$ 79	$ 214	$ 349	$ 440	$ 222
Nonperforming Asset Ratio	0.2%	0.7%	1.2%	1.4%	0.6%
Allowance for Loan Losses/Nonperforming Loans	629.7	277.5	191.2	149.2	188.7
Allowance for Loan Losses/Nonperforming Assets	524.0	276.5	191.2	148.9	187.0
Allowance for Credit Losses/Nonperforming Loans	865.4	345.6	230.2	189.1	280.0
Allowance for Credit Losses/Nonperforming Assets	720.2	344.3	230.2	188.7	277.6

Significant nonperforming assets at December 31, 2005 include $13 million related to aircraft leasing, $9 million of emerging markets exposure, and $8 million to a grocery retailer.

The following table shows loans past due 90 days or more and still accruing interest for the last five years:

(In millions)	2005	2004	2003	2002	2001
Domestic:					
Consumer	$ 7	$ 11	$ 14	$ 3	$ 3
Commercial	7	4	6	18	11
	14	15	20	21	14
Foreign:					
Banks				5	
	$ 14	$ 15	$ 20	$ 26	$ 14

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Activity in Allowance for Credit Losses

The following table details changes in the Company s allowance for credit losses for the last five years.

(Dollars in millions)	2005	2004	2003	2002	2001
Loans Outstanding, December 31,	$ 40,726	$ 35,781	$ 35,283	$ 31,340	$ 35,747
Average Loans Outstanding	39,682	37,778	35,623	34,305	38,770
Allowance for Credit Losses					
Balance, January 1					
Domestic	$ 590	$ 621	$ 653	$ 508	$ 491
Foreign	27	70	79	43	67
Unallocated	119	113	99	65	58
Total, January 1	736	804	831	616	616
Charge-Offs:					
Commercial	(144)	(24)	(118)	(396)	(345)
Foreign	(10)	(28)	(26)	(23)	(18)
Regional Commercial	(11)	(11)	(22)	(42)	(7)
Consumer	(30)	(30)	(32)	(23)	(18)
Total	(195)	(93)	(198)	(484)	(388)
Recoveries:					
Commercial	1	2	9	7	4
Foreign	2	3	1	2	5
Regional Commercial	2	2	3	2	1
Consumer	4	3	3	3	3
Total	9	10	16	14	13
Net Charge-Offs	(186)	(83)	(182)	(470)	(375)
Provision	15	15	155	685	375
Balance, December 31,					
Domestic	458	590	621	653	508
Foreign	11	27	70	79	43
Unallocated	96	119	113	99	65
Total, December 31,	$ 565	$ 736	$ 804	$ 831	$ 616
Allowance for Loan Losses	$ 411	$ 591	$ 668	$ 656	$ 415
Allowance for Lending-Related Commitments	154	145	136	175	201
Ratios					
Net Charge-Offs to Average Loans Outstanding	0.47%	0.22%	0.51%	1.37%	0.97%
Net Charge-Offs to Total Allowance for Credit Losses	32.92	11.28	22.64	56.56	60.88
Total Allowance for Credit Losses to Year-End Loans Outstanding	1.39	2.06	2.28	2.65	1.72
Allowance for Loan Losses to Year-End Loans Outstanding	1.01	1.65	1.89	2.09	1.16

Net charge-offs were $186 million in 2005, $83 million in 2004, and $182 million in 2003. In 2005, net charge-offs increased from 2004 primarily due to the charge-off of $140 million of leases with two bankrupt domestic airline customers in the fourth quarter of 2005. Net charge-offs decreased in 2004 and 2003 primarily due to improvement in asset quality.

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The provision for credit losses was $15 million in 2005, compared with $15 million in 2004 and $155 million in 2003. The decrease in the provision in 2004 primarily reflects the Company s improved risk profile as well as improvements in the credit environment. In 2005 and 2004, asset quality improved as nonperforming loans declined and loan granularity improved.

Allowance for Credit Losses

(Dollars in millions)	At December 31, 2005	2004
Margin Loans	$ 6,089	$ 6,059
Non-Margin Loans	34,637	29,722
Total Loans	$ 40,726	$ 35,781
Allowance for Loan Losses	$ 411	$ 591
Allowance for Lending-Related Commitments	154	145
Total Allowance for Credit Losses	$ 565	$ 736
Allowance for Loan Losses As a Percent of Total Loans	1.01%	1.65%
Allowance for Loan Losses As a Percent of Non-Margin Loans	1.19	1.99
Total Allowance for Credit Losses As a Percent of Total Loans	1.39	2.06
Total Allowance for Credit Losses As a Percent of Non-Margin Loans	1.63	2.48

The total allowance for credit losses was $565 million and $736 million at year-end 2005 and 2004, respectively. The ratio of the total allowance for credit losses to year-end non-margin loans was 1.63% and 2.48% at December 31, 2005 and 2004, reflecting improved credit quality in 2005. The decline in the allowance and in the ratios also reflects the charge-off of $153 million of airline credits which had $140 million of allowance for credit losses associated with them.

The Company has $6.1 billion of secured margin loans on its balance sheet at December 31, 2005. The Company has rarely suffered a loss on these types of loans and does not allocate any of its allowance for credit losses to these loans. The Company believes that the ratio of allowance for credit losses to non-margin loans is a more appropriate metric to measure the adequacy of the reserve.

Loans at December 31, 2005, were $40.7 billion compared with $35.8 billion at the prior year-end. Non-margin loans increased to $34.6 billion in 2005 from $29.7 billion in 2004, reflecting increased lending to financial institutions and higher holdings of residual mortgage loans. The decrease in the total allowance for credit losses in 2005 reflects a charge-off of $140 million related to airline exposure and continued improvement in credit quality.

The Company s total allowance at year-end equated to approximately 3.5 times the average charge-offs and 3.8 times the average net charge-offs for the last three years. Because historical charge-offs are not necessarily indicative of future charge-off levels, the Company also gives consideration to other risk indicators when determining the appropriate allowance level.

The allowance for loan losses and the allowance for lending-related commitments consist of four elements: (1) an allowance for impaired credits (nonaccrual commercial credits over $1 million); (2) an allowance for higher risk rated credits; (3) an allowance for pass rated credits; and (4) an unallocated allowance based on general economic conditions and risk factors in the Company s individual markets.

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The first element, impaired credits, is based on individual analysis of all nonperforming commercial credits over $1 million. The allowance is measured by the difference between the recorded value of impaired loans and their fair value. Fair value is either the present value of the expected future cash flows from the borrower, the market value of the loan, or the fair value of the collateral.

The second element, higher risk rated credits, is based on the assignment of loss factors for each specific risk category of higher risk credits. The Company rates each credit in its portfolio that exceeds $1 million and assigns the credits to specific risk pools. A potential loss factor is assigned to each pool, and an amount is included in the allowance equal to the product of the amount of the loan in the pool and the risk factor. Reviews of higher risk rated loans are conducted quarterly and the loan s rating is updated as necessary. The Company prepares a loss migration analysis and compares its actual loss experience to the loss factors on an annual basis to attempt to ensure the accuracy of the loss factors assigned to each pool. Pools of past due consumer loans are included in specific risk categories based on their length of time past due.

The third element, pass rated credits, is based on the Company s expected loss model. Borrowers are assigned to pools based on their credit ratings. The expected loss for each loan in a pool incorporates the borrower s credit rating, loss given default rating and maturity. The credit rating is dependent upon the borrower s probability of default. The loss given default incorporates a recovery expectation. Borrower and loss given default ratings are reviewed semi-annually at a minimum and are periodically mapped to third party, including rating agency and default and recovery data bases to ensure ongoing consistency and validity. Commercial loans over $1 million are individually analyzed before being assigned a credit rating. In 2004, the Company began to apply this technique to its leasing and consumer portfolios. In addition, the Company adjusted the estimates for default probabilities to a long-term average and adjusted from estimated to actual maturities. At the time of these changes, the impact was to increase the reserve requirement by $56 million. All current consumer loans are included in the pass rated consumer pools.

The fourth element, the unallocated allowance, is based on management s judgment regarding the following factors:

- Economic conditions including duration of the current cycle;
- Past experience including recent loss experience;
- Credit quality trends;
- Collateral values;
- Volume, composition, and growth of the loan portfolio;
- Specific credits and industry conditions;
- Results of bank regulatory and internal credit exams;
- Actions by the Federal Reserve Board;
- Delay in receipt of information to evaluate loans or confirm existing credit deterioration; and
- Geopolitical issues and their impact on the economy.

In 2005, the allowance for pass rated credits increased due to a slight increase in exposure and some downward credit migration, primarily in the automotive industry. This was more than offset by a decline in the allowance for impaired credits as several impaired credits were repaid or sold. The major portion of the overall decline in the allowance was due to a decline in reserve for higher risk credits as a result of the charge-offs taken on two bankrupt domestic airlines. The amount of allocated allowance decreased reflecting the continued relatively benign credit environment.

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Based on an evaluation of these four elements, including individual credits, historical credit losses, and global economic factors, the Company has allocated its allowance for credit losses as follows:

	2005	2004	2003	2002	2001
Domestic:					
Real Estate	2%	2%	2%	3%	6%
Commercial	69	71	73	74	73
Consumer	10	7	2	2	3
Foreign	2	4	9	9	7
Unallocated	17	16	14	12	11
	100%	100%	100%	100%	100%

Such an allocation is inherently judgmental, and the entire allowance for credit losses is available to absorb credit losses regardless of the nature of the loss.

The following table shows the maturity structure of the Company s commercial loan portfolio at December 31, 2005.

(In millions)	Within 1 Year	Between 1 and 5 Years	After 5 Years	Total
Domestic:				
Real Estate, Excluding Loans Collateralized by 1-4 Family Residential Properties	$ 263	$ 1,244	$ 511	$ 2,018
Commercial and Industrial Loans	2,212	3,619	440	6,271
Loans for Purchasing or Carrying Securities	4,800	135		4,935
Margin Loans	6,089			6,089
Other, Excluding Loans to Individuals and Those Collateralized by 1-4 Family Residential Properties	2,443	613	46	3,102
	15,807	5,611	997	22,415
Foreign	4,843	554	91	5,488
Total	$ 20,650	$ 6,165	$ 1,088	$ 27,903
Loans with:				
Predetermined Interest Rates	$ 5,291	$ 622	$ 266	$ 6,179
Floating Interest Rates	15,359	5,543	822	21,724
Total	$ 20,650	$ 6,165	$ 1,088	$ 27,903

Deposits

Total deposits were $64.4 billion in 2005, compared with $58.7 billion in 2004 and $56.4 billion in 2003. The increase was primarily due to higher market activity levels, which resulted in a higher level of customer deposits at year-end. The rise also reflects customers greater use of compensating balances in a rising rate environment. Noninterest-bearing deposits were $18.2 billion in 2005, compared with $17.4 billion in 2004 and $14.8 billion in 2003. Interest-bearing deposits were $46.2 billion in 2005, compared with $41.3 billion in 2004 and $41.6 billion in 2003.

The aggregate amount of deposits by foreign customers in domestic offices was $5.6 billion, $5.2 billion, and $4.1 billion at December 31, 2005, 2004, and 2003, respectively.

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The following table shows the maturity breakdown of domestic time deposits of $100,000 or more at December 31, 2005.

(In millions)	Certificates of Deposits	Other Time Deposits	Total
3 Months or Less	$ 769	$ 11,337	$ 12,106
Between 3 and 6 Months	429		429
Between 6 and 12 Months	996		996
Over 12 Months	1,906		1,906
Total	$ 4,100	$ 11,337	$ 15,437

Other Borrowed Funds

Federal funds purchased and securities sold under repurchase agreements were $834 million in 2005, compared with $1,205 million in 2004 and $1,039 million in 2003. Other borrowed funds were $860 million in 2005, compared with $533 million in 2004 and $834 million in 2003.

Information related to other borrowed funds in 2005, 2004, and 2003 is presented in the table below.

	2005		2004		2003	
(Dollars in millions)	Amount	Average Rate	Amount	Average Rate	Amount	Average Rate
Federal Funds Purchased and Securities Sold Under Repurchase Agreements						
At December 31	$ 834	3.04%	$ 1,205	0.91%	$ 1,039	0.69%
Average During Year	1,284	2.73	1,551	0.99	1,542	0.85
Maximum Month-End Balance During Year	3,349	4.19	4,173	0.92	2,436	0.75
Other						
At December 31	$ 860	3.07%	$ 533	2.13%	$ 834	1.15%
Average During Year	1,865	3.10	2,675	1.93	1,654	1.26
Maximum Month-End Balance During Year	1,414	2.52	2,052	2.98	1,415	0.95

Other consists primarily of commercial paper, extended federal funds purchased, and amounts owed to the U.S. Treasury.

LIQUIDITY

The Company maintains its liquidity through the management of its assets and liabilities, utilizing worldwide financial markets. The diversification of liabilities reflects the Company s efforts to maintain flexibility of funding sources under changing market conditions. Stable core deposits, including demand, retail time, and trust deposits from processing businesses, are generated through the Company s diversified network and managed with the use of trend studies and deposit pricing. The use of derivative products such as interest rate swaps and financial futures enhances liquidity by enabling the Company to issue long-term liabilities with limited exposure to interest rate risk. Liquidity also results from the maintenance of a portfolio of assets which can be easily sold and the monitoring of unfunded loan commitments, thereby reducing unanticipated funding requirements. Liquidity is managed on both a consolidated basis and also at The Bank of New York Company, Inc. parent company (Parent).

On a consolidated basis, non-core sources of funds such as money market rate accounts, certificates of deposit greater than $100,000, federal funds purchased and other borrowings were $13.1 billion and $14.6 billion on an average basis in 2005 and 2004, respectively. Average foreign deposits, primarily from the Company s European based securities servicing business, were $26.6 billion compared with $25.8 billion in 2004. Domestic

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savings and other time deposits were $10.1 billion on an average basis compared to $10.2 billion in 2004. Average payables to customers and broker-dealers declined to $6.0 billion from $6.4 billion. Long-term debt averaged $7.3 billion in 2005 and $6.2 billion in 2004.

The Company has entered into several modest securitization transactions. See Securitizations in the Notes to the Consolidated Financial Statements. These transactions have not had a significant impact on the Company s liquidity or capital.

The Parent s cash position was $791 million and $1,195 million at December 31, 2005 and 2004, respectively. The majority of these funds were deposited with the Bank of New York (The Bank). The Company s policy is to maintain sufficient cash for the Parent to be able to satisfy its obligations for one year without the need to access the capital markets or take a dividend from the Bank.

The Parent has four major sources of liquidity: dividends from its subsidiaries, the commercial paper market, a revolving credit agreement with third party financial institutions, and access to the capital markets.

In 2006, the Bank can pay dividends of approximately $278 million to the Parent without the need for regulatory waiver. This dividend capacity will increase in the remainder of 2006 to the extent of the Bank s net income less dividends. Nonbank subsidiaries of the Parent have liquid assets of approximately $264 million. These assets could be liquidated and the proceeds delivered by dividend or loan to the Parent.

Restrictions on the ability of the Company to obtain funds from its subsidiaries are discussed in more detail in the Company Financial Information in the Notes to the Consolidated Financial Statements.

In 2005 and 2004, the Parent s average commercial paper borrowings were $248 million and $155 million, respectively. Commercial paper outstandings were $85 million and $253 million at December 31, 2005 and 2004, respectively. At December 31, 2005, the Parent had cash of $791 million compared with cash of $1,195 million at December 31, 2004. Net of commercial paper outstanding, the Parent s cash position at December 31, 2005 was down $236 million to $706 million compared with December 31, 2004.

The Company has a back-up line of credit of $275 million with 14 financial institutions. This line of credit matures in October 2006. The fee on this facility depends on the Company s credit rating and is currently eight basis points. The credit agreement requires the Company to maintain: stockholders equity of $5 billion; a ratio of Tier 1 capital plus the allowance for credit losses to nonperforming assets of at least 2.5; a double leverage ratio less than 1.3; and all its banks adequately capitalized for regulatory purposes. There were no borrowings under the line of credit at December 31, 2005.

The Company also has the ability to access the capital markets. Access to the capital markets is partially dependent on the Company s credit ratings, which as of January 31, 2006 were as follows:

	Parent Commercial Paper	Parent Subordinated Long-Term Debt	Parent Senior Long-Term Debt	The Bank of New York Long-Term Deposits	Outlook
Standard & Poor s	A-1	A	A+	AA-	Stable
Moody s	P-1	A1	Aa3	Aa2	Stable
Fitch	F1+	A+	AA-	AA	Stable
Dominion Bond Rating Service	R-1(middle)	A(high)	AA(low)	AA	Stable

The Parent s major uses of funds are payment of dividends, principal and interest on its borrowings, acquisitions, and additional investment in its subsidiaries.

The Parent has $225 million of long-term debt that becomes due in 2006. In addition, the Parent has the option to call $229 million of subordinated debt in 2006, which it will call and refinance if market conditions are favorable. The Parent expects to refinance any debt it repays by issuing a combination of senior and subordinated debt.

The Company has $800 million of preferred trust securities that are callable in 2006. These securities qualify as Tier 1 Capital. The Company has not yet decided if it will call these securities. The decision to call will be based on interest rates, the availability of cash and capital, and regulatory conditions. If the Company calls the preferred trust securities, it expects to replace them with new preferred trust securities or senior or subordinated debt. See discussion of qualification of preferred trust securities as capital in Accounting Changes and New Accounting Pronouncements in the Notes to the Consolidated Financial Statements.

Double leverage is the ratio of investment in subsidiaries divided by the Company s consolidated equity plus preferred trust securities. The Company s double leverage ratio at December 31, 2005, 2004, and 2003 was 103.90%, 92.99%, and 100.24%, respectively. The Company s target double leverage ratio is a maximum of 120%. The double leverage ratio is monitored by regulators and rating agencies and is an important constraint on the Company s ability to invest in its subsidiaries to expand its businesses.

Pershing LLC, an indirect subsidiary of the Company, has committed and uncommitted lines of credit in place for liquidity purposes. The committed line of credit of $500 million with five financial institutions matures in March 2006. There were no borrowings against this line of credit in 2005. Pershing LLC has three separate uncommitted lines of credit amounting to $1 billion in aggregate. In 2005, average daily borrowing under these lines was $15 million in aggregate.

Pershing Limited, an indirect subsidiary of the Company, has committed and uncommitted lines in place for liquidity purposes. The committed line of credit of $275 million with four financial institutions matures in April 2006. In 2005, the average borrowing against this line of credit was $14 million. Pershing Limited has three separate uncommitted lines of credit amounting to $300 million in aggregate. In 2005, average daily borrowing under these lines was $200 million in aggregate.

The following comments relate to the information disclosed in the Consolidated Statements of Cash Flows.

Earnings and other operating activities used $1.1 billion in cash flows in 2005, compared with $3.4 billion and $3.8 billion provided in 2004 and 2003, respectively. The cash flows from operations in 2005, 2004 and 2003 were principally the result of earnings and changes in trading activities.

In 2005, cash used for investing activities was $7.6 billion as compared to $2.2 billion used for investing activities in 2004 and $6.5 billion used for investing activities in 2003. In 2005, 2004, and 2003, cash was used to increase the Company s investment securities portfolio, which is part of an ongoing strategy to shift the Company s asset mix from loans towards highly-rated investment securities and short-term liquid assets. Interest-bearing deposits were a use of funds in 2005, 2004, and 2003. Federal funds sold and securities purchased under resale agreements was a source of funds in 2005 and 2003 while it was a use of funds in 2004. Payments for the Pershing transaction were a significant use of cash in 2003.

In 2005, cash provided by financing activities was $8.1 billion as compared to $0.8 billion used for financing activities in 2004 and $1.8 billion provided by financing activities in 2003. In 2005, sources of funds included deposits, issuance of long-term debt and common stock. Payables to customers and broker-dealers were a significant use of funds in 2004. In 2003, the Company issued common stock and long-term debt to fund the Pershing acquisition as well as repay maturing long-term debt.

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COMMITMENTS AND OBLIGATIONS

The Company has contractual obligations to make fixed and determinable payments to third parties as indicated in the table below. The table excludes certain obligations such as trade payables and trading liabilities, where the obligation is short-term or subject to valuation based on market factors.

(In millions)		Payments Due by Period			
Contractual Obligations	Total	Less Than 1 Year	1-3 Years	4-5 Years	Over 5 Years
Deposits Without a Stated Maturity	$ 9,023	$ 9,023	$	$	$
Term Deposits	37,165	35,131	1,232	752	50
Federal Funds Borrowed and Securities Sold Under Repurchase Agreements	834	834			
Payables to Customer and Broker Dealers	8,623	8,623			
Other Borrowed Funds	860	860			
Long-Term Debt[(1)]	12,297	899	2,661	1,026	7,711
Operating Leases	1,157	183	306	196	472
Unfunded Pension and Post Retirement Benefits	234	37	47	47	103
Total Contractual Cash Obligations	$ 70,193	$ 55,590	$ 4,246	$ 2,021	$ 8,336

(1) Including Interest

The Company has entered into fixed and determinable commitments as indicated in the table below:

(In millions)		Amount of Commitment Expiration Per Period			
Other Commercial Commitments	Total Amounts Committed	Less Than 1 Year	1-3 Years	4-5 Years	Over 5 Years
Lending Commitments	$ 36,954	$ 10,391	$ 2,906	$ 5,386	$ 18,271
Standby Letters Of Credit	10,383	6,632	1,525	2,127	99
Commercial Letters Of Credit	1,189	1,121	33	32	3
Securities Lending Indemnifications	310,970	310,970			
Contingent Acquisitions Payments	195	126	67	2	
Investment Commitments[(1)]	312	89	91	9	123
Purchase Obligations	209	44	114	24	27
Total Commitments	$ 360,212	$ 329,373	$ 4,736	$ 7,580	$ 18,523

(1) Includes venture capital, community reinvestment act, and other investment-related commitments. Commitments to venture capital limited partnerships may extend beyond expiration period shown to cover certain follow-on investments, claims and liabilities, and organizational and partnership expenses.

OFF-BALANCE SHEET ARRANGEMENTS

Off-balance sheet arrangements required by regulation to be discussed in this section are limited to guarantees, retained or contingent interests, certain derivative instruments related to the Company s common stock, and obligations arising out of unconsolidated variable interest entities. For the Company, these items include certain credit guarantees and securitizations. Guarantees include lending-related guarantees issued as part of the Company s corporate banking business and securities lending indemnifications issued as part of the Company s servicing and fiduciary businesses.

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The Company has issued guarantees as indicated in the table below:

(In millions) Guarantees	Notional	Typical Revenue Based on Notional (Basis Points)
Corporate Banking		
Standby Letters of Credit	$ 10,383	5 - 135
Commercial Letters of Credit	1,189	15 - 75
Credit Derivatives	370	20 - 40
Securities Lending Indemnifications	310,970	4 - 6

The Company expects many of these guarantees to expire without the need to advance any cash. The revenue associated with guarantees frequently depends on the credit rating of the obligor and the structure of the transaction including collateral, if any. Advances under securities lending indemnifications would be secured by collateral.

The Company provides services to 6 QSPEs as of December 31, 2005. All of the Company s securitizations are QSPEs as defined by SFAS 140 which by design are passive investment vehicles, and are therefore not consolidated by the Company. See Securitizations in the Notes to the Consolidated Financial Statements.

CAPITAL RESOURCES

Shareholders equity was $9,876 million at December 31, 2005, compared with $9,290 million at December 31, 2004, and $8,428 million at December 31, 2003. During 2005, the Company retained $927 million of earnings. Accumulated other comprehensive income declined $128 million reflecting higher unrealized mark-to-market losses in the securities available-for-sale portfolio.

In 2005, the Company issued $285 million of callable medium-term subordinated notes bearing interest at rates from 5.00% to 5.90%. The notes are due in 2020 and 2030 and are callable by the Company after three to five years. The notes qualify as Tier II capital.

The Company also issued $500 million of non-callable subordinated notes due in 2015 and bearing interest at a rate of 4.95%. The notes qualify as Tier II capital.

In 2005, the Company issued $600 million of senior debt with an initial maturity date of April 4, 2006. The investors have the right to extend the maturity date on a monthly basis through March 10, 2015. If an investor does not extend the maturity date of the note, the note becomes payable in 13 months. The debt bears interest at a floating rate ranging from 1-month Libor minus 3 basis points at inception to 1-month Libor plus 2 basis points in 2015.

Also, in 2005, the Company issued $400 million of senior debt due in 2011 and bearing interest at a rate of 4.95%.

On February 27, 2006, indirect subsidiaries of the Company entered into a financing transaction (the Transaction) structured as a series of leases pursuant to which the Company s headquarters building and another office building it occupies in New York City (collectively, the Premises) were leased to a foreign financial institution (the Investor) pursuant to the terms of a lease (the Lease) between the Investor and an indirect subsidiary (the Subsidiary) of the Company. The Investor pre-paid rent under the Lease equal to the Euro equivalent of $527 million and subleased the Premises to The Bank of New York. Repayment of the $527 million and all other financial obligations under the Transaction documents are guaranteed by the Company.

The Company recorded the Transaction as long-term debt of $527 million bearing interest at a fixed Euro rate of 3.1% per annum and amortizing on a quarterly basis through 2031, unless terminated earlier.

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The arrangement can be terminated early by either the Subsidiary or the Investor upon the occurrence of certain events within the first two years. After the second anniversary of the transaction date the Investor may terminate the Lease at its discretion, and the Subsidiary may, at its discretion, discontinue paying operating expenses on the Premises, which would substantially reduce the yield to the Investor and induce the Investor to terminate the Lease.

During 2005, the Company called $94 million of higher rate debt and $110 million of debt matured. In 2005, long-term debt increased to $7,817 million from $6,121 million reflecting the transfer of Pershing from the Bank to the Parent.

The Company raised its common stock dividend to 21 cents per quarter in July 2005. In January 2006, the Company declared a quarterly common stock dividend of 21 cents per share. The Company has two shelf registrations with a remaining capacity of $1,257 million of debt, preferred stock, preferred trust securities, or common stock at December 31, 2005.

In 2004, the Company retained $832 million of earnings, restoring its tangible common equity ratio to its target range. In 2004, the Company issued $206 million of callable medium-term subordinated notes qualifying as Tier 2 capital, as well as $305 million of senior debt. During 2004, the Company called $175 million of higher rate debt, and $300 million of debt matured. Long-term debt was flat at $6,121 million.

In 2003, the Company retained $594 million of earnings. In connection with the acquisition of Pershing, the Company sold 40 million common shares for $996 million. The Company also issued $400 million of non-callable subordinated notes and $239 million of callable medium-term subordinated notes qualifying as Tier 2 capital. In addition, the Company issued $1,281 million of senior debt. The increased long-term debt replaced subordinated debt ceasing to qualify as Tier 2 capital, $525 million of higher rate debt that the Company called during 2003, $710 million of debt that matured in 2003, and provided funding for the Pershing acquisition.

Regulators establish certain levels of capital for bank holding companies and banks, including the Company and the Bank, in accordance with established quantitative measurements. For the Parent to maintain its status as a financial holding company, the Bank must qualify as well capitalized. In addition, major bank holding companies such as the Parent are expected by the regulators to be well capitalized. As of December 31, 2005 and 2004, the Company and the Bank were considered well capitalized on the basis of the ratios (defined by regulation) of Total and Tier 1 capital to risk-weighted assets and leverage (Tier 1 capital to average assets), which are shown as follows:

	December 31, 2005		December 31, 2004				
	Company	Bank	Company	Bank	Company Targets	Well Capitalized Guidelines	Adequately Capitalized Guidelines
Tier 1*	8.38%	8.88%	8.31%	7.07%	7.75%	6%	4%
Total Capital**	12.48	11.84	12.21	11.41	11.75	10	8
Leverage	6.60	7.05	6.41	5.45		5	3-5
Tangible Common Equity	5.58	6.62	5.56	5.24	5.00-5.25%	N.A.	N.A.

* Tier 1 capital consists, generally, of common equity, preferred trust securities, and certain qualifying preferred stock, less goodwill and most other intangibles.

** Total Capital consists of Tier 1 capital plus Tier 2 capital. Tier 2 capital consists, generally, of certain qualifying preferred stock and subordinated debt and a portion of the loan loss allowance.

If a bank holding company or bank fails to qualify as adequately capitalized , regulatory sanctions and limitations are imposed.

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At December 31, 2005, the amounts of capital by which the Company and the Bank exceed the well capitalized guidelines are as follows:

(In millions)	Company	Bank
Tier 1 Capital	$ 1,886	$ 1,950
Total Capital	1,970	1,244
Leverage	1,610	1,749

In 2005, the Company bought back a net 5 million shares of which 1 million shares were part of the newly announced buyback program of 20 million shares, leaving 19 million shares authorized for repurchase at December 31, 2005.

In 2006, the Company will balance its acquisition initiatives with continued buyback activity. The Company is also factoring in the use of capital for completion of the Alcentra and Urdang acquisitions, growth in the balance sheet, and the proposed change in lease accounting. Currently, the Company expects a net share reduction in a comparable range to the 5 million share reduction in 2005.

In the first quarter of 2005, ownership of Pershing was transferred from The Bank of New York to the parent company, The Bank of New York Company, Inc. In connection with the transfer, the Company issued $1.1 billion of debt of which $500 million qualified as Tier 2 Capital.

The following table presents the components of the Company s risk-based capital at December 31, 2005 and 2004:

(In millions)		2005	2004
Common Stock		$ 9,876	$ 9,290
Preferred Trust Securities		1,150	1,150
Adjustments:	Intangibles	(4,426)	(4,265)
	Securities Valuation Allowance	51	(51)
	Merchant Banking Investments	(8)	(6)
Tier 1 Capital		6,643	6,118
Qualifying Unrealized Equity Security Gains			
Qualifying Subordinated Debt		2,690	2,149
Qualifying Allowance for Loan Losses		565	729
Tier 2 Capital		3,255	2,878
Total Risk-based Capital		$ 9,898	$ 8,996

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The following table presents the components of the Company s risk-adjusted assets at December 31, 2005 and 2004:

	2005		2004	
(In millions)	**Balance sheet/ notional amount**	**Risk adjusted balance**	**Balance sheet/ notional amount**	**Risk adjusted balance**
Assets				
Cash, Due From Banks and Interest-Bearing Deposits in Banks	$ 12,159	$ 2,121	$ 12,078	$ 1,918
Securities	27,326	6,555	23,802	6,578
Trading Assets	5,930		4,627	
Fed Funds Sold and Securities Purchased Under Resale Agreements	2,425	169	5,708	752
Loans	40,726	33,748	35,781	30,900
Allowance for Loan Losses	(411)		(591)	
Other Assets	13,919	10,455	13,124	8,853
Total Assets	$ 102,074	53,048	$ 94,529	49,001
Off-Balance Sheet Exposures				
Commitments to Extend Credit	$ 37,005	$ 12,979	$ 36,836	$ 11,966
Securities Lending	310,970	222	232,184	977
Standby Letters of Credit and Other Guarantees	13,703	10,762	12,626	9,464
Interest Rate Contracts	695,874	1,271	565,908	1,149
Foreign Exchange Contracts	94,535	575	93,850	623
Total Off-Balance Sheet Exposures	$ 1,152,087	25,809	$ 941,404	24,179
Market Risk Equivalent Assets		426		488
Allocated Transfer Risk Reserve		(1)		(7)
Risk-Adjusted Assets		$ 79,282		$ 73,661

CAPITAL FRAMEWORK

The U.S. federal bank regulatory agencies risk capital guidelines are based upon the 1988 Capital Accord of the Basel Committee on Banking Supervision (the Basel Committee). The Basel Committee is a committee of central banks and bank supervisors of the major industrialized countries that develop broad policy guidelines with respect to bank supervisory policies. The Basel Committee issued, in June 2004, and updated in November 2005 a revised framework for capital adequacy commonly known as the New Accord (New Accord) or Basel II (Basel II) that would set capital requirements for operational risk and refine the existing capital requirements for credit risk. Operational risk would be defined as the risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems, or from external events. Capital measurement for credit risk under the revised framework would differentiate capital levels based upon the risk characteristics of the underlying exposures. The Basel Committee proposal outlines several alternatives for capital assessment of credit and operational risks. The Basel Committee requires two years of impact analysis and parallel testing for banks adopting the advanced approaches under the New Accord, with implementation extended until year-end 2007.

U.S. Implementation of Basel II

In the United States, U.S. regulators are mandating the adoption of the New Accord by banks, such as The Bank of New York, which are considered internationally active or critical to the U.S. payments system. The only approach available to these mandated banks under the New Accord is the Advanced Internal Ratings Based (AIRB) approach for credit risk and the Advanced Measurement Approach (AMA) for operational risk.

In June 2004 the U.S. federal bank regulatory agencies published a joint release describing proposed Basel II revisions to capital adequacy standards based on the AIRB and AMA approaches. The regulatory agencies have also published draft implementation guidance addressing a number of issues. During 2005, the U.S. federal bank regulatory agencies indicated that the publication of a formal notice of proposed rulemaking setting forth the details of the AIRB and AMA approaches for internationally active banking organizations would be delayed until the first quarter of 2006. During this interim period pending publication and ultimate adoption of new rules, banks that will adopt the new rules in the U.S. are relying upon the current proposal.

The Bank has been relying upon the current proposal the Advanced Notice Proposed Rulemaking and draft guidance to prepare its implementation strategies. Additionally, the Bank and other mandated banks have been coordinating with international regulatory agencies responsible for supervising the implementation of Basel II at foreign subsidiaries. Jurisdictions outside of the United States are adhering to the original implementation schedule outlined in the New Accord, namely a parallel run of Basel I and Basel II capital calculations by January 2007.

Banking organizations that are not internationally active banking organizations may choose to adopt the AIRB/AMA approaches of the New Accord or they may calculate regulatory capital according to current rules based on the 1988 Accord, subject to revisions to those rules that may be implemented. In October 2005 the U.S. federal bank regulatory agencies published proposed revisions to existing capital guidelines that would apply to these banking organizations and that are based on the so-called standardized approach in Basel II. The comment period for these proposals expired on January 18, 2006. The regulators have indicated that the AIRB/AMA provisions for internationally active banking organizations and these provisions for others will become effective on similar time frames.

Both the terms and timing of implementation of Basel II are the subject of considerable controversy among both the bank regulators and Congress. Accordingly, it is not possible to predict the timing or ultimate terms of implementation of Basel II.

The Company s Implementation

Since June 2004, the Company s Basel Project Management Office (Basel PMO) has been managing the Company s implementation of the AIRB and AMA approach under the New Accord. The Basel PMO s primary responsibilities include managing the development of the systems infrastructure to facilitate the data collection and retention requirements under the New Accord and ensuring the Company satisfies the AIRB qualification requirements of the New Accord. The Company believes it is currently in compliance with the requirements of the AMA.

The Company has assigned 24 full-time staff members to the effort and has retained a team of consultants to assist with the systems infrastructure development effort. The estimated cost of implementation to the Company is approximately $30 million and is slated for completion in 2006 to meet both the U.S. and international regulatory agencies implementation schedules.

The Basel PMO is nearing completion of its systems infrastructure development effort. It has built the core data warehouse to store the credit risk data necessary to calculate regulatory capital. The Company will begin populating the warehouse with data in the first quarter of 2006 and will be ready to test Basel II capital calculations shortly thereafter. The Basel PMO has also completed the design of validation methodologies for its parameter estimates and has documented the development of the Company s validation methodologies. The Company has engaged in active discussion with U.S. regulators during the design of these methodologies to help facilitate a smooth transition during the Basel II qualification process.

Basel II Impact on the Company

The Company has participated in four quantitative impact studies with banking regulators to assess the impact of the New Accord. Based on the results of the Fourth Quantitative Impact Study, which used June 30, 2004 data, the Company believes that the New Accord, as currently envisioned, like the current capital requirements under Basel I, will not constrain its current business practices.

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RISK MANAGEMENT

The major risks to which the Company is exposed are credit, market (primarily interest rate and foreign exchange) and operational risk. Risk management and oversight begins with the Board of Directors and two key Board committees: the Audit and Examining Committee and the Risk Committee.

The Risk Committee meets on a regular basis to review the Company s risks, policies, and risk management activities. The delegation of policy formulation and day-to-day oversight is to the Company s Chief Risk Policy Officer, who, together with the Chief Auditor and Chief Compliance Officer helps ensure an effective risk management structure.

The Audit & Examining Committee of the Board of Directors (the A&E Committee) is comprised of independent directors, all of whom have been determined by the Board to have financial expertise, as defined under SEC regulations. The A&E Committee meets on a regular basis to perform, among other things, an oversight review of the integrity of the Company s financial statements and financial reporting process, compliance with legal and regulatory requirements, the independent public accountant s qualifications and independence, and the performance of the independent public accountant and the Company s internal audit function. The A&E Committee also reviews management s assessment of the adequacy of internal controls. The functions of the A&E Committee are described in more detail in its charter, a copy of which is available on the Company s website, www.bankofny.com.

The Company s risk management framework is designed to:

- Provide that risks are identified, monitored, reported, and priced properly;
- Define and communicate the types and amount of risks to take;
- Communicate to the appropriate level within the Company the type and amount of risk taken;
- Maintain a risk management organization that is independent of the risk taking activities; and
- Promote a strong risk management culture that encourages a focus on risk-adjusted performance.

Credit Risk Management

Credit risk is the possible loss the Company would suffer if any of its borrowers or other counterparties were to default on their obligations to the Company. Credit risk arises primarily from lending, trading, and securities servicing activities. To balance the value of its activities with the credit risk incurred in pursuing them, the Company sets and monitors internal credit limits for activities that entail credit risk, most often on the size of the exposure and the maximum maturity of credit extended. For credit exposures, driven by changing market rates and prices, exposure measures include an add-on for such potential changes.

The Company manages credit risk at both the individual exposure level as well as at the portfolio level. Credit risk at the individual exposure level is managed through the Company s credit approval system of Divisional Portfolio Managers (DPMs) and Senior Credit Officers (SCOs). The DPMs and SCOs are responsible for approving the size, terms and maturity of all credit exposures as well as the ongoing monitoring of the exposures. In addition, they are responsible for assigning and maintaining the risk ratings on each exposure. The Credit Risk Review area regularly examines the credit portfolio to determine compliance with approval policies.

Credit risk at the portfolio level is managed by the Portfolio Management Division (PMD). The PMD is responsible for calculating two fundamental credit measures. First, the Company projects a statistically expected credit loss, used to help determine the appropriate loan loss reserve and to measure customer profitability. Expected loss considers three basic components: the estimated size of the exposure whenever default might occur, the probability of default before maturity, and the severity of the loss the Company would incur, commonly called loss given default. For corporate banking, where most of the Company s credit risk is

created, unfunded commitments are assigned a usage given default percentage. Borrowers/Counterparties are assigned ratings by DPMs and SCOs on an 18-grade scale, which translates to a scaled probability of default. Additionally, transactions are assigned loss-given-default ratings (on a 12-grade scale) that reflect the transactions structure including the effects of guarantees, collateral, and relative seniority of position.

The second fundamental measurement of credit risk calculated by the PMD is called economic capital. The Company s economic capital model estimates the capital required to support the overall credit risk portfolio. Using a Monte Carlo simulation engine and measures of correlation among borrower defaults, the economic model examines extreme and highly unlikely scenarios of portfolio credit loss in order to estimate credit related capital, and then allocates that capital to individual borrowers and exposures. Credit related capital calculation supports a second tier of policy standards and limits by serving as an input to both profitability analysis and concentration limits of capital at risk with any one borrower, country or industry.

The PMD is responsible for the calculation methodologies and the estimates of the inputs used in those methodologies for the determination of expected loss and economic capital. These methodologies and input estimates are regularly evaluated to insure their appropriateness and accuracy. As new techniques and data become available, the PMD attempts to incorporate, where appropriate, those techniques or data.

Credit risk is intrinsic to much of the banking business and necessary to its smooth functioning. However, the Company seeks to limit both on and off-balance sheet credit risk through prudent underwriting and the use of capital only where risk-adjusted returns warrant. The Company seeks to manage risk and improve its portfolio diversification through syndications, asset sales, credit enhancements, credit derivatives, and active collateralization and netting agreements. In addition, the Company has a separate Credit Risk Review group made up of experienced loan review officers who perform timely reviews of the loan files and credit ratings assigned to the loans.

Market Risk Management

Market risk is the risk of loss due to adverse changes in the financial markets. Market risk arises from derivative financial instruments, such as futures, forwards, swaps and options, and other financial instruments, including loans, securities, deposits, and other borrowings. The Company s market risks are primarily interest rate and foreign exchange risk and, to a lesser extent, equity and credit risk.

The Company s market risk governance structure includes two committees comprised of senior executives who review market risk activities, risk measurement methodologies, and risk limits; approve new products; and provide direction for the Company s market risk profile. The Asset/Liability Management Committee oversees the market risk management process for interest rate risk related to asset/liability management activities. The Market Risk Management Committee oversees the market risk management process for trading activities, including foreign exchange risk. Both committees are supported by a comprehensive risk management process that is designed to help identify, measure, and manage market risk, as discussed under Trading Activities and Risk Management and Asset/Liability Management below and in Fair Value of Financial Instruments in the Notes to the Consolidated Financial Statements.

The information presented that follows with respect to market risk is forward looking information. As such it is subject to risks and uncertainties that could cause actual results to differ materially from projected results discussed in this Report. These include adverse changes in market conditions, the timing of such changes and the actions that management could take in response to these changes as well as the additional factors discussed under Forward Looking Statements and Risk Factors That Could Affect Future Results .

Trading Activities and Risk Management

The Company s trading activities are focused on acting as a market maker for the Company s customers. The risk from these market making activities and from the Company s own positions is managed by the Company s traders and limited in total exposure as described below.

The Company manages trading risk through a system of position limits, a value at risk (VAR) methodology based on a Monte Carlo simulation, stop loss advisory triggers, and other market sensitivity measures. Risk is monitored and reported to senior management by a separate unit on a daily basis. Based on certain assumptions, the VAR methodology is designed to capture the potential overnight pre-tax dollar loss from adverse changes in fair values of all trading positions. The calculation assumes a one-day holding period for most instruments, utilizes a 99% confidence level, and incorporates the non-linear characteristics of options. The VAR model is used to calculate economic capital which is allocated to the business units for computing risk-adjusted performance.

As VAR methodology does not evaluate risk attributable to extraordinary financial, economic or other occurrences, the risk assessment process includes a number of stress scenarios based upon the risk factors in the portfolio and management s assessment of market conditions. Additional stress scenarios based upon historic market events are also tested. Stress tests by their design incorporate the impact of reduced liquidity and the breakdown of observed correlations. The results of these stress tests are reviewed weekly with senior management.

The following table indicates the calculated VAR amounts for the trading portfolio for the years ending December 31, 2005 and 2004.

(In millions)	**2005**				**2004**			
Market Risk	**Average**	**Minimum**	**Maximum**	**12/31/05**	**Average**	**Minimum**	**Maximum**	**12/31/04**
Interest Rate	$ 2.7	$ 1.8	$ 4.6	$ 2.8	$ 3.8	$ 1.4	$ 7.8	$ 4.0
Foreign Exchange	1.5	0.4	4.1	0.9	0.9	0.2	3.1	0.9
Equity	0.6	0.3	1.1	0.8	1.1	0.5	2.8	0.7
Credit Derivatives	1.4	0.7	2.1	0.9	1.9	1.4	2.3	2.0
Diversification	(1.2)	NM	NM	(1.1)	(1.4)	NM	NM	(1.3)
Overall Portfolio	5.0	3.1	9.1	4.3	6.3	3.6	12.8	6.3

NM Because the minimum and maximum may occur on different days for different risk components, it is not meaningful to compute a portfolio diversification effect.

During the year 2005, interest rate risk generated 41% of average VAR, credit derivatives generated 28% of average VAR, foreign exchange accounted for 22% of average VAR, and equity generated 9% of average VAR. During 2005, the Company s daily trading loss did not exceed the Company s calculated VAR amounts on any given day.

Asset/Liability Management

The Company s asset/liability management activities include lending, investing in securities, accepting deposits, raising money as needed to fund assets, and processing securities and other transactions. The market risks that arise from these activities are interest rate risk and, to a lesser degree, foreign exchange risk. The Company s primary market risk is exposure to movements in U.S. dollar interest rates. Exposure to movements in foreign currency interest rates also exists but to a significantly lower degree. The Company actively manages interest rate sensitivity. In addition to gap analysis, the Company uses earnings simulation and discounted cash flow models to identify interest rate exposures.

An earnings simulation model is the primary tool used to assess changes in pre-tax net interest income. The model incorporates management s assumptions regarding interest rates, balance changes on core deposits, changes in the prepayment behavior of loans and securities, and the impact of derivative financial instruments used for interest rate risk management purposes. These assumptions have been developed through a combination of historical analysis and future expected pricing behavior. These assumptions are inherently uncertain, and, as a result, the earnings simulation model cannot precisely estimate net interest income or the impact of higher or lower interest rates on net interest income. Actual results may differ from projected results due to timing, magnitude and frequency of interest rate changes and changes in market conditions and management s strategies, among other factors.

The Company evaluates the effect on earnings by running various interest rate ramp scenarios up and down from a baseline scenario, which assumes no changes in interest rates. These scenarios are reviewed to examine the impact of large interest rate movements. Interest rate sensitivity is quantified by calculating the change in pre-tax net interest income between the scenarios over a 12 month measurement period. The measurement of interest rate sensitivity is the percentage change in net interest income as shown in the following table:

	Estimated Changes in Net Interest Income December 31, 2005	
	(In millions)	%
+200 basis point Ramp vs. Stable Rate	$ (65)	(3.2)%
+100 basis point Ramp vs. Stable Rate	(29)	(1.4)
-100 basis point Ramp vs. Stable Rate	(8)	(0.4)
-200 basis point Ramp vs. Stable Rate	(32)	(1.6)

The base case scenario fed funds rate in the December 31, 2005 analysis was 4.25%. The 100+ basis point ramp scenario assumes short-term rates rise 25 basis points in each of the next four quarters, while the 200+ ramp scenario assumes a 50 basis point per quarter increase. The 100+ basis point December 31, 2005 scenario assumes a steepening of the yield curve with 10-year rates rising 114 basis points. The 200+ basis point December 31, 2005 scenario assumes a slight steepening of the yield curve with 10-year rates rising 214 basis points. These scenarios do not reflect strategies that management could employ to limit the impact as interest rate expectations change.

The above table relies on certain critical assumptions, including depositors behavior related to interest rate fluctuations and the prepayment and extension risk in certain of the Company s assets. In addition, if interest rates decline, the Company s portfolio of mortgage-related assets would have reduced returns if the borrowers pay off their mortgages earlier than anticipated. To the extent that actual behavior is different from that assumed in the models, there could be a change in interest rate sensitivity.

The Company also projects future cash flows from its assets and liabilities over a long-term horizon and then discounts these cash flows using the same assumptions noted above. The aggregation of these discounted cash flows is the Economic Value of Equity (EVE). The following table shows how the EVE would change in response to changes in interest rates:

Rate Change	Estimated Change in EVE December 31, 2005 (In millions)
+200 basis point Ramp vs. Stable Rate	$ 42
+100 basis point Ramp vs. Stable Rate	56
-100 basis point Ramp vs. Stable Rate	(56)
-200 basis point Ramp vs. Stable Rate	(176)

These results do not reflect strategies that management could employ to limit the impact as interest rate expectations change.

The asymmetrical accounting treatment of the impact of a change in interest rates on the Company s balance sheet may create a situation in which an increase in interest rates can adversely affect reported equity and regulatory capital, even though economically there may be no impact on the economic capital position of the Company. For example, an increase in rates will result in a decline in the value of the Company s fixed income investment portfolio, which will be reflected through a reduction in other comprehensive income in the Company s shareholders equity, thereby affecting the tangible common equity (TCE) ratio. Under current accounting rules, there is no corresponding change on the Company s fixed liabilities, even though economically these liabilities are more valuable as rates rise.

The Company projects the impact of this change using the same interest rate ramp up assumptions described earlier and comparing the projected mark-to-market on the investment securities portfolio at December 31, 2005, under the higher rate environments versus a stable rate scenario. The table below shows the impact of a change in interest rates on the TCE ratio:

Rate Change	Estimated Change in TCE ratio December 31, 2005 (In basis points)
+200 basis point Ramp vs. Stable Rate	(40)
+100 basis point Ramp vs. Stable Rate	(19)
-100 basis point Ramp vs. Stable Rate	13
-200 basis point Ramp vs. Stable Rate	19

These results do not reflect strategies that management could employ to limit the impact as interest rate expectations change.

To manage foreign exchange risk, the Company funds foreign currency-denominated assets with liability instruments denominated in the same currency. The Company utilizes various foreign exchange contracts if a liability denominated in the same currency is not available or desired, and to minimize the earnings impact of translation gains or losses created by investments in overseas markets. The foreign exchange risk related to the interest rate spread on foreign currency-denominated asset/liability positions is managed as part of the Company s trading activities. The Company uses forward foreign exchange contracts to protect the value of its net investment in foreign operations. At December 31, 2005, net investments in foreign operations totaled approximately $1,589 million and were spread across 13 foreign currencies.

Operational Risk

Overview

Operational risk is the risk of loss resulting from inadequate or failed internal processes, human factors and systems, or from external events.

In providing securities servicing, global payment services, asset management, and traditional banking and trust services, the Company is exposed to operational risk. Operational risk may result from, but is not limited to, errors related to transaction processing, breaches of the internal control system and compliance requirements, and the risk of fraud by employees or persons outside the corporation or business interruption due to system failures or other events. The risk of loss from operational risk also includes potential legal or regulatory actions that could arise as a result of noncompliance with applicable laws and/or regulatory requirements. As discussed in Certain Regulatory Considerations , the Company is subject to a very comprehensive and frequently changing regulatory scheme.

In the event of an operational event, the Company could suffer financial loss, face regulatory or law enforcement action and/or suffer damage to its reputation.

To address this risk, the Company maintains comprehensive policies and procedures and an internal control framework designed to provide a sound operational environment. These controls have been designed to manage operational risk at appropriate levels given the Company s financial strength, the business environment and markets in which it operates, the nature of its businesses, and considering factors such as competition and regulation. The Company s internal auditors monitor and test the overall effectiveness of the internal control and financial reporting systems on an ongoing basis.

The Company has also established procedures that are designed to ensure that policies relating to conduct, ethics and business practices are followed on a uniform basis. Among the procedures designed to ensure effectiveness are the Company s Code of Conduct , Know Your Customer , and compliance training programs.

Operational Risk Management

The Company has established operational risk management as an independent risk discipline. The Operational Risk Management (ORM) group reports to the Chief Risk Policy Officer. The organizational framework for operational risk is based upon a strong risk culture that incorporates both governance and risk management activities comprising:

Board Oversight and Governance The Company has established a Risk Committee of the Board that approves and oversees the Company s operational risk management strategy in addition to credit and market risk. The Committee meets regularly to review and approve operational risk management initiatives, discuss key risk issues, and review the effectiveness of the risk management systems.

Business Line Accountability Business managers are responsible for maintaining an effective system of internal controls commensurate with their risk profiles and in accordance with Company policies and procedures.

ORM group The ORM group is responsible for developing risk management policies and tools for assessing, monitoring, and measuring operational risk for the Company. The primary objectives of the ORM group are to promote effective risk management, create incentives for generating continuous improvement in controls, optimize capital, and improve shareholder value.

Key elements of the operational risk management function include systems to measure, monitor, and allocate economic capital to the business units for operational risks.

Global Compliance

The Company s global compliance function provides leadership, guidance, and oversight to help business units identify applicable laws and regulations and implement effective measures to meet the specific requirements. Compliance attempts to take a proactive approach by anticipating evolving regulatory standards and remaining aware of industry best practices, legislative initiatives, competitive issues, and public expectations and perceptions. The function uses its global reach to disseminate information about compliance-related matters throughout the Company. The Chief Compliance Officer reports to the General Counsel, is a member of all critical Corporate committees, and provides routine updates to the Audit and Examining Committee of the Board.

Internal Audit

The Company s internal audit function employs over 190 professionals globally. The group reports directly to the Audit & Examining Committee of the Company. Internal Audit utilizes a risk based approach to its audit approach covering the risks in the operational, compliance, regulatory, technology, fraud, processing and other key risks areas of the Company. Internal Audit has unrestricted access to the Company and regularly participates in all key committees of the Company. In addition, Internal Audit has established an active monitoring program to ensure that the risk based audit program is continually being enhanced for current issues and events.

Business Continuity

The Company has prepared for events that could damage the Company s physical facilities, cause delay or disruptions to operational functions, including telecommunications networks, or impair the Company s clients, vendors, and counterparties. Key elements of the Company s business continuity strategies are extensive planning and testing, and diversity of business operations, data centers and telecommunications infrastructure.

The Company has established multiple geographically diverse locations for its funds transfer and broker-dealer services operations, which have redundant full functionality to assure uninterrupted processing. The Company s mutual fund accounting and custody, securities operations, securities lending, corporate trust, master trust, UIT, stock transfer, and treasury have common functionality in multiple sites designed to facilitate recovery within 24 hours. In addition, the Company has recovery positions outside downtown Manhattan for over 5,000 employees.

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The Company has continued to develop geographic diversity outside Manhattan by moving additional personnel to growth centers outside New York City, and by establishing its primary data center in the U.S. mid-South region in late 2005.

The Company replicates 100% of its critical production computer data to its recovery data center, which is at a distance of well over 500 miles from its primary data center.

In the telecommunications area, the Company uses multiple central office sites, with a fiber optic relay network backed up by T-3 lines to ensure the continuity of its voice and data communications. In addition, primary customer connectivity has been moved outside of New York City and back-up lines are generally leased rather than dial-up. The Company has an active program to test customer back-up connections.

In May 2003, the Federal Reserve published the Interagency Paper, Sound Practices to Strengthen the Resilience of the U.S. Financial System (Interagency Paper). The purpose of the document was to define the guidelines for the financial services industry and other interested parties regarding best practices related to business continuity planning. The Interagency Paper identified the Company as a core clearing and settlement organization required to meet a higher standard for business continuity. Significant areas impacting the Company include the proximity of production to contingency sites for technology processing and business operations, technology recovery, recovery timeframes, regional diversification, definition of critical functions in financial services, and timetables for implementing best practices.

The Company is committed to meeting or exceeding all of the requirements. As a core clearing and settlement organization, the Company believes that it is at the forefront of the industry in improving its business continuity practices. Acceleration of the implementation of this plan resulted in overlap costs of $26 million which will phase out over 2006 and 2007. With the Company s new primary data center having become operational in late 2005, the Company believes it has met substantially all of the requirements.

The Company is committed to ensuring that requirements for business continuity are met not just within its own data centers, but also within the facilities of those vendors and service providers whose operation is critical to the Company s safety and soundness. To that end, the Company has a Service Provider Management Office whose function is to ensure that new and existing service providers and vendors meet the Company s standards for business continuity, as well as information security, financial stability, personnel practices, etc.

Although the Company is committed to observing best practices as well as meeting regulatory requirements, geopolitical uncertainties and other external factors will continue to create risk that cannot always be identified and anticipated.

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STATISTICAL INFORMATION

Average Balances and Rates on a Tax Equivalent Basis

	2005			2004			2003		
(Dollars in millions)	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
Assets									
Interest-Bearing Deposits in Banks (Primarily Foreign)	$ 8,996	$ 274	3.04%	$ 11,675	$ 305	2.62%	$ 6,690	$ 150	2.24%
Federal Funds Sold and Securities Purchased Under Resale Agreements	4,685	142	3.03	6,562	80	1.22	7,326	79	1.07
Margin Loans	6,403	267	4.17	6,342	156	2.46	3,795	86	2.27
Non-Margin Loans									
Domestic Offices									
Consumer	5,648	347	6.15	4,598	233	5.06	4,069	223	5.47
Commercial	17,157	704	4.10	17,255	566	3.28	16,389	632	3.86
Foreign Offices	10,474	454	4.33	9,583	283	2.95	11,370	332	2.93
Non-Margin Loans	33,279	1,505*	4.52	31,436	1,082*	3.44	31,828	1,187*	3.73
Securities									
U.S. Government Obligations	273	9	3.43	415	11	2.58	323	11	3.12
U.S. Government Agency Obligations	3,766	153	4.05	3,853	128	3.33	3,516	128	3.66
Obligations of States and Political Subdivisions	215	15	6.95	229	17	7.41	329	23	6.94
Other Securities									
Domestic Offices	19,066	784	4.11	17,101	593	3.47	14,597	529	3.62
Foreign Offices	1,882	83	4.44	1,354	59	4.36	1,085	42	3.91
Total Other Securities	20,948	867	4.14	18,455	652	3.53	15,682	571	3.64
Trading Securities									
Domestic Offices	593	22	3.77	584	16	2.72	587	15	2.55
Foreign Offices	2,956	131	4.45	1,510	36	2.41	4,018	115	2.85
Total Trading Securities	3,549	153	4.34	2,094	52	2.50	4,605	130	2.81
Total Securities	28,751	1,197	4.16	25,046	860	3.43	24,455	863	3.53
Total Interest-Earning Assets	82,114	$ 3,385	4.12%	81,061	$ 2,483	3.06%	74,094	$ 2,365	3.19%
Allowance for Credit Losses	(574)			(623)			(672)		
Cash and Due from Banks	3,357			3,151			2,834		
Other Assets	16,538			15,751			15,211		
Total Assets	$ 101,435			$ 99,340			$ 91,467		
Assets Attributable to Foreign Offices **	26.27%			26.47%			29.09%		

Tax equivalent adjustments were $29 million in 2005, $30 million in 2004, and $35 million in 2003, and are based on the federal statutory tax rate (35%) and applicable state and local taxes.

* Includes fees of $69 million in 2005, $95 million in 2004, and $88 million in 2003. Nonaccrual loans are included in the average loan balance; the associated income, recognized on the cash basis, is included in interest.

** Includes Cayman Islands branch office.

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Average Balances and Rates on a Tax Equivalent Basis

	2005			2004			2003		
(Dollars in millions)	**Average Balance**	**Interest**	**Average Rate**	**Average Balance**	**Interest**	**Average Rate**	**Average Balance**	**Interest**	**Average Rate**
Liabilities and Shareholders Equity									
Interest-Bearing Deposits									
Domestic Offices									
Money Market Rate Accounts	$ 6,767	$ 109	1.62%	$ 6,648	$ 54	0.81%	$ 7,381	$ 60	0.82%
Savings	8,695	103	1.18	9,224	65	0.71	9,014	71	0.78
Certificates of Deposit of $100,000 or More	3,167	108	3.40	3,706	55	1.49	4,179	65	1.56
Other Time Deposits	1,378	35	2.57	955	15	1.57	1,257	20	1.55
Total Domestic Offices	20,007	355	1.77	20,533	189	0.92	21,831	216	0.99
Foreign Offices									
Banks in Foreign Countries	6,050	129	2.13	5,705	60	1.05	5,765	56	0.98
Government & Official Institutions	581	14	2.44	419	8	1.84	422	8	1.92
Other Time and Savings	19,930	459	2.30	19,633	291	1.49	17,927	227	1.26
Total Foreign Offices	26,561	602	2.26	25,757	359	1.39	24,114	291	1.21
Total Interest-Bearing Deposits	46,568	957	2.05	46,290	548	1.18	45,945	507	1.10
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	1,284	35	2.73	1,551	15	0.99	1,542	13	0.85
Other Borrowed Funds									
Domestic Offices	1,480	55	3.68	2,025	40	1.95	1,580	20	1.27
Foreign Offices	385	3	0.84	650	12	1.88	74	1	0.88
Total Other Borrowed Funds	1,865	58	3.10	2,675	52	1.93	1,654	21	1.26
Payables to Customers and Broker-Dealers	6,014	128	2.12	6,361	57	0.89	3,945	30	0.75
Long-Term Debt	7,312	269	3.68	6,152	136	2.19	6,103	150	2.45
Total Interest-Bearing Liabilities	63,043	1,447	2.29%	63,029	808	1.28%	59,189	721	1.22%
Noninterest-Bearing Deposits (Primarily Domestic)	15,647			14,766			12,670		
Other Liabilities	13,272			12,748			11,954		
Common Shareholders Equity	9,473			8,797			7,654		
Total Liabilities and Shareholders Equity	$ 101,435			$ 99,340			$ 91,467		
Net Interest Earnings and Interest Rate Spread		$ 1,938	1.83%		$ 1,675	1.78%		$ 1,644	1.97%
Net Yield on Interest-Earning Assets			2.36%			2.07%			2.22%
Liabilities Attributable to Foreign Offices	28.06%			28.40%			28.78%		

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Rate/Volume Analysis on a Tax Equivalent Basis

(In millions)	2005 vs. 2004 Increase (Decrease) due to change in: Average Balance	Average Rate	Total Increase (Decrease)	2004 vs. 2003 Increase (Decrease) due to change in: Average Balance	Average Rate	Total Increase (Decrease)
Interest Income						
Interest-Bearing Deposits in Banks	$ (76)	$ 45	$ (31)	$ 127	$ 28	$ 155
Federal Funds Sold and Securities Purchased Under Resale Agreements	(28)	90	62	(9)	10	1
Margin Loans	2	109	111	62	8	70
Non-Margin Loans						
Domestic Offices						
Consumer	58	56	114	27	(17)	10
Commercial	(3)	141	138	33	(99)	(66)
Foreign Offices	28	143	171	(52)	3	(49)
Non-Margin Loans	83	340	423	8	(113)	(105)
Securities						
U.S. Government Obligations	(5)	3	(2)	2	(2)	
U.S. Government Agency Obligations	(3)	28	25	12	(12)	
Obligations of States and Political Subdivisions	(1)	(1)	(2)	(7)	1	(6)
Other Securities:						
Domestic Offices	74	117	191	88	(24)	64
Foreign Offices	23	1	24	11	6	17
Total Other Securities	97	118	215	99	(18)	81
Trading Securities:						
Domestic Offices		6	6		1	1
Foreign Offices	50	45	95	(63)	(16)	(79)
Total Trading Securities	50	51	101	(63)	(15)	(78)
Total Securities	138	199	337	43	(46)	(3)
Total Interest Income	119	783	902	231	(113)	118
Interest Expense						
Interest-Bearing Deposits						
Domestic Offices:						
Money Market Rate Accounts	1	54	55	(5)	(1)	(6)
Savings	(4)	42	38	1	(7)	(6)
Certificate of Deposits of $100,000 or More	(9)	62	53	(7)	(3)	(10)
Other Time Deposits	8	12	20	(5)		(5)
Total Domestic Offices	(4)	170	166	(16)	(11)	(27)
Foreign Offices:						
Banks in Foreign Countries	4	65	69		4	4
Government and Official Institutions	3	3	6			
Other Time and Savings	5	163	168	22	42	64
Total Foreign Offices	12	231	243	22	46	68

Total Interest-Bearing Deposits	8	401	409	6	35	41
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	(3)	23	20		2	2
Other Borrowed Funds						
Domestic Offices	(13)	28	15	7	13	20
Foreign Offices	(4)	(5)	(9)	10	1	11
Total Other Borrowed Funds	(17)	23	6	17	14	31
Payables to Customers and Broker-Dealers	(3)	74	71	21	6	27
Long-Term Debt	30	103	133	1	(15)	(14)
Total Interest Expense	15	624	639	45	42	87
Change in Net Interest Income	$ 104	$ 159	$ 263	$ 186	$ (155)	$ 31

Changes which are not solely due to balance changes or rate changes are allocated to such categories on the basis of the respective percentage changes in average balances and average rates.

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Operating Leverage

	2005			2004			% Change	% Change
(In millions)	Reported	Adj	Core	Reported	Adj	Core	Reported	Core
Noninterest Income	$ 4,956	$	$ 4,956	$ 4,650	$ (70)	$ 4,580	6.6%	8.2%
Net Interest Income	1,909		1,909	1,645	66	1,711	16.0	11.6
Total Revenue	6,865		6,865	6,295	(4)	6,291	9.1	9.1
Total Expense	4,483		4,483	4,122	(48)	4,074	8.8	10.0
Operating Leverage							0.3%	(0.9)%

	2004			2003			% Change	% Change
	Reported	Adj	Core	Reported	Adj	Core	Reported	Core
Noninterest Income	$ 4,650	$ (70)	$ 4,580	$ 3,996	$	$ 3,996	16.4%	14.6%
Net Interest Income	1,645	66	1,711	1,609		1,609	2.2	6.3
Total Revenue	6,295	(4)	6,291	5,605		5,605	12.3	12.2
Total Expense	4,122	(48)	4,074	3,698		3,698	11.5	10.2
Operating Leverage							0.8%	2.0%

UNAUDITED QUARTERLY DATA

(Dollars in millions,	2005				2004			
except per share amounts)	Fourth	Third	Second	First	Fourth	Third	Second	First
Total Revenue (tax equivalent basis)	$ 2,237	$ 2,126	$ 2,077	$ 1,917	$ 1,967	$ 1,736	$ 1,765	$ 1,667
Interest Income	956	870	814	732	782	629	601	441
Interest Expense	464	378	344	277	255	201	180	173
Net Interest Income	492	492	470	455	527	428	421	268
Provision for Credit Losses	10	10	5	(10)	(7)		10	12
Noninterest Income	1,274	1,248	1,256	1,178	1,176	1,099	1,156	1,220
Noninterest Expense	1,148	1,135	1,123	1,077	1,097	999	1,012	1,013
Income Before Income Taxes	608	595	598	566	613	528	555	463
Income Taxes	203	206	200	187	262	174	184	99
Net Income	$ 405	$ 389	$ 398	$ 379	$ 351	$ 354	$ 371	$ 364
Per Common Share Data:								
Basic Earnings	$ 0.53	$ 0.51	$ 0.52	$ 0.49	$ 0.45	$ 0.46	$ 0.48	$ 0.47
Diluted Earnings	0.53	0.51	0.52	0.49	0.45	0.46	0.48	0.47
Cash Dividend	0.21	0.21	0.20	0.20	0.20	0.20	0.20	0.19
Stock Price								
High	32.96	31.25	29.58	33.31	33.92	30.26	33.01	34.71
Low	28.83	28.69	27.25	28.74	29.65	27.55	28.69	30.58

Ratios:

Return on Average Common Shareholders Equity	16.57%	16.15%	17.12%	16.52%	15.34%	15.90%	17.14%	17.17%
Return on Average Assets	1.53	1.53	1.59	1.55	1.40	1.45	1.49	1.47

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The Company s securities that are listed on the New York Stock Exchange® (NYSE) are Common Stock, 5.95% Preferred Trust Securities Series F, and 6.88% Preferred Trust Securities Series E. The NYSE symbol for the Company s Common Stock is BK. All of the Company s other securities are not currently listed. The Company had 25,186 common shareholders of record at January 31, 2006.

New York Stock Exchange Annual Certification

Because the Company s common stock is listed on the NYSE, the Company s Chief Executive Officer is required to make, and has made, an annual certification to the NYSE stating that he was not aware of any violation by the Company of the corporate governance listing standards of the NYSE. The Company s chief executive officer submitted his annual certification to that effect to the NYSE as of May 11, 2005.

The Company has filed with the SEC the certification required to be made by the Company s Chief Executive Officer and Chief Financial Officer under Section 302 of the Sarbanes Oxley Act of 2002, as an exhibit to this Annual Report on Form 10-K for the year ending December 31, 2005.

Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

On October 10, 2005, 2,400 shares of common stock were issued to a new non-employee director as part of his annual retainer. This transaction was exempt from registration under the Securities Act of 1933 pursuant to Section 4(2).

Under its stock repurchase program, the Company buys back shares from time to time. The following table discloses the Company s repurchases of its common stock made during the fourth quarter of 2005.

Period	**Total Number of Shares Purchased**	**Average Price Paid Per Share**	**Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs**	**Maximum Number of Shares That May Yet be Repurchased Under the Plans or Programs**
October 1-31	51,407	$ 31.12	51,407	19,255,175
November 1-30	3,723	31.49	3,723	19,251,452
December 1-31	250,172	32.25	250,172	19,001,280
Total	305,302		305,302	

All shares were repurchased through the Company s 20 million share stock repurchase program, which was announced on July 12, 2005. All the shares repurchased in the fourth quarter were from employee benefit plans.

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OTHER 2004 DEVELOPMENTS

(1) In 2004 the Company recorded several gains and charges that in the aggregate reduced reported earnings by 3 cents per share. These items were recorded in the first and fourth quarters of 2004 and are summarized in the table below.

(In millions) **Item**	**Applicable Quarter**	**Income Statement Caption**	**Pre-Tax Income**	**Tax**	**After-Tax Income**
Net Interest Income[(a)]					
SFAS 13 cumulative lease adjustment (leasing portfolio)	First	Net Interest Income	$ (145)	$ 113	$ (32)
lease adjustment (cross-border rail equipment leases)	Fourth	Net Interest Income	89	(37)	52
lease adjustment (aircraft leases)	Fourth	Net Interest Income	(10)	4	(6)
Subtotal Net Interest Income			(66)	80	14
Aircraft leases/other	Fourth	Provision for Credit Losses	7	(3)	4
Subtotal Net Interest Income After Provision for Credit Losses			(59)	77	18
Noninterest Income[(b)]					
Gain on sale of Wing Hang	First	Other Income	48	(21)	27
Gain on sponsor fund investments	First	Securities Gains	19	(7)	12
Aircraft leases	Fourth	Other Income	3	(1)	2
Subtotal Noninterest Income			70	(29)	41
Noninterest Expense[(c)]					
Severance tied to relocations	First	Salaries and Employee Benefits	(10)	4	(6)
Lease terminations	First	Net Occupancy	(8)	3	(5)
Charge for the RW Matter	Fourth	Other Expense	(30)	8	(22)
Subtotal Noninterest Expense			(48)	15	(33)
Federal tax reserve adjustment related to LILO exposure	Fourth	Income Tax		(50)	(50)
Total			$ (37)	$ 13	$ (24)

(a) An after-tax charge of $32 million resulting from a cumulative adjustment to the leasing portfolio was triggered under Statement of Financial Accounting Standards No. 13 Accounting for Leases (SFAS 13) by the combination of a reduction in state and local taxes and a restructuring of the lease portfolio completed in the first quarter. The SFAS 13 adjustment impacts the timing of lease income reported by the Company, and resulted in a reduction in net interest income of $145 million, offset by tax benefits of $113 million.

An after-tax benefit of $52 million resulted from a SFAS 13 cumulative adjustment to the leasing portfolio for customers exercising their early buy-out (EBO) options. The Company s leasing portfolio contains a number of large cross-border leveraged leases where the lessee has an early buy-out option to purchase the leased assets, generally railcars and related assets. Given a confluence of economic factors, the value of the leased equipment currently exceeds the exercise price of the early buy-out option. The Company offered financial incentives to these lessees to accelerate the exercise of their early buy-out options. As a result, several lessees agreed to this proposal, triggering the after-tax $52 million gain. The gain results from the recognition of lease income over a shorter time frame, since the term of the lease has been shortened to the early buy-out date.

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Net investment in aircraft leases was impacted by a $6 million after-tax adjustment related to aircraft leased to two airlines. The Company recorded a $7 million reduction in the provision for credit losses which largely reflects release of reserves on the aircraft leases.

(b) A $27 million after-tax gain on the sale of a portion of the Company s interest in Wing Hang Bank Limited (Wing Hang), a Hong Kong based bank, which was recorded in other income, and $19 million ($12 million after-tax) of higher than anticipated securities gains in the first quarter resulting from realized gains on sponsor fund investments in Kinkos, Inc., Bristol West Holdings, Inc., Willis Group Holdings, Ltd., and True Temper Sports, Inc.

The Company also had an after-tax gain of $2 million on the sale of a leased aircraft.

(c) The Company also took several actions associated with its long-term cost reduction initiatives. These actions included an after-tax severance charge of $6 million related to staff reductions tied to job relocations and a $5 million after-tax charge for terminating high cost leases associated with the staff redeployments.

The Company recorded an after-tax expense of $22 million in connection with the anticipated settlement of the RW Professional Leasing Services Corp. matter (RW Matter). This expense is only partially tax deductible.

The Company had several appellate conferences with the IRS related to the Company s cross-border leveraged lease transactions in December of 2004 and January 2005. Based on a revision to the probabilities and costs assigned to litigation and settlement outcomes, the Company recorded a $50 million expense associated with increasing the tax reserve on these transactions.

GLOSSARY

Alternative investments: Usually refers to investments in hedge funds, leveraged loans, subordinated and distressed debt, real estate and foreign currency overlay. Many hedge funds pursue strategies that are uncommon relative to mutual funds. Examples of alternative investment strategies are: long-short equity, event driven, statistical arbitrage, fixed income arbitrage, convertible arbitrage, short bias, global macro, and equity market neutral.

Assets Under Custody: The financial institution has legal responsibility for the customer s assets. This includes management, administration and safekeeping.

Assets Under Management: Usually refers to the market value of assets an investment company manages on behalf of investors. The Company includes in its assets under management funds managed by its foreign exchange overlay business and short term investment funds managed as part of its securities lending business.

Collateral Management: Collateral management is a comprehensive program designed to simplify collateralization and expedite securities transfers for buyers and sellers. The Company acting as an independent collateral manager is positioned between the buyer and seller to provide a convenient, flexible, and efficient service to ensure proper collateralization throughout the term of the transaction. The service includes verification of securities eligibility and maintenance of margin requirements.

Credit derivatives are contractual agreements that provide insurance against a credit event of one or more referenced credits. The nature of the credit event is established by the buyer and seller at the inception of the transaction, such events include bankruptcy, insolvency and failure to meet payment obligations when due. The buyer of the credit derivative pays a periodic fee in return for a contingent payment by the seller (insurer) following a credit event.

Credit risk: The risk of loss due to borrower or counterparty default.

Cross-currency swaps are contracts that generally involve the exchange of both interest and principal amounts in two different currencies. Also see interest rate swaps in this glossary.

Depositary receipts (DR): A negotiable security that generally represents a non-U.S. company s publicly traded equity. Although typically denominated in U.S. dollars, depositary receipts can also be denominated in Euros. Depositary receipts are eligible to trade on all U.S. stock exchanges and many European stock exchanges. American depositary receipts (ADR) trade only in the U.S.

Economic Value of Equity (EVE): An aggregation of discounted future cash flows of assets and liabilities over a long-term horizon.

Exchange traded fund (ETF): Each share of an ETF tracks a basket of stocks in some index or benchmark, providing investors with a vehicle that closely parallels the performance of these benchmarks while allowing for intraday trading.

Foreign currency options are similar to interest rate options except they are based on foreign exchange rates. Also see interest rate options in this glossary.

Foreign currency swaps: An agreement to exchange stipulated amounts of one currency for another currency at one or more future dates.

Foreign exchange contracts are contracts that provide for the future receipt or delivery of foreign currency at previously agreed-upon terms.

Foreign exchange overlay: The Company s specialist currency management group, BNY Overlay Associates, provides foreign exchange risk management solutions and alternative investment products. The

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currency programs can be structured as independent investment vehicles or as value-enhancing overlays on another asset class. The Company provides complete management service, from initial consultation to strategy execution and electronic reporting.

Forward rate agreements are contracts to exchange payments on a specified future date, based on a market change in interest rates from trade date to contract settlement date.

Granularity refers to the amount of concentration in the credit portfolio due to large individual exposures. One measure of granularity is the amount of economic capital an exposure uses. As the average economic capital per exposure declines, the portfolio is considered to be more granular.

Hedge fund: A fund, usually used by wealthy individuals and institutions, which is allowed to use aggressive strategies that are unavailable to mutual funds, including selling short, leverage, program trading, swaps, arbitrage, and derivatives. Hedge funds are exempt from many of the rules and regulations governing mutual funds, which allow them to accomplish aggressive investing goals. Legal requirements in many countries allow only certain sophisticated investors to participate in hedge funds.

Interest rate options, including caps and floors, are contracts to modify interest rate risk in exchange for the payment of a premium when the contract is initiated. As a writer of interest rate options, the Company receives a premium in exchange for bearing the risk of unfavorable changes in interest rates. Conversely, as a purchaser of an option, the Company pays a premium for the right, but not the obligation, to buy or sell a financial instrument or currency at predetermined terms in the future.

Interest rate sensitivity: The exposure of net interest income to interest rate movements.

Interest rate swaps are contracts in which a series of interest rate flows in a single currency is exchanged over a prescribed period. Interest rate swaps are the most common type of derivative contract that the Company uses in its asset/liability management activities. An example of a situation in which the Company would utilize an interest rate swap would be to convert its fixed-rate debt to a variable rate. By entering into the swap, the principal amount of the debt would remain unchanged, but the interest streams would change.

Investment grade equivalent: The Company s internal risk assessment which generally represents a risk profile similar to that of a BBB-/Baa3 or better rating as defined by independent rating agencies, such as Standard & Poor s or Moody s.

Invoiced services are services provided by global payment services that are paid for by fees or by leaving a compensating balance.

Liquidity risk: The risk of being unable to fund the Company s portfolio of assets at appropriate maturities and rates, and the risk of being unable to liquidate a position in a timely manner at a reasonable price.

Mark-to-market exposure: Mark-to market exposure is a measure, at a point in time, of the value of a derivative or foreign exchange contract in the open market. When the mark-to-market is positive, it indicates the counterparty owes the Company and, therefore, creates a repayment risk for the Company. When the mark-to-market is negative, the Company owes the counterparty. In this situation, the Company does not have repayment risk.

Market risk: The potential loss in value of portfolios and financial instruments caused by movements in market variables, such as interest and foreign-exchange rates, credit spreads, and equity and commodity prices.

Net yield on interest-earning assets: The average rate for interest-earning assets less the average rate paid for all sources of funds.

Operating leverage is measured by comparing the rate of increase in revenue to the rate of increase in expenses.

Operational risk: The risk of loss resulting from inadequate or failed processes or systems, human factors, or external events.

Securities lending short-term investment fund: For some of its securities lending clients, the Company invests the cash collateral received in the customer s securities lending transactions in a short-term highly liquid commingled investment fund. The fund is rated AAA by Standard & Poor s and started operation in 2003.

SFAS: Statement of Financial Accounting Standard.

Sub-custodian: A local provider (e.g., a bank) contracted by the Company to provide specific custodial related services in a selected country or geographic area. Services generally include holding foreign securities in safekeeping, facilitating settlements and reporting holdings to the custodian.

Tangible common equity (TCE) ratio: The percentage computed by dividing common shareholders equity less intangibles and goodwill by period end assets less intangibles and goodwill.

Unit investment trust (UIT): A sponsor-created portfolio of securities. Like mutual funds, these securities portfolios are designed to meet specific investment objectives. However, unlike a mutual fund, a UIT is an unmanaged portfolio consisting of securities that are fixed at the UIT s initiation and generally remain unchanged over the security s life.

Value at risk (VAR): A measure of the dollar amount of potential loss from adverse market moves in an everyday market environment.

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T HE BANK OF NEW YORK COMPANY, INC.

CONSOLIDATED BALANCE SHEETS

(Dollars in millions, except per share amounts)	December 31, 2005	2004
Assets		
Cash and Due from Banks	$ 3,515	$ 3,886
Interest-Bearing Deposits in Banks	8,644	8,192
Securities		
Held-to-Maturity (fair value of $1,951 in 2005 and $1,873 in 2004)	1,977	1,886
Available-for-Sale	25,349	21,916
Total Securities	27,326	23,802
Trading Assets	5,930	4,627
Federal Funds Sold and Securities Purchased Under Resale Agreements	2,425	5,708
Loans (less allowance for loan losses of $411 in 2005 and $591 in 2004)	40,315	35,190
Premises and Equipment	1,060	1,097
Due from Customers on Acceptances	233	137
Accrued Interest Receivable	391	285
Goodwill	3,619	3,477
Intangible Assets	811	793
Other Assets	7,805	7,335
Total Assets	$ 102,074	$ 94,529
Liabilities and Shareholders Equity		
Deposits		
Noninterest-Bearing (principally domestic offices)	$ 18,236	$ 17,442
Interest-Bearing		
Domestic Offices	19,522	18,692
Foreign Offices	26,666	22,587
Total Deposits	64,424	58,721
Federal Funds Purchased and Securities Sold Under Repurchase Agreements	834	1,205
Trading Liabilities	2,401	2,873
Payables to Customers and Broker-Dealers	8,623	8,664
Other Borrowed Funds	860	533
Acceptances Outstanding	235	139
Accrued Taxes and Other Expenses	4,124	4,452
Accrued Interest Payable	172	113
Other Liabilities (including allowance for lending-related commitments of $154 in 2005 and $145 in 2004)	2,708	2,418
Long-Term Debt	7,817	6,121
Total Liabilities	92,198	85,239
Shareholders Equity		
Common Stock-par value $7.50 per share, authorized 2,400,000,000 shares, issued 1,044,994,517 shares in 2005 and 1,041,495,972 shares in 2004	7,838	7,811
Additional Capital	1,826	1,734
Retained Earnings	7,089	6,162
Accumulated Other Comprehensive Income	(134)	(6)
	16,619	15,701

Less: Treasury Stock (273,662,218 shares in 2005 and 263,374,998 shares in 2004), at cost	6,736	6,411
Loan to ESOP (203,507 shares in 2005), at cost	7	
Total Shareholders Equity	9,876	9,290
Total Liabilities and Shareholders Equity	$ 102,074	$ 94,529

See accompanying Notes to Consolidated Financial Statements.

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THE BANK OF NEW YORK COMPANY, INC.

CONSOLIDATED STATEMENTS OF INCOME

	For the years ended December 31,			Percent Inc/(Dec)	
(In millions, except per share amounts)	**2005**	**2004**	**2003**	**2005 vs. 2004**	**2004 vs. 2003**
Interest Income					
Loans	$ 1,505	$ 1,080	$ 1,187	39%	(9)%
Margin Loans	267	156	86	71	81
Securities					
Taxable	976	741	651	32	14
Exempt from Federal Income Taxes	40	40	48		(17)
	1,016	781	699	30	12
Deposits in Banks	274	305	150	(10)	103
Federal Funds Sold and Securities					
Purchased Under Resale Agreements	142	80	79	78	1
Trading Assets	152	51	129	198	(60)
Total Interest Income	3,356	2,453	2,330	37	5
Interest Expense					
Deposits	957	548	507	75	8
Federal Funds Purchased and Securities Sold Under					
Repurchase Agreements	35	15	13	133	15
Other Borrowed Funds	58	52	21	12	148
Customer Payables	128	57	30	125	90
Long-Term Debt	269	136	150	98	(9)
Total Interest Expense	1,447	808	721	79	12
Net Interest Income	1,909	1,645	1,609	16	2
Provision for Credit Losses	15	15	155		(90)
Net Interest Income After Provision for Credit Losses	1,894	1,630	1,454	16	12
Noninterest Income					
Servicing Fees					
Securities	3,148	2,857	2,412	10	18
Global Payment Services	294	319	314	(8)	2
	3,442	3,176	2,726	8	17
Private Client Services and Asset Management Fees	490	448	384	9	17
Service Charges and Fees	382	384	375	(1)	2
Foreign Exchange and Other Trading Activities	391	364	327	7	11
Securities Gains	68	78	35	(13)	123
Other	183	200	149	(9)	34
Total Noninterest Income	4,956	4,650	3,996	7	16
Noninterest Expense					
Salaries and Employee Benefits	2,549	2,324	2,002	10	16

Net Occupancy	323	305	261	6	17
Furniture and Equipment	208	204	185	2	10
Clearing	187	176	154	6	14
Sub-custodian Expenses	96	87	74	10	18
Software	215	193	170	11	14
Communications	95	93	92	2	1
Amortization of Intangibles	40	34	25	18	36
Merger and Integration Costs			96		
Other	770	706	639	9	10
Total Noninterest Expense	4,483	4,122	3,698	9	11
Income Before Income Taxes	2,367	2,158	1,752	10	23
Income Taxes	796	718	595		