BANK OF NEW YORK CO INC
Form 10-Q
August 03, 2006

THE BANK OF NEW YORK COMPANY, INC.

Quarterly Report on Form 10-Q
For the quarterly period ended June 30, 2006

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| Continuing Operations(1) | $\begin{gathered} \text { June } 30, \\ 2006 \end{gathered}$ |  | $\begin{gathered} \text { March 31, } \\ 2006 \end{gathered}$ |  | June 30,$2005$ |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Quarter |  |  |  |  |  |  |
| Net Interest Income Noninterest Income | \$ | 358 | \$ | 339 | \$ | 329 |
|  |  | 1,366 |  | 1,261 |  | 1,194 |
|  |  | 1,724 |  | 1,600 |  | 1,523 |
| Tax Equivalent Adjustment |  | 7 |  | 7 |  | 6 |
| Revenue (tax equivalent basis) | \$ | 1,731 | \$ | 1,607 | \$ | 1,529 |
| Income from Continuing Operations |  |  |  |  |  |  |
| Income Taxes |  | 200 |  | 175 |  | 162 |
| Income from Continuing Operations 391 360 <br> Income from Discontinued Operations,  343 |  |  |  |  |  |  |
|  |  |  |  |  |  |  |
| Net Income | \$ | 448 | \$ | 422 | \$ | 398 |
| Basic EPS: |  |  |  |  |  |  |
| Income from Continuing Operations | \$ | 0.52 | \$ | 0.47 | \$ | 0.45 |
| Income from Discontinued Operations, Net |  | 0.07 |  | 0.08 |  | 0.07 |
| Net Income |  | 0.59 |  | 0.55 |  | 0.52 |
| Diluted EPS: |  |  |  |  |  |  |
| Income from Continuing Operations |  | 0.52 |  | 0.47 |  | 0.45 |
| Income from Discontinued Operations, Net |  | 0.07 |  | 0.08 |  | 0.07 |
| Net Income |  | 0.59 |  | 0.55 |  | 0.52 |
| Cash Dividends Per Share |  | 0.21 |  | 0.21 |  | 0.20 |
| Return on Average Common |  |  |  |  |  |  |
| Return on Average Assets |  | 1.54 |  | 1.50 |  | 1.49 |
| Efficiency Ratio |  | 66.4 |  | 67.0 |  | 67.8 |

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THE BANK OF NEW YORK COMPANY, INC.
Consolidated Financial Highlights
(Dollars in millions, except per share amounts)
(Unaudited)

|  | June 30, | March 31, | June 30, |
| :---: | :---: | :---: | :---: |
| Continuing Operations(1) | 2006 | 2006 | 2005 |


| Net Interest Income | \$ | 697 | \$ | 339 | \$ | 650 |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Noninterest Income |  | 2,627 |  | 1,261 |  | 2,310 |
|  |  | 3,324 |  | 1,600 |  | 2,960 |
| Tax Equivalent Adjustment |  | 14 |  | 7 |  | 13 |
| Revenue (tax equivalent basis) | \$ | 3,338 | \$ | 1,607 | \$ | 2,973 |
| Income from Continuing Operations |  |  |  |  |  |  |
| Income Taxes |  | 375 |  | 175 |  | 317 |
| Income from Continuing Operations |  | 751 |  | 360 |  | 671 |
| Income from Discontinued Operations, Net of Taxes |  | 119 |  | 62 |  | 106 |
| Net Income | \$ | 870 | \$ | 422 | \$ | 777 |
| Basic EPS: |  |  |  |  |  |  |
| Income from Continuing Operations | \$ | 0.99 | \$ | 0.47 | \$ | 0.87 |
| Income from Discontinued Operations, Net |  | 0.15 |  | 0.08 |  | 0.14 |
| Net Income |  | 1.14 |  | 0.55 |  | 1.01 |
| Diluted EPS: |  |  |  |  |  |  |
| Income from Continuing Operations |  | 0.98 |  | 0.47 |  | 0.86 |
| Income from Discontinued Operations, Net |  | 0.15 |  | 0.08 |  | 0.14 |
| Net Income |  | 1.13 |  | 0.55 |  | 1.00 |
| Cash Dividends Per Share |  | 0.42 |  | 0.21 |  | 0.40 |
| Return on Average Common |  |  |  |  |  |  |
| Shareholders' Equity |  | 15.30\% |  | 14.75\% |  | $14.52 \%$ |
| Return on Average Assets |  | 1.52 |  | 1.50 |  | 1.48 |
| Efficiency Ratio |  | 66.7 |  | 67.0 |  | 67.8 |
| Assets | \$ | 99,935 | \$ | 94,851 | \$ | 94,370 |
| Loans |  | 35,650 |  | 32,191 |  | 32,950 |
| Securities |  | 27,355 |  | 27,190 |  | 25,691 |
| Deposits - Domestic |  | 25,602 |  | 20,751 |  | 22,611 |
| - Foreign |  | 31,139 |  | 30,049 |  | 26,076 |
| Long-Term Debt |  | 8,207 |  | 8,309 |  | 7,586 |
| Common Shareholders' Equity |  | 10,056 |  | 10,101 |  | 9,471 |
| Employees |  | 20,109 |  | 19,989 |  | 19,506 |
| Allowance for Loan Losses as <br> a Percent of Total Loans |  |  |  |  |  |  |
| Allowance for Loan Losses as a Percent of Non-Margin Loans |  | 1.10 |  | 1.24 |  | 1.72 |
| Total Allowance for Credit Losses as a Percent of Total Loans |  | 1.35 |  | 1.47 |  | 1.82 |
| Total Allowance for Credit Losses as a Percent of Non-Margin Loans |  | 1.57 |  | 1.76 |  | 2.23 |

## THE BANK OF NEW YORK COMPANY, INC. <br> Consolidated Financial Highlights - Supplemental Information

 (Dollars in millions, except per share amounts)(Unaudited)

|  | June 30, | March 31, | 2006 |
| :---: | :---: | :---: | :---: |

## Quarter

| Net Interest Income | \$ | 512 | \$ | 488 | \$ | 470 |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| Noninterest Income |  | 1,426 |  | 1,332 |  | 1,256 |
|  |  | 1,938 |  | 1,820 |  | 1,726 |
| Tax Equivalent Adjustment |  | 9 |  | 7 |  | 7 |
| Revenue (tax equivalent basis) | \$ | 1,947 | \$ | 1,827 | \$ | 1,733 |
| Net Income | \$ | 448 | \$ | 422 | \$ | 398 |
| Basic EPS |  | 0.59 |  | 0.55 |  | 0.52 |
| Diluted EPS |  | 0.59 |  | 0.55 |  | 0.52 |
| Cash Dividends Per Share |  | 0.21 |  | 0.21 |  | 0.20 |
| Efficiency Ratio |  | $64.9 \%$ |  | 65.1 \% |  | $65.7 \%$ |
| Year-to-date |  |  |  |  |  |  |
| Net Interest Income Noninterest Income | \$ | 1,000 | \$ | 488 | \$ | 925 |
|  |  | 2,758 |  | 1,332 |  | 2,434 |
|  |  | 3,758 |  | 1,820 |  | 3,359 |
| Tax Equivalent Adjustment |  | 15 |  | 7 |  | 14 |
| Revenue (tax equivalent basis) | \$ | 3,773 | \$ | 1,827 | \$ | 3,373 |
| Net Income | \$ | 870 | \$ | 422 | \$ | 777 |
| Basic EPS |  | 1.14 |  | 0.55 |  | 1.01 |
| Diluted EPS |  | 1.13 |  | 0.55 |  | 1.00 |
| Cash Dividends Per Share |  | 0.42 |  | 0.21 |  | 0.40 |
| Efficiency Ratio |  | $65.0 \%$ |  | 65.1 \% |  | $65.9 \%$ |
| Assets | \$ | 108,881 | \$ | 103,611 | \$ | 103,063 |
| Loans |  | 43,622 |  | 40,054 |  | 40,681 |
| Securities |  | 27,459 |  | 27,288 |  | 25,779 |
| Deposits - Domestic |  | 39,280 |  | 35,175 |  | 37,921 |
| - Foreign |  | 31,139 |  | 30,049 |  | 26,077 |
| Long-Term Debt |  | 8,207 |  | 8,309 |  | 7,586 |


| Common Shareholders' Equity | 10,056 | 10,101 | 9,471 |
| :--- | :---: | :---: | :---: |
| Allowance for Loan Losses as <br> a Percent of Total Loans <br> Allowance for Loan Losses as <br> a Percent of Non-Margin Loans <br> Total Allowance for Credit Losses as <br> a Percent of Total Loans | $0.96 \%$ | $1.05 \%$ | $1.38 \%$ |
| Total Allowance for Credit Losses as <br> a Percent of Non-Margin Loans | 1.08 | 1.21 | 1.62 |
| Employees |  |  |  |

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THE BANK OF NEW YORK COMPANY, INC.
Consolidated Financial Highlights (Dollars in millions, except per share amounts) (Unaudited)

| June 30, | March 31, | June 30, |
| :---: | :---: | :---: |
| 2006 | 2006 | 2005 |

Assets Under Custody
--------------------
(In trillions) - Estimated $\begin{array}{lllllll}\text { Assets Under Custody } & \$ 12.0 & \$ 11.3 & \$ 10.3\end{array}$

Equity Securities 32\% 33\% 35 30
Fixed Income Securities
68
$\begin{array}{lllll}\$ & 4.1 & \$ & 3.7 & \$\end{array}$

Assets Under Management
(In billions)- Estimated Asset Management Sector

Equity Securities

| \$ | 116 | \$ | 113 | \$ | 105 |
| :---: | :---: | :---: | :---: | :---: | :---: |
|  | 36 |  | 37 |  | 36 |
|  | 21 |  | 21 |  | 22 |
|  | 28 |  | 26 |  | 15 |
|  | 31 |  | 29 |  | 32 |
|  | 11 |  | 11 |  | 8 |
|  | 43 |  | 49 |  | 39 |
| \$ | 170 | \$ | 173 | \$ | 152 |

```
Capital Ratios
Tier 1 Capital Ratio
Total Capital Ratio
Tangible Common Equity Ratio
```

Tangible Common Equity Ratio
$7.96 \%$ 8.28\% 8.07\%

| 12.06 | 12.44 | 12.49 |
| ---: | ---: | ---: |
| 6.22 | 6.51 | 6.55 |

$6.22 \quad 6.51 \quad 6.55$
$5.07 \quad 5.42 \quad 5.26$

```
Performance Ratios
--------------
Quarter
------- 
Shareholders' Equity
        18.17%
        1.63
        7.31%
        17.12%
        1.61
        1.59
Year-to-date
Return on Average Common
    Shareholders' Equity
Return on Average Assets
        17.74%
    17.31%
    1.61
        16.82%
    1.62
    1.57
```



$$
13.09 \quad \$
$$

$$
12.29
$$

32.20
12.29

$$
02.20
$$

36.04
1.63
1.61
1.59

Year-to-date
Return on Average Common
Shareholders' Equity
Return on Average Assets

```
Other Data
```

Other Data
----------
----------
Common Shareholders'
Common Shareholders'
Equity Per Share
Equity Per Share
Market Value Per Share
Market Value Per Share
of Common Stock
of Common Stock Of Common Stock

```
    Of Common Stock
-

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Management's Discussion and Analysis of Financial Condition and
Results of Operations ("MD\&A")

\section*{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 that 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," "intend," "believe," "plan," "goal," "should," "may," "strategy," "target," and words of similar meaning are intended to identify forward-looking statements in addition to statements specifically identified as forward-looking statements. In addition, certain business terms used in this document are defined in the Company's 2005 Annual Report on Form 10-K.

OVERVIEW

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, private banking, and asset management. 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 ("The Bank"), 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 one of the industry's broadest arrays 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,

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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 LLC ("Pershing") in 2003 for \(\$ 2\) billion was the largest of these acquisitions completed to date. The acquisition of the corporate trust business of JPMorgan Chase \& Co. ("JPMorgan Chase"), announced in April 2006, and the formation of BNY ConvergEx Group, announced in June 2006 , should also contribute to the Company's ability to achieve its key objectives.

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, significantly reducing non-financial corporate credit exposures by \(41 \%\) from December 31, 2001 to December 31, 2005, and, most recently, announcing an agreement to sell retail and regional middle market banking businesses to JPMorgan Chase. To the extent these actions generated capital, the capital has been reallocated to the Company's higher-growth businesses or used to repurchase shares.

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.

\section*{SECOND QUARTER 2006 HIGHLIGHTS}

The Company reported one of its most successful quarters ever, not simply in terms of the strength and quality of its financial results but also in terms of the significant actions taken in sharpening its focus, strengthening its business mix and improving the earnings potential of the franchise. The Company is moving toward a "pure" trust and custody business model with the JPMorgan Chase transaction. Subsequently, the Company has made its business model even stronger and more focused by repositioning its execution services business through the formation of BNY ConvergEx Group.

The Company was also successful in winning new business. This was reflected in the Company's revenue growth, which was strong across all areas of securities servicing, as well as in asset management and private banking - the Company's primary areas of focus. This revenue growth drove strong performance in other key operating measures, such as operating leverage, EPS growth, and return on equity.

The Company reported second quarter net income of \(\$ 448\) million and diluted earnings per share of 59 cents, compared with net income of \(\$ 398\) million and diluted earnings per share of 52 cents in the second quarter of 2005 , up \(13 \%\), and net income of \(\$ 422\) million and diluted earnings per share of 55 cents in the first quarter of 2006. Year-to-date net income was \(\$ 870\) million, or \(\$ 1.13\) of diluted earnings per share, compared to \(\$ 777\) million, or \(\$ 1.00\) of diluted earnings per share in 2005 .

On April 8, 2006, the Company entered into a definitive agreement with JPMorgan Chase to acquire its corporate trust business, with JPMorgan Chase

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acquiring the Company's retail and regional middle market banking businesses. In the second quarter of 2006 , the Company adopted discontinued operations accounting for its retail and regional middle market banking business. The results from continuing operations exclude its retail and regional middle market banking business and do not include the operations of JPMorgan Chase's corporate trust business expected to be acquired in the fourth quarter and therefore are of limited value in projecting future results. Adjusted financial statements combining continuing and discontinued operations are presented in "Supplemental Financial Information."

Second quarter 2006 income from continuing operations increased to \$391 million, or 52 cents of diluted earnings per share. This compares to income from continuing operations of \(\$ 343\) million, or 45 cents of diluted earnings per share in the second quarter of 2005 , up \(16 \%\), and \(\$ 360\) million, or 47 cents of diluted earnings per share in the first quarter of 2006 . On a year-to-date basis, income from continuing operations was \(\$ 751\) million, or 98 cents of diluted earnings per share, compared to \(\$ 671\) million, or 86 cents of diluted earnings per share in 2005, up 14\%.

Performance highlights for the quarter include:
```

* Significant positive operating leverage over year ago and sequential
periods.
* Return on average common shareholders' equity of 18.2%.
* Securities servicing fees up 17% versus the year ago quarter. The growth

```
was led by strong performance in issuer services, broker-dealer services, investor services, and execution and clearing services.
* Net interest income up 9\% over last year's second quarter reflecting growth in deposits, particularly from the Company's corporate trust and custody businesses.
* Foreign exchange and other trading revenues up 29\% from the year ago quarter.
* Private banking and asset management revenues up 23\% from the year ago quarter, reflecting both acquisitions and growth at Ivy Asset Management.
* Two major strategic transactions announced: the swap transaction with JPMorgan Chase and the formation of BNY ConvergEx Group to better position the Company's execution business for future growth.

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SUPPLEMENTAL FINANCIAL INFORMATION

On April 8, 2006, the Company entered into a definitive agreement with JPMorgan Chase to acquire its corporate trust business, with JPMorgan Chase acquiring the Company's retail and regional middle market banking businesses. The transaction further increases the Company's focus on the securities services and asset management and private banking businesses that are at the core of its long-term business strategy. The transaction has been approved by each company's board of directors and is expected to be completed in the fourth quarter of 2006 , subject to regulatory approvals.

For the quarters and six months ended June 30, 2006 and 2005, the Company has prepared supplemental financial information as follows:
* Full income statement and balance sheet for continuing operations, which excludes the results of substantially all of Retail \& Regional Middle Market Banking Business
* Full income statement and balance sheet for the Retail \& Regional Middle Market Banking Business, which is reflected as discontinued operations
* Adjusted results, which combine the continuing and discontinued operations to provide continuity with historical results

The Company believes that providing supplemental adjusted non-GAAP financial information is useful to investors in understanding the underlying operational performance of the Company and its businesses and performance trends. Specifically, the Company believes that the results of continuing operations are of limited value in projecting future results because they do not include the net income associated with the acquisition of the JPMorgan Chase corporate trust business, planned to close in the fourth quarter of 2006. By combining the results of continuing and discontinued operations and comparing the results with prior periods, the Company believes investors can obtain greater insight into the current performance of the Company in relation to historical results. Although the Company believes that the non-GAAP financial measures presented in this report enhance investors' understanding of the Company's business and performance, these non-GAAP measures should not be considered an alternative to GAAP. A reconciliation of the Company's adjusted and GAAP financial results for the quarters and six-month periods ended June 30, 2006 and 2005 are included in "Supplemental Data".

Income statements for both continuing operations and for adjusted results is provided on the following two pages. In addition, see "Consolidated Financial Highlights - Supplemental Information" and "Supplemental Data."

THE BANK OF NEW YORK COMPANY, INC. Income Statement - Supplemental Information (In millions, except per share amounts) (Unaudited)

Continuing Operations
\begin{tabular}{|c|c|c|c|c|}
\hline & Quarter Ended & & Six & Months Ended \\
\hline June 30, & March 31, & June 30, & & June 30, \\
\hline 2006 & 2006 & 2005 & 2006 & 2005 \\
\hline
\end{tabular}
\begin{tabular}{|c|c|c|c|c|c|}
\hline Net Interest Income & \$ 358 & \$ 339 & \$ 329 & \$ 697 & \$ 65 \\
\hline Provision for Credit Losses & (1) & - & (3) & (1) & (2) \\
\hline Net Interest Income After Provision for Credit Losses & 359 & 339 & 332 & 698 & 67 \\
\hline Noninterest Income & & & & & \\
\hline Servicing Fees & & & & & \\
\hline Securities & 909 & 831 & 775 & 1,740 & 1,52 \\
\hline Global Payment Services & 63 & 62 & 67 & 125 & 13 \\
\hline & 972 & 893 & 842 & 1,865 & 1,65 \\
\hline \begin{tabular}{l}
Private Banking and \\
Asset Management Fees
\end{tabular} & 138 & 130 & 112 & 268 & 22 \\
\hline Service Charges and Fees & 53 & 52 & 64 & 105 & 11 \\
\hline Foreign Exchange and Other Trading Activities & 130 & 113 & 101 & 243 & 19 \\
\hline Securities Gains & 23 & 17 & 23 & 40 & \\
\hline Other & 50 & 56 & 52 & 106 & 8 \\
\hline Total Noninterest Income & 1,366 & 1,261 & 1,194 & 2,627 & 2,31 \\
\hline Noninterest Expense & & & & & \\
\hline Salaries and Employee Benefits & 656 & 604 & 581 & 1,260 & 1,13 \\
\hline Net Occupancy & 68 & 68 & 65 & 136 & 12 \\
\hline Furniture and Equipment & 48 & 51 & 49 & 99 & \\
\hline Clearing & 53 & 50 & 42 & 103 & \\
\hline Sub-custodian Expenses & 36 & 34 & 24 & 70 & \\
\hline Software & 53 & 55 & 55 & 108 & 10 \\
\hline Communications & 22 & 26 & 21 & 48 & \\
\hline Amortization of Intangibles & 15 & 13 & 10 & 28 & \\
\hline Other & 183 & 164 & 174 & 347 & 32 \\
\hline Total Noninterest Expense & 1,134 & 1,065 & 1,021 & 2,199 & 1,99 \\
\hline Income Before Income Taxes & 591 & 535 & 505 & 1,126 & 98 \\
\hline Income Taxes & 200 & 175 & 162 & 375 & 31 \\
\hline Net Income & \$ 391 & \$ 360 & \$ 343 & \$ 751 & \$ 67 \\
\hline
\end{tabular}
\begin{tabular}{|c|c|c|c|}
\hline Diluted Earnings Per Share & \$0.52 & \$0.47 & \$0.45 \\
\hline \multicolumn{4}{|l|}{Diluted earnings per share from continuing operations for the second} \\
\hline \multicolumn{4}{|l|}{quarter of 2006 were 52 cents, up 16\% from 45 cents a year ago. For the year-} \\
\hline \multicolumn{4}{|l|}{to-date period, diluted earnings per share grew 14\% to 98 cents from a year ago.} \\
\hline
\end{tabular}

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THE BANK OF NEW YORK COMPANY, INC. Income Statement - Supplemental Information (In millions, except per share amounts)
(Unaudited)

Adjusted Income Statement (1)

\begin{tabular}{|c|c|c|c|c|c|}
\hline Net Interest Income & \$ 512 & \$ 488 & \$ 470 & \$1,000 & \\
\hline Provision for Credit Losses & - & 5 & 5 & 5 & \\
\hline Net Interest Income After Provision for Credit Losses & 512 & 483 & 465 & 995 & 93 \\
\hline Noninterest Income & & & & & \\
\hline Servicing Fees & & & & & \\
\hline Securities & 909 & 831 & 775 & 1,740 & 1,52 \\
\hline Global Payment Services & 70 & 70 & 76 & 140 & 15 \\
\hline & 979 & 901 & 851 & 1,880 & 1,67 \\
\hline \begin{tabular}{l}
Private Banking and \\
Asset Management Fees
\end{tabular} & 150 & 141 & 123 & 291 & 24 \\
\hline Service Charges and Fees & 91 & 89 & 103 & 180 & 19 \\
\hline Foreign Exchange and Other Trading Activities & 132 & 115 & 103 & 247 & 19 \\
\hline Securities Gains & 23 & 17 & 23 & 40 & \\
\hline Other & 51 & 69 & 53 & 120 & 8 \\
\hline Total Noninterest Income & 1,426 & 1,332 & 1,256 & 2,758 & 2,43 \\
\hline Noninterest Expense & & & & & \\
\hline Salaries and Employee Benefits & 723 & 668 & 640 & 1,391 & 1,25 \\
\hline Net Occupancy & 86 & 88 & 82 & 174 & 16 \\
\hline Furniture and Equipment & 50 & 53 & 51 & 103 & 10 \\
\hline Clearing & 53 & 50 & 42 & 103 & 8 \\
\hline
\end{tabular}

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\begin{tabular}{|c|c|c|c|c|}
\hline Sub-custodian Expenses & 36 & 34 & 24 & 70 \\
\hline Software & 53 & 56 & 55 & 109 \\
\hline Communications & 23 & 27 & 22 & 50 \\
\hline Amortization of Intangibles & 15 & 13 & 10 & 28 \\
\hline Other & 209 & 189 & 197 & 398 \\
\hline Total Noninterest Expense & 1,248 & 1,178 & 1,123 & 2,426 \\
\hline Income Before Income Taxes & 690 & 637 & 598 & 1,327 \\
\hline Income Taxes & 242 & 215 & 200 & 457 \\
\hline Net Income & \$ 448 & \$ 422 & \$ 398 & \$ 870 \\
\hline Diluted Earnings Per Share & \$0.59 & \$0.55 & \$0.52 & \$ 1.13 \\
\hline
\end{tabular}

\footnotetext{
Diluted earnings per share from adjusted results for the second quarter of 2006 were 59 cents, up \(13 \%\) from 52 cents a year ago. For the year-to-date period, diluted earnings per share grew 13\% to \$1.13 from a year ago.
}

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CONSOLIDATED INCOME STATEMENT REVIEW

Noninterest Income

Continuing Operations
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|c|}
\hline \multirow[b]{3}{*}{(In millions)} & \multicolumn{2}{|l|}{\multirow[b]{3}{*}{2206}} & \multicolumn{2}{|r|}{\multirow[b]{3}{*}{1006}} & \multicolumn{2}{|r|}{\multirow[b]{3}{*}{\(2 Q 05\)}} & \multicolumn{5}{|l|}{Percent Inc/(Dec)} \\
\hline & & & & & & & & \multirow[b]{2}{*}{\[
\begin{gathered}
2 Q 06 \text { vs. } \\
2 Q 05
\end{gathered}
\]} & \multicolumn{2}{|l|}{Year-to-date} & \multirow[t]{2}{*}{\begin{tabular}{l}
Percent \\
Inc/ \\
(Dec)
\end{tabular}} \\
\hline & & & & & & & \[
\begin{gathered}
2 Q 06 \text { vs. } \\
1206
\end{gathered}
\] & & 2006 & 2005 & \\
\hline \multicolumn{12}{|l|}{Servicing Fees} \\
\hline Securities & \$ & 909 & \$ & 831 & \$ & 775 & 9\% & 17\% & \$1,740 & \$1,525 & 14\% \\
\hline \multicolumn{12}{|l|}{Global Payment} \\
\hline Services & & 63 & & 62 & & 67 & 2 & (6) & 125 & 133 & (6) \\
\hline & & 972 & & 893 & & 842 & 9 & 15 & 1,865 & 1,658 & 12 \\
\hline \multicolumn{12}{|l|}{Private Banking and Asset} \\
\hline Management Fees & & 138 & & 130 & & 112 & 6 & 23 & 268 & 224 & 20 \\
\hline \multicolumn{12}{|l|}{Service Charges} \\
\hline \multicolumn{12}{|l|}{Foreign Exchange and} \\
\hline Other Trading Activities & & 130 & & 113 & & 101 & 15 & 29 & 243 & 193 & 26 \\
\hline Securities Gains & & 23 & & 17 & & 23 & 35 & - & 40 & 35 & 14 \\
\hline Other & & 50 & & 56 & & 52 & (11) & (4) & 106 & 82 & 29 \\
\hline \multicolumn{12}{|l|}{Total Noninterest} \\
\hline Income & & , 366 & \$1 & 261 & & , 194 & 8 & 14 & \$2,627 & \$2,310 & 14 \\
\hline
\end{tabular}

Adjusted
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|c|}
\hline \multirow[b]{3}{*}{(In millions)} & \multicolumn{2}{|l|}{\multirow[b]{3}{*}{2006}} & \multicolumn{2}{|l|}{\multirow[b]{3}{*}{1006}} & \multicolumn{2}{|r|}{\multirow[b]{3}{*}{2 Q 05}} & \multicolumn{5}{|l|}{Percent Inc/(Dec)} \\
\hline & & & & & & & \multirow[b]{2}{*}{\[
\begin{gathered}
2 Q 06 \text { vs. } \\
1206
\end{gathered}
\]} & \multirow[b]{2}{*}{\[
\begin{gathered}
2 Q 06 \text { vs. } \\
2 Q 05
\end{gathered}
\]} & \multicolumn{2}{|l|}{Year-to-date} & \multirow[t]{2}{*}{\[
\begin{gathered}
\text { Percent } \\
\text { Inc/ } \\
\text { (Dec) }
\end{gathered}
\]} \\
\hline & & & & & & & & & 2006 & 2005 & \\
\hline \multicolumn{12}{|l|}{Servicing Fees} \\
\hline Securities & \$ & 909 & \$ & 831 & \$ & 775 & 9\% & 17\% & \$1,740 & \$1,525 & 14\% \\
\hline Global Payment & & & & & & & & & & & \\
\hline Services & & 70 & & 70 & & 76 & - & (8) & 140 & 151 & (7) \\
\hline & & 979 & & 901 & & 851 & 9 & 15 & 1,880 & 1,676 & 12 \\
\hline \multicolumn{12}{|l|}{Private Banking and Asset} \\
\hline Management Fees & & 150 & & 141 & & 123 & 6 & 22 & 291 & 245 & 19 \\
\hline Service Charges and Fees & & 91 & & 89 & & 103 & 2 & (12) & 180 & 195 & (8) \\
\hline \multicolumn{12}{|l|}{Foreign Exchange and} \\
\hline Other Trading Activities & & 132 & & 115 & & 103 & 15 & 28 & 247 & 199 & 24 \\
\hline Securities Gains & & 23 & & 17 & & 23 & 35 & - & 40 & 35 & 14 \\
\hline Other & & 51 & & 69 & & 53 & (26) & (4) & 120 & 84 & 43 \\
\hline \multicolumn{12}{|l|}{Total Noninterest} \\
\hline Income & & , 426 & \$1 & , 332 & & 256 & 7 & 14 & \$2,758 & \$2,434 & 13 \\
\hline
\end{tabular}

Unless otherwise indicated, the discussion below refers to noninterest income on both a continuing operations basis and on an adjusted basis.

The increase in noninterest income versus the second quarter of 2005 and the prior quarter reflects positive revenue trends in securities servicing, foreign exchange and other trading, and private banking and asset management. The increase on a year-to-date basis in noninterest income primarily reflects increases in securities servicing, foreign exchange and other trading, private banking and asset management, securities gains, and other income.

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The following table provides the breakdown of securities servicing fees.

\begin{tabular}{crrrrrr} 
Broker-Dealer Services & 66 & 61 & 57 & 8 & 16 & 127
\end{tabular}

Double-digit securities servicing fee growth over the second quarter and year-to-date periods of 2005 reflects strong performance in all securities servicing businesses. On a sequential-quarter basis, fees were up significantly, reflecting seasonally strong issuer services and good growth in broker-dealer services and investor services. See "Institutional Services Segment" in "Business Segment Review" for additional details.

On a continuing operations basis, global payment services fees decreased from the second quarter and year-to-date periods of 2005 but increased slightly on a sequential-quarter basis. The decline from last year reflects customers paying with higher compensating balances in lieu of fees. The sequential quarter increase primarily reflects growth from U.S. financial institutions. On an invoiced services basis, total revenue was up \(6 \%\) over the second quarter of 2005 and 5\% on a sequential-quarter basis. Performance trends on an adjusted basis were relatively consistent with the continuing operations basis.

Private banking and asset management fees increased significantly from the second quarter and year-to-date periods of 2005 primarily due to acquisitions and higher fees in private banking. On a sequential-quarter basis, growth is attributable to higher fees at Ivy Asset Management and Alcentra as well as the full quarter impact of the Urdang acquisition, which closed on March 2, 2006. Total assets under management for private banking and asset management were \$116 billion, up from \$105 billion at June 30, 2005 and \(\$ 113\) billion at March 31, 2006.

Service charges and fees were down from the second quarter and year-todate periods of 2005 reflecting lower capital markets activity. On a sequential-quarter basis, service charges and fees were up reflecting higher underwriting fees.

Foreign exchange and other trading revenues were up significantly from the second quarter and year-to-date periods of 2005 . Foreign exchange was up from the 2005 periods and sequentially due to higher customer volumes driven by cross-border investment flows, good new business activity, and increased volatility. Other trading was up from the 2005 periods and sequentially primarily due to stronger results in equity and interest rate derivatives, and in fixed income trading.

Securities gains in the second quarter were flat with the year-ago quarter and up significantly on a sequential-quarter basis. The gains in the quarter were primarily attributable to exceptionally strong returns on investments in the sponsor fund portfolio. Securities gains were up in the first six months of 2006 versus a year ago reflecting favorable market conditions and liquidity in the private equity markets.

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

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investment income primarily reflects the Company's proportionate share of the income from its investment in Wing Hang Bank Limited, AIB/BNY Securities

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}

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
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|}
\hline & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{\(2 Q 06\)}} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{1206}} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{2Q05}} & \multicolumn{4}{|r|}{Year-to-date} \\
\hline (In millions) & & & & & & & & 006 & & 05 \\
\hline Asset-Related Gains & \$ & 18 & \$ & 34 & \$ & 35 & \$ & 52 & \$ & 49 \\
\hline Equity Investment Income & & 14 & & 11 & & 10 & & 25 & & 22 \\
\hline Other & & 18 & & 11 & & 7 & & 29 & & 11 \\
\hline Other Noninterest Income from Continuing Operations & & 50 & & 56 & & 52 & & 106 & & 82 \\
\hline Other Noninterest Income from Discontinued Operations & & 1 & & 13 & & 1 & & 14 & & 2 \\
\hline Adjusted Other Noninterest Income & \$ & 51 & \$ & 69 & \$ & 53 & \$ & 120 & \$ & 84 \\
\hline
\end{tabular}

Other noninterest income on an adjusted basis decreased slightly versus the second quarter of 2005 and was down significantly from the first quarter of 2006. The first quarter of 2006 includes a pre-tax gain of \(\$ 31\) million related to the conversion of the Company's New York Stock Exchange ("NYSE") seats into cash and shares of NYSE Group, Inc. common stock. The year-to-date period of 2005 includes a \(\$ 17\) million gain on the sale of the company's interest in Financial Models Company, Inc.

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Net Interest Income
----------------------

Continuing Operations


Spread
Net Yield on Interest
Earning Assets
\(1.29 \% 1.37 \% 1.54 \%\)
\(1.95 \quad 1.95 \quad 2.01\)
\(1.33 \% 1.60 \%\)
1.952 .03

Adjusted
---------


\begin{abstract}
Net interest income on a continuing operations basis and on an adjusted basis increased from the year ago quarter reflecting higher interest earning assets and the higher value of interest-free balances in a rising rate environment. Average earning assets increased to \(\$ 75.3\) billion in the second quarter of 2006 from \(\$ 66.7\) billion in last year's second quarter. Net interest income increased on a sequential-quarter basis reflecting an increase in interest earning assets due to higher foreign deposits, principally in the Company's corporate trust and custody businesses, one additional day in the quarter, and a \(\$ 6\) million impact of a cumulative adjustment in the Company's reserve position with the Federal Reserve in the first quarter of 2006 . On a year-to-date basis, net interest income increased reflecting the same factors impacting the quarterly results.

On a continuing operations basis, the net interest income rate spread was \(1.29 \%\) in the second quarter of 2006 , compared with \(1.54 \%\) in the second quarter of 2005 and \(1.37 \%\) in the first quarter of 2006 . The net yield on interest earning assets was \(1.95 \%\) in the second quarter of 2006 , compared with \(2.01 \%\) in the second quarter of 2005 and \(1.95 \%\) in the first quarter of 2006 .

On a continuing operations basis, the year-to-date net interest income spread was \(1.33 \%\) in 2006 compared with \(1.60 \%\) in 2005 , while the net yield on interest earning assets was \(1.95 \%\) in 2006 and \(2.03 \%\) in 2005.
\end{abstract}

\footnotetext{
Noninterest Expense and Income Taxes
}

Continuing Operations


Adjusted
---------
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|c|}
\hline \multirow[b]{3}{*}{(Dollars in millions)} & \multicolumn{2}{|r|}{\multirow[b]{3}{*}{\(2 Q 06\)}} & \multicolumn{2}{|r|}{\multirow[b]{3}{*}{1206}} & \multicolumn{2}{|r|}{\multirow[b]{3}{*}{\(2 Q 05\)}} & \multicolumn{5}{|l|}{Percent Inc/(Dec)} \\
\hline & & & & & & & & & \multicolumn{2}{|l|}{Year-to-date} & \multirow[t]{2}{*}{Percent Inc/ (Dec)} \\
\hline & & & & & & & \multicolumn{2}{|l|}{\[
\begin{array}{cc}
2 Q 06 \text { vs. } 2206 \text { vs. } \\
1206 & 2 Q 05
\end{array}
\]} & 2006 & \[
2005
\] & \\
\hline \multicolumn{12}{|l|}{Salaries and} \\
\hline Employee Benefits & \$ & 723 & \$ & 668 & \$ & 640 & 8\% & 13\% & \$1,391 & \$1,258 & 11\% \\
\hline Net Occupancy & & 86 & & 88 & & 82 & (2) & 5 & 174 & 160 & 9 \\
\hline Furniture and Equipment & & 50 & & 53 & & 51 & (6) & (2) & 103 & 103 & - \\
\hline Clearing & & 53 & & 50 & & 42 & 6 & 26 & 103 & 88 & 17 \\
\hline Sub-custodian Expenses & & 36 & & 34 & & 24 & 6 & 50 & 70 & 47 & 49 \\
\hline Software & & 53 & & 56 & & 55 & (5) & ( 4 ) & 109 & 108 & 1 \\
\hline Communications & & 23 & & 27 & & 22 & (15) & 5 & 50 & 45 & 11 \\
\hline \multicolumn{12}{|l|}{Amortization} \\
\hline of Intangibles & & 15 & & 13 & & 10 & 15 & 50 & 28 & 18 & 56 \\
\hline Other & & 209 & & 189 & & 197 & 11 & 6 & 398 & 373 & 7 \\
\hline \multicolumn{12}{|l|}{Total Noninterest} \\
\hline Expense & & 248 & & 178 & \$ & 123 & 6 & 11 & \$2,426 & \$2,200 & 10 \\
\hline
\end{tabular}

Unless otherwise indicated, the discussion below refers to noninterest expense on both a continuing operations basis and on an adjusted basis.

Noninterest expense was up compared with the second quarter of 2005 and the first quarter of 2006 . The increase versus the year-ago quarter reflects
increased staffing costs associated with new business and acquisitions, and higher incentive compensation as well as higher pension expenses.

Relative to the year-ago periods and sequentially, salaries and benefits rose as a result of: a charge of \(\$ 12\) million associated with the implementation of SFAS \(123(R)\) related to the retirement provisions of equity compensation programs; higher incentive compensation related to revenue growth; acquisitions; and increased severance, temporary help, and medical costs. Pension expense was also higher on a year-over-year basis. Severance expense in the second quarter of 2006 included \(\$ 5\) million related to the businesses being sold as part of the transaction with JPMorgan Chase.

Clearing and sub-custodian expenses were higher year-over-year and on a sequential-quarter basis reflecting increased transaction volumes.

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Other noninterest expense is attributable to vendor services, business development, legal expenses, settlements and claims, and other. 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 four categories is shown below:

Other Noninterest Expense
\begin{tabular}{|c|c|c|c|c|c|c|c|c|}
\hline \multirow[b]{2}{*}{(In millions)} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{2 Q06}} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{1206}} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{2Q05}} & \multicolumn{2}{|l|}{Year-to-date} \\
\hline & & & & & & & 2006 & 2005 \\
\hline Vendor Services & \$ & 88 & \$ & 71 & \$ & & \$159 & \$145 \\
\hline Business Development & & 28 & & 23 & & 24 & 51 & 44 \\
\hline Legal Fees, Settlements and Claims & & 13 & & 22 & & 30 & 35 & 49 \\
\hline Other & & 54 & & 48 & & 45 & 102 & 91 \\
\hline Other Noninterest Expense from Continuing Operations & & 183 & & 164 & & 174 & 347 & 329 \\
\hline Other Noninterest Expense from Discontinued Operations & & 26 & & 25 & & 23 & 51 & 44 \\
\hline Adjusted Other Noninterest Expense & \$ & 209 & \$ & 189 & \$ & 197 & \$398 & \$373 \\
\hline
\end{tabular}

Other expenses were higher compared with the second quarter and year-todate periods of 2005 reflecting higher costs for advertising, travel and entertainment, and employment agency fees, as well as vendor services related expenses associated with business growth. On a sequential-quarter basis, the increase in vendor services was due to higher Depository Trust Company and consulting expenses. The sequential increase in business development primarily reflects seasonally higher travel and entertainment expenses. The decline in legal fees, settlements and claims reflects the settlement of certain regulatory matters over the past year.

The effective tax rate for the second quarter of 2006 on a continuing operations basis was 33.8\%, compared to \(32.1 \%\) in the second quarter of 2005 and \(32.7 \%\) in the first quarter of 2006 . The effective tax rate for the six-month period ended June 30,2006 was \(33.3 \%\) compared with \(32.1 \%\) for the six-month period ended June 30, 2005. The effective tax rate for the second quarter of 2006 on an adjusted basis was \(35.1 \%\), compared to \(33.4 \%\) in the second quarter of 2005 and \(33.8 \%\) in the first quarter of 2006 . The effective tax rate for the

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six-month period ended June 30,2006 was \(34.4 \%\) compared with \(33.2 \%\) for the sixmonth period ended June 30, 2005. The increases on a year-over-year basis primarily reflect lower expected Section 29 tax credits related to synthetic fuels. The sequential quarter increase also reflects a non-recurring \(\$ 5\) million negative impact from the loss of foreign sales corporation benefits on certain leveraged leases as a result of recent legislation.

The Company's effective tax rate in the future is expected to be impacted by the price of oil, which determines the amount of synthetic fuel tax credits it will receive.

\section*{17}

At June 30, 2006, the Company assumed a \(\$ 72\) average price per barrel after June 30, 2006 to estimate the 2006 benefit from synthetic fuel credits. To the extent the average oil price differs from this assumption, the table below shows the effect on earnings per share ("EPS") for 2006.

(1) June 30,2006 assumption used to compute effective tax rate.

Credit Loss Provision and Net Charge-Offs
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|}
\hline & & & & & & & & \(a r-t\) & - & \\
\hline (In millions) & \multicolumn{2}{|c|}{2206} & \multicolumn{2}{|c|}{1206} & \multicolumn{2}{|r|}{\(2 Q 05\)} & \multicolumn{2}{|r|}{2006} & \multicolumn{2}{|c|}{2005} \\
\hline \multicolumn{11}{|l|}{Provision} \\
\hline Continuing Operations & \$ & (1) & \$ & - & \$ & (3) & \$ & (1) & \$ & (20) \\
\hline Discontinued Operations & & 1 & & 5 & & 8 & & 6 & & 15 \\
\hline Adjusted Total Provision & \$ & - & \$ & 5 & \$ & 5 & \$ & 5 & \$ & ( 5 ) \\
\hline \multicolumn{11}{|l|}{Net (Charge-offs)/Recoveries:} \\
\hline Commercial & \$ & 2 & \$ & 1 & \$ & (2) & \$ & 3 & \$ & (2) \\
\hline Foreign & & 4 & & 2 & & ( 4 ) & & 6 & & ( 4 ) \\
\hline Other & & 1 & & - & & - & & 1 & & - \\
\hline Total Continuing Operations & & 7 & & 3 & & (6) & & 10 & & (6) \\
\hline Discontinued Operations & & ( 6 ) & & (7) & & ( 5 ) & & (13) & & (15) \\
\hline \multicolumn{11}{|l|}{Adjusted Total} \\
\hline Net (Charge-offs)/Recoveries & \$ & 1 & \$ & (4) & \$ & (11) & \$ & (3) & \$ & (21) \\
\hline
\end{tabular}

The sequential increase in the credit to the provision for continuing operations reflects a continued strong credit environment. During the second quarter of 2006, nonperforming loans on a continuing operations basis declined and credit loss recoveries increased.

\section*{18}

BUSINESS SEGMENT REVIEW

Segment Data

The Company has an internal information system that produces performance data for its three 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 determined that it was 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 . All prior periods have been restated to reflect this realignment.

On April 8, 2006, the Company entered into a definitive agreement to sell to JPMorgan Chase substantially all of the assets of the Company's retail and regional middle market banking businesses. The business segment information is reported on a continuing operations basis for all periods presented, but do not include the operations of the JPMorgan Chase corporate trust business, which is expected to be acquired in the fourth quarter. As a result, information related to the Company's retail and regional middle market banking businesses is no longer included in the segment data. See "Discontinued Operations" in the Notes to the Consolidated Financial Statements for a discussion of discontinued operations. The Company currently reports results for three segments, 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
* Corporate and Other Segment

Other specific segment 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

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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 those businesses' products or services. Credit-only relationships and borrowers using both credit and payment services remain in Treasury Services Business. Segments with a net liability position are allocated assets primarily from the securities portfolio.

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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 \& BrokerDealer Services Business (which includes the Company's custody operations.)
* Noninterest income associated with Treasury-related services (global payment services for corporate customers, as well as lending and creditrelated services) is similarly allocated back to the other Institutional Services businesses.
* Support and other indirect expenses are allocated to segments based on internally-developed methodologies.

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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 \(\$ 12.0\) trillion of assets under custody at June 30, 2006. 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 \(\$ 1.7\) trillion in total assets. The Company also services more than \(16 \%\) 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 \(\$ 1.7\) trillion in 27 markets around the world.

The Company's Broker-Dealer Services business clears approximately 50\% of transactions in U.S. Government securities. The Company is a leader in global clearance, clearing equity and fixed income transactions in 101 markets. With over \(\$ 1.2\) 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 691 million shares and clearing one million trades daily. In Execution Services, the Company provides broker-assisted and electronic trading services, transition management, and independent research services. 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. The Company announced on June 30, 2006 that it agreed to join forces with Eze Castle Software and GTCR Golder Ruaner, LLC, a private equity firm, to form a new company called BNY ConvergEx Group. BNY ConvergEx Group will bring together BNY Securities Group's trade execution, commission management, independent research and transition management business with Eze Castle Software, a leading provider of trade order management and related investment technologies.

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

\section*{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 1,255 American and global depositary receipt programs, with a \(64 \%\) market share, servicing leading companies from 61 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 in the United States, servicing more than 17 million shareowners.

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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 150,000 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 an active arranger or agent of syndicated financings for clients in the U.S., having completed 56 transactions totaling in excess of \(\$ 43\) billion during the first half of 2006 .

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 \& BNY Asset Management Segment

The Private Bank \& BNY Asset Management Segment includes traditional banking and trust services for 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 arrange intergenerational wealth transition, which 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 corporations 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 funds of hedge 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 fund of hedge funds firms, offers a comprehensive range of multi-manager hedge fund products and customized portfolio solutions.
* Alcentra offers sophisticated alternative credit investments, including leveraged loans and subordinated and distressed debt.

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* Urdang, a real estate investment firm, 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 securities management and equity portfolio strategies.

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

\section*{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 two 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's 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.

In addition, this segment includes the difference between amounts previously reported in the Company's Retail and Middle Market Banking Segment and the discontinued operations of the Company's retail and regional middle market banking business, which is being sold to JPMorgan Chase.

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Segment Analysis
Institutional Services Segment
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|c|c|c|c|c|c|}
\hline & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{\(2 Q 06\)}} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{1206}} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{2 Q 05}} & \multicolumn{4}{|c|}{Inc/( Dec )} & & & & & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{\begin{tabular}{l}
Inc/ \\
(Dec)
\end{tabular}}} \\
\hline (In millions) & & & & & & & & \[
\begin{gathered}
206 \text { vs. } \\
1206
\end{gathered}
\] & & \[
\begin{gathered}
206 \text { vs. } \\
2 Q 05
\end{gathered}
\] & & Year-t

2006 & - & date & & \\
\hline Net Interest Income & \$ & 337 & \$ & 315 & \$ & 292 & \$ & 22 & \$ & 45 & \$ & 652 & \$ & 572 & \$ & 80 \\
\hline Noninterest Income & & 1,196 & & 1,122 & & 1,045 & & 74 & & 151 & & 2,318 & & 2,046 & & 272 \\
\hline Total Revenue & & 1,533 & & 1,437 & & 1,337 & & 96 & & 196 & & 2,970 & & 2,618 & & 352 \\
\hline Provision for Credit Losses & & 16 & & 16 & & 16 & & - & & - & & 32 & & 32 & & - \\
\hline Noninterest Expense & & 947 & & 906 & & 856 & & 41 & & 91 & & 1,853 & & 1,689 & & 164 \\
\hline Income Before Taxes & & 570 & & 515 & & 465 & & 55 & & 105 & & 1,085 & & 897 & & 188 \\
\hline Average Assets & & 82,666 & & 79,032 & & 74,792 & & 3,634 & & , 874 & & 80,859 & & 74,314 & & 6,545 \\
\hline Average Deposits & & 51,680 & & 49,608 & & 44,271 & & 2,072 & & , 409 & & 50,651 & & 43,791 & & 6,860 \\
\hline
\end{tabular}

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 \(23 \%\) to \(\$ 570\) million for the second quarter of 2006 from \(\$ 465\) million in the second quarter of 2005, and up 11\% from \(\$ 515\) million in the first quarter of 2006. For the first six months of 2006 , income before taxes was up \(21 \%\) to \$1,085 million compared with 2005.

Equity volumes and values were up modestly during the most recent quarter compared with the second quarter of 2005, and cross-border activity levels were strong. As a result, the Company's equity-linked businesses performed well.

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The depositary receipts businesses had its best quarter ever powered by crossborder activity and seasonally strong dividend payments. After excluding the previously disclosed loss of a significant customer, Pershing had good revenue growth and the execution business benefited from high levels of international activity. The Company's global custody and global fund services businesses also had a robust quarter. The fixed income markets were stable, and as a result, the Company's securities lending, broker-dealer services and corporate trust businesses all improved on a year-over-year basis. Other areas demonstrating strong growth include foreign exchange and alternative investment servicing.
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Market Data

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(1) Period End

The S\&P 500 (registered trademark) Index was down 2\% sequentially for the quarter, with average daily price levels essentially flat compared with the first quarter of 2006 . Performance for the NASDAQ (registered trademark) Composite Index was down \(7 \%\) sequentially for the second quarter of 2006 , with average daily prices down by \(2 \%\) from the first quarter of 2006 . The S\&P 500 (registered trademark) Index and the NASDAQ (registered trademark) Composite Index were up \(7 \%\) and \(6 \%\) respectively over the second quarter of 2005 . Globally, the MSCI (registered trademark) EAFE index was flat sequentially but up \(24 \%\) over the second quarter of 2005 . On a sequential-quarter basis,

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combined NYSE and NASDAQ (registered trademark) non-program trading volumes were down an estimated \(2 \%\). Average fixed-income trading volume was down 3\% sequentially.

As of June 30,2006 , assets under custody rose to \(\$ 12.0\) trillion, from \(\$ 10.3\) trillion at June 30,2005 and \(\$ 11.3\) trillion at March 31, 2006. The
increase in assets under custody relative to June 30, 2005 primarily reflects rising equity prices and new business wins. Equity securities comprised \(32 \%\) of the assets under custody at June 30, 2006 compared with \(33 \%\) at March 31, 2006, while fixed income securities were 68\% compared with 67\% at March 31, 2006. Assets under custody in the second quarter of 2006 consisted of assets related to the custody and mutual funds businesses of \(\$ 7.6\) trillion, broker-dealer services assets of \(\$ 2.4\) trillion, and all other assets of \(\$ 2.0\) trillion.

The results for the businesses in the Institutional Services Segment are discussed below.

Investor \& Broker-Dealer Services Business


In the second quarter of 2006, income before taxes in the Investor \& Broker-Dealer Services business increased to \(\$ 218\) million from \(\$ 187\) million in the second quarter of 2005 and \(\$ 198\) million in the first quarter of 2006 . For the first six months of 2006 , income before taxes was \(\$ 416\) million compared with \(\$ 372\) million in 2005. The year-over-year and sequential quarter increases reflect improvements in both net interest income and noninterest income.

Noninterest income was \(\$ 524\) million in the second quarter of 2006 , compared with \(\$ 461\) million in the second quarter of 2005 and \(\$ 490\) million in the first quarter of 2006. The increase in noninterest income in the second quarter of 2006 relative to both time periods 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. On a year-to-date basis, noninterest income increased to \(\$ 1,014\) million from \(\$ 902\) million, reflecting the same factors impacting the quarterly results.

Investor services fees increased from the year-ago quarter because of higher volumes within securities lending and higher custody fees, reflecting improvements in cross-border transaction volumes and market price levels as well as new business. Sequential performance reflects improved securities lending fees, and higher global fund services and custody fees. On a year-todate basis, investor services fees increased compared with 2005, reflecting the same factors driving the year-over-year quarterly increase.

Broker-dealer services fees improved versus the year-ago and sequential
periods as a result of strong performance in domestic and global collateral management fees, an increase in transaction volumes and good net new business flows. The Company now handles approximately \(\$ 1.2\) trillion of financing for the Company's broker-dealer clients daily through collaterized financing agreements, up approximately 17\% from a year ago.

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Net interest income in the Investor \& Broker-Dealer Services business was \(\$ 155\) million in the second quarter of 2006 , compared with \(\$ 138\) million in the second quarter of 2005 and \(\$ 149\) million in the first quarter of 2006 . On a year-over-year basis, net interest income growth in the second quarter reflects increased deposit flows from customers in both businesses and higher rates. Average deposits generated by the Investor \& Broker-Dealer Services business were \(\$ 32.9\) billion in the second quarter of 2006 , compared with \(\$ 27.1\) billion in the second quarter of 2005 and \(\$ 31.8\) billion in the first quarter of 2006 . Average assets in the business were \(\$ 39.8\) billion in the second quarter of 2006, compared with \(\$ 36.4\) billion in the second quarter of 2005 and \(\$ 38.2\) billion in the first quarter of 2006 . For the first six months of 2006 , average deposits were \(\$ 32.4\) billion compared with \(\$ 27.5\) billion in 2005 . On the same basis, average assets in the business were \(\$ 39.0\) billion in 2006 compared with \(\$ 36.4\) billion in 2005.

Noninterest expense was \(\$ 458\) million in the second quarter of 2006 , compared with \(\$ 410\) million in the second quarter of 2005 and \(\$ 438\) million in the first quarter of 2006 . The year-over-year increase in noninterest expense was due to higher costs tied to increased activity levels and higher technology, pension, and occupancy expense. The sequential rise in noninterest expense in the second quarter was attributable primarily to higher salaries, benefits, and sub-custody expenses associated with revenue growth. For the first six months of 2006, noninterest expense increased to \(\$ 896\) million compared with \(\$ 803\) million in 2005 , reflecting costs associated with revenue growth and higher technology and pension costs.

Net charge-offs were zero in the second quarter of 2006 , compared with zero in the second quarter of 2005 and \(\$ 1\) million in the first quarter of 2006 . On a year-to-date basis, net charge-offs were \(\$ 1\) million compared with zero in 2005. Nonperforming assets were \(\$ 3\) million at June 30,2006 , compared with \(\$ 15\) million at June 30, 2005 and \(\$ 4\) million at March 31, 2006.

Execution \& Clearing Services Business

\begin{tabular}{lrrrrrrrr} 
Customers and & & & & & \\
Broker-Dealers & 5,034 & 5,231 & 5,984 & \((197)\) & \((950)\) & 5,132 & 6,184 & \((1,052)\) \\
Nonperforming Assets & - & - & 1 & - & \((1)\) & - & 1 & \((1)\) \\
\begin{tabular}{l} 
Net Charge-offs/ \\
(Recoveries)
\end{tabular} & \((4)\) & \((2)\) & 5 & \((2)\) & \((9)\) & \((6)\) & 5 & (11)
\end{tabular}

\begin{abstract}
In the second quarter of 2006, income before taxes in the Execution \& Clearing Services Business increased to \(\$ 123\) million from \(\$ 94\) million a year ago and decreased from \(\$ 154\) million in the first quarter of 2006 . The increase over the second quarter of 2005 reflects strong growth in net interest income, higher fees for value added services at Pershing, and the acquisition of Lynch, Jones \& Ryan ("LJR"), Inc. in July 2005. The sequential quarter decrease reflects the \(\$ 31\) million gain on New York Stock Exchange seats in the first quarter and the full second quarter impact of the previously disclosed loss of a significant customer at Pershing partially offset by good organic growth at Pershing. On a year-to-date basis, income before taxes increased to \$277 million from \(\$ 176\) million in 2005. The increase from a year-ago reflects the same factors impacting the quarterly year-over-year increase as well as the \$31 million gain on the sale of New York Stock Exchange seats.
\end{abstract}

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Noninterest income was \(\$ 359\) million in the second quarter of 2006 , compared with \(\$ 319\) million in the second quarter of 2005 and \(\$ 390\) million in the first quarter of 2006 . For the first six months of 2006 , noninterest income increased to \(\$ 749\) million from \(\$ 636\) million in 2005.

Execution and clearing fees increased from the second quarter and year-todate periods of 2005, reflecting growth in value-added fees at Pershing and stronger global transition management and cross-border trading activity in execution services. On a sequential basis, execution and clearing fees were down slightly, as good organic growth in fees at Pershing largely offset the full quarter impact of the previously disclosed loss of a significant customer. Excluding the impact of this customer, total active accounts and customer assets at Pershing increased sequentially by \(4 \%\) and \(3 \%\), respectively.

Net interest income in the Execution \& Clearing Services business was \(\$ 66\) million in the second quarter of 2006 , compared with \(\$ 52\) million in the second quarter of 2005 and \(\$ 61\) million in the first quarter of 2006 . On a year-todate basis, net interest income was \(\$ 127\) million, up from \(\$ 97\) million in 2005. The increase in net interest income reflect the benefit of rising interest rates on spreads at Pershing, partially offset by the recent loss of a customer discussed above.

Average assets in the business were \(\$ 15.1\) billion in the second quarter of 2006, compared with \(\$ 14.3\) billion in the second quarter of 2005 and \(\$ 15.0\) billion in the first quarter of 2006 . For the first six months of 2006 , average assets were \(\$ 15.0\) billion compared with \(\$ 14.2\) billion in 2005 . Average payables to customers and broker-dealers were \(\$ 5.0\) billion in the second quarter of 2006 , compared with \(\$ 6.0\) billion in the second quarter of 2005 and \(\$ 5.2\) billion in the first quarter of 2006 . The decrease in second quarter balances reflects the previously disclosed loss of a significant customer. For the first six months of 2006, average payables to customers and broker-dealers were \(\$ 5.1\) billion compared with \(\$ 6.2\) billion in 2005.

Noninterest expense was \(\$ 302\) million in the second quarter of 2006 , compared with \(\$ 277\) million in the second quarter of 2005 and \(\$ 297\) million in the first quarter of 2006. The increase in noninterest expense on a year-overyear basis was due to stronger business activity, higher technology expenses and the addition of expenses of LJR. The increase in noninterest expense

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}
sequentially was attributable to increased business activity partially offset by lower expenses due to the loss of a significant customer at Pershing and lower legal expense. For the first six months of 2006 , noninterest expense was \(\$ 599\) million compared with \(\$ 557\) million in 2005 . The increase reflects the same factors impacting the quarterly year-over-year increase.

Net charge-offs were a recovery of \(\$ 4\) million in the second quarter of 2006, charge-offs of \(\$ 5\) million in the second quarter of 2005 and a recovery of \(\$ 2\) million in the first quarter of 2006, respectively. On a year-to-date basis, net charge-offs were a recovery of \(\$ 6\) million compared with charge-offs of \(\$ 5\) million in 2005. Nonperforming assets were zero at June 30, 2006, compared with \$1 million at June 30, 2005 and zero at March 31, 2006.

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Issuer Services Business


In the second quarter of 2006, income before taxes in the Issuer Services Business increased to \(\$ 175\) million from \(\$ 134\) million in the second quarter of 2005 and \(\$ 120\) million in the first quarter of 2006 . For the first six months of 2006, income before taxes increased to \(\$ 295\) million from \(\$ 239\) million in 2005. The year-over-year increases in 2006 reflect growth in net interest income and higher corporate trust and depositary receipt fees. The sequential quarter increase reflects seasonally higher depositary receipt fees.

Noninterest income was \(\$ 240\) million in the second quarter of 2006, compared with \(\$ 194\) million in the second quarter of 2005 and \(\$ 179\) million in the first quarter of 2006 . For the first six months of 2006 , noninterest income was \(\$ 419\) million compared with \(\$ 361\) million in 2005 . Issuer services fees increased substantially versus the year-ago periods and on a sequential quarter basis. This quarter's results were the best ever for the depositary receipt business, which is typically strong in the second quarter due to the timing of foreign dividend payments. This quarter further benefited from both a higher level of net issuance, reflecting the continued growth in cross-border investing activity, as well as increased corporate actions related to mergers, acquisitions and spin-offs. Growth in corporate trust revenues was primarily attributable to activity in structured and global trust products.

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Net interest income in the Issuer Services business was \$74 million in the second quarter of 2006 , compared with \(\$ 57\) million in the second quarter of 2005 and \(\$ 67\) million in the first quarter of 2005 . For the first six months of 2006, net interest income was \(\$ 141\) million compared with \(\$ 110\) million in 2005. The increases in net interest income year-over-year and sequentially were driven primarily by the increase in interest rates and higher average assets.

Average deposits generated by the Issuer Services business were \$9.6 billion in the second quarter of 2006 , compared with \(\$ 8.6\) billion in the second quarter of 2005 and \(\$ 8.4\) billion in the first quarter of 2006 reflecting increased liquidity from the Company's issuer services customers. On a year-todate basis, average deposits were \(\$ 9.0\) billion compared with \(\$ 8.1\) billion in 2005. Average assets in the business were \(\$ 15.5\) billion in the second quarter of 2006 , compared with \(\$ 13.4\) billion in the second quarter of 2005 and \(\$ 14.6\) billion in the first quarter of 2006 . On a year-to-date basis, average assets were \(\$ 15.1\) billion compared with \(\$ 13.4\) billion in 2005.

Noninterest expense was \(\$ 135\) million in the second quarter of 2006 , compared with \(\$ 114\) million in the second quarter of 2005 and \(\$ 122\) million in the first quarter of 2006 . For the first six months of 2006 , noninterest expense was \(\$ 257\) million compared with \(\$ 226\) million in 2005 . The rise in noninterest expense year-over-year and sequentially was attributable to higher salaries and benefits and subcustodian expense reflecting increased activity.

Net charge-offs were zero in the second quarter of 2006 , unchanged from the second quarter of 2005 and down from \(\$ 1\) million in the first quarter of 2006. For the first six months of 2006 , net charge-offs were \(\$ 1\) million

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compared with zero in 2005. Nonperforming assets were \(\$ 3\) million at June 30 , 2006, compared with \(\$ 16\) million at June 30,2005 and \(\$ 4\) million at March 31, 2006 .

Treasury Services Business


In the second quarter of 2006, income before taxes in the Treasury Services Business was \(\$ 54\) million, compared with \(\$ 50\) million in the second quarter of 2005 and \(\$ 43\) million in the first quarter of 2006 . The increase versus a year ago reflects higher asset-related gains in the current quarter. On a year-to-date basis, income before taxes was \(\$ 97\) million compared with \(\$ 110\) million in 2005.

The increase in noninterest income to \(\$ 73\) million in the current period from \(\$ 71\) million in the second quarter of 2005 was due to higher asset-related gains, partially offset by lower underwriting fees from clients in this segment and lower global payments fees as more clients used compensating balances to pay for services. The sequential quarter increase in noninterest income reflects higher foreign exchange related income, underwriting fees, and assetrelated gains. For the first six months of 2006, noninterest income decreased to \(\$ 136\) million from \(\$ 147\) million in 2005.

Net interest income was \(\$ 42\) million in the second quarter of 2006 , compared with \(\$ 45\) million in the second quarter of 2005 and \(\$ 38\) million in the first quarter of 2006 . On a year-over-year basis, the decrease reflects lower credit spreads due to the higher asset quality of the portfolio partially offset by customers using compensating balances to pay for global payment services. For the first six months of 2006, net interest income was \(\$ 80\) million compared with \(\$ 88\) million in 2005. Average assets for the second quarter of 2006 were \(\$ 12.2\) billion, compared with \(\$ 10.7\) billion in the second quarter of 2005 and \(\$ 11.3\) billion in the first quarter of 2006 . For the first six months of 2006, average assets were \(\$ 11.7\) billion compared with \(\$ 10.3\) billion in 2005 . Average deposits were \(\$ 9.0\) billion in the second quarter of 2006 , compared with \(\$ 8.4\) billion in the second quarter of 2005 and \(\$ 9.1\) billion in the first quarter of 2006 . For the first six months of 2006 , average deposits were \(\$ 9.1\) billion compared with \(\$ 8.0\) billion in 2005.

The provision for credit losses, which is assessed on a long-term credit cycle basis (see "Business Segments Accounting Principles"), was \(\$ 9\) million in the second quarter of 2006, compared with \(\$ 11\) million in the second quarter of 2005 and \(\$ 9\) million in the first quarter of 2006 . For the first six months of 2006, provision for credit losses was \(\$ 18\) million compared with \(\$ 22\) million in 2005. The year-over-year decrease reflects improved credit quality.

Net charge-offs in the Treasury Services business were a recovery of \(\$ 2\) million in the second quarter of 2006, compared with a charge-off of \(\$ 1\) million in both the second quarter of 2005 and the first quarter of 2006 . For the first six months of 2006, net charge-offs were a recovery of \(\$ 1\) million compared with

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a charge-off of \(\$ 1\) million in 2005. Nonperforming assets were \(\$ 11\) million at June 30, 2006, compared with \(\$ 48\) million at June 30, 2005, and \(\$ 12\) million at March 31, 2006.

Noninterest expense in the second quarter of 2006 was \(\$ 52\) million, compared to \(\$ 55\) million in the second quarter of 2005 and \(\$ 49\) million in the first quarter of 2006 . For the first six months of 2006 , noninterest expense was \(\$ 101\) million compared with \(\$ 103\) million in 2005 . The decrease in noninterest expense year-over-year was due in part to lower compensation expenses.

Private Bank \& BNY Asset Management Segment
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|c|c|c|c|c|c|}
\hline \multirow[b]{2}{*}{(In millions)} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{2006}} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{1206}} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{2205}} & \multicolumn{4}{|l|}{\multirow[t]{2}{*}{}} & \multicolumn{4}{|r|}{Year-to-date} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{\[
\begin{aligned}
& \text { Inc/ } \\
& \text { (Dec) }
\end{aligned}
\]}} \\
\hline & & & & & & & & & & & & 2006 & & 2005 & & \\
\hline Net Interest Income & \$ & 16 & \$ & 17 & \$ & 16 & \$ & (1) & \$ & - & \$ & 33 & \$ & 33 & \$ & - \\
\hline Noninterest Income & & 137 & & 129 & & 114 & & 8 & & 23 & & 266 & & 226 & & 40 \\
\hline Total Revenue & & 153 & & 146 & & 130 & & 7 & & 23 & & 299 & & 259 & & 40 \\
\hline Provision for Credit Losses & & - & & - & & 1 & & - & & (1) & & - & & 2 & & (2) \\
\hline Noninterest Expense & & 99 & & 90 & & 78 & & 9 & & 21 & & 189 & & 157 & & 32 \\
\hline Income Before Taxes & & 54 & & 56 & & 51 & & (2) & & 3 & & 110 & & 100 & & 10 \\
\hline Average Assets & & 2,448 & & 2,543 & & 2,317 & & (95) & & 131 & & 2,495 & & 2,212 & & 283 \\
\hline Average Deposits & & 2,205 & & 1,772 & & 1,851 & & 433 & & 354 & & 1,990 & & 1,817 & & 173 \\
\hline Nonperforming Assets & & - & & 1 & & 1 & & (1) & & (1) & & - & & 1 & & (1) \\
\hline Net Charge-offs/ (Recoveries) & & (1) & & - & & - & & (1) & & (1) & & (1) & & - & & (1) \\
\hline
\end{tabular}

In the second quarter of 2006, income before taxes in the Private Bank \& BNY Asset Management Segment was \(\$ 54\) million, compared with \(\$ 51\) million in the second quarter of 2005 and \(\$ 56\) million in the first quarter of 2006 . The improvement year-over-year is attributable to the acquisitions of Alcentra and Urdang as well as higher fee levels in Private Banking.

Noninterest income was \(\$ 137\) million in the second quarter of 2006 , compared with \(\$ 114\) million in the second quarter of 2005 and \(\$ 129\) million in the first quarter of 2006 . Private bank and asset management revenues in the second quarter of 2006 were up sequentially and year-over-year. The year-overyear growth reflects the acquisitions of Alcentra and Urdang as well as midsingle digit organic growth. On a sequential quarter basis, growth is attributable to higher fees at Ivy Asset Management and Alcentra as well as the full quarter impact of Urdang. The S\&P 500 (registered trademark) Index was down 2\% from March 31, 2006, with average daily price levels essentially flat from March 31, 2006. Performance for the NASDAQ (registered trademark) Composite Index was down \(7 \%\) for the quarter, with average daily prices down by \(2 \%\) from the first quarter of 2006 .

Assets Under Management - Asset Management Sector
\begin{tabular}{lrrr} 
(In billions) - Estimated & 2006 & 1206 & \(2 Q 05\) \\
Equity Securities & --36 & \(\$ 37\) & \(\$ 36\) \\
Fixed Income Securities & 21 & 21 & 22 \\
Alternative Investments & 28 & 26 & 15 \\
Liquid Assets & 31 & 29 & 32 \\
& ---- & ---- & ---- \\
Total Assets Under Management & \(\$ 116\) & \(\$ 113\) & \(\$ 105\) \\
& \(====\) & \(====\) & \(====\)
\end{tabular}

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Assets under management ("AUM") were \$116 billion at June 30, 2006, compared with \(\$ 105\) billion at June 30, 2005, and \(\$ 113\) billion at March 31, 2006. The year-over-year increases in AUM primarily reflect the acquisition of Alcentra and Urdang. The sequential quarter growth reflects growth in alternative investments. Institutional clients represent \(72 \%\) of AUM while individual clients equal \(28 \%\). At June 30 , 2006 , such assets were invested \(31 \%\) in equities, \(18 \%\) in fixed income, and \(24 \%\) in alternative investments, with the
remaining amount invested in liquid assets.

Net interest income in the Private Bank \& BNY Asset Management Segment was \(\$ 16\) million in the second quarter of 2006 , essentially flat in comparison to the second quarter of 2005 and the first quarter of 2006 . For the first six months of 2006 and 2005, net interest income was \(\$ 33\) million. Average deposits generated by the Private Bank \& BNY Asset Management Segment were \$2.2 billion in second quarter of 2006 , compared with \(\$ 1.9\) billion in the second quarter of 2005 and \(\$ 1.8\) billion in the first quarter of 2006 . For the first six months of 2006, average deposits were \(\$ 2.0\) billion compared with \(\$ 1.8\) billion in 2005. Average assets in the segment were \(\$ 2.4\) billion in the second quarter of 2006 , compared with \(\$ 2.3\) billion in the second quarter of 2005 and \(\$ 2.5\) billion in the first quarter of 2006 . For the first six months of 2006 , average assets were \(\$ 2.5\) billion compared with \(\$ 2.2\) billion in the first six months of 2005 .

Noninterest expense was \(\$ 99\) million in the second quarter of 2006 , compared with \(\$ 78\) million in the second quarter of 2005 and \(\$ 90\) million in the first quarter of 2006 . For the first six months of 2006 , noninterest expense was \(\$ 189\) million compared with \(\$ 157\) million in 2005 . Relative to a year ago, the increase reflects the acquisitions of Alcentra and Urdang as well as higher compensation, technology, and legal staffing costs. The increase in noninterest expense on a sequential basis was primarily attributable to higher compensation costs.

Net charge-offs were a recovery of \(\$ 1\) million in the second quarter of 2006, and zero in the second quarter of 2005 and the first quarter of 2006 , respectively. On a year-to-date basis, net charge-offs were a recovery of \(\$ 1\) million in 2006 compared with zero in 2005. Nonperforming assets were zero at June 30, 2006, compared with \(\$ 1\) million at June 30, 2005, and \(\$ 1\) million at March 31, 2006.

Corporate and Other Segment


In the second quarter of 2006 , income before taxes in the corporate and Other Segment was a loss of \(\$ 33\) million, compared with a loss of \(\$ 11\) million in the second quarter of 2005 and a loss of \(\$ 36\) million in the first quarter of 2006 .

Net interest income in the Corporate and Other Segment was \(\$ 5\) million in the second quarter of 2006 , compared with \(\$ 21\) million in the second quarter of 2005 and \(\$ 7\) million in the first quarter of 2006 . For the first six months of 2006, net interest income was \(\$ 12\) million compared with \(\$ 45\) million in 2005 . The decrease in net interest income over the second quarter of 2005 reflects

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lower leasing income and the impact of accounting for the retail and regional middle market banking business as discontinued operations.

Noninterest income was \(\$ 33\) million in the second quarter of 2006 , compared with \(\$ 35\) million in the second quarter of 2005 and \(\$ 10\) million in the first quarter of 2006 . The increase in noninterest income in the second quarter of 2006 over the first quarter of 2006 is attributable to higher securities and other investment gains. For the first six months of 2006 , noninterest income was \(\$ 43\) million compared with \(\$ 38\) million in 2005 . Securities gains were \(\$ 23\) million in the second quarter of 2006 , compared with \(\$ 23\) million in the second quarter of 2005 and \(\$ 17\) million in the first quarter of 2006 . Securities gains on a year-to-date basis were \(\$ 40\) million in 2006 compared with \(\$ 35\) million in 2005 .

Provision for credit losses was a credit of \(\$ 17\) million in the second quarter of 2006 , compared with a \(\$ 20\) million credit in the second quarter of 2005 and a \(\$ 16\) million credit in the first quarter of 2006 . For the first six months of 2006 , provision for credit losses was a \(\$ 33\) million credit compared with a credit of \(\$ 54\) million in 2005 . 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. As such, the favorable credit environment has currently resulted in the business segments absorbing more than the Company's aggregate reported credit provision.

Noninterest expense includes unallocated corporate overhead, amortization of goodwill, nonrecurring items, and certain expenses previously allocated to the Retail and Middle Market Banking Segment that are not included in the businesses sold to JPMorgan Chase. Noninterest expense was \(\$ 88\) million in the second quarter of 2006 , compared with \(\$ 87\) million in the second quarter of 2005 and \(\$ 69\) million in the first quarter of 2006 . For the first six months of 2006, noninterest expense was \(\$ 157\) million compared with \(\$ 146\) million in 2005. The year-over-year growth includes higher intangible amortization. The Company expects certain costs previously allocated to the Retail and Middle Market Banking Segment now included with Corporate and Other Segment will be reallocated to the Institutional Services Segment when JPMorgan Chase's corporate trust business is acquired.

Net charge-offs were zero in the second quarter of 2006 , compared with zero in the second quarter of 2005 and a recovery of \(\$ 4\) million in the first quarter of 2006 . On a year-to-date basis, net charge-offs were a recovery of \(\$ 4\) million in 2006 compared with zero in 2005. Nonperforming assets were \(\$ 15\) million at June 30, 2006, compared with \(\$ 6\) million at June 30,2005 , and \(\$ 4\) million at March 31, 2006. The increase in nonperforming assets at June 30 , 2006 reflects the buyout of debt associated with a lease on an aircraft that is being positioned for sale as part of a workout strategy.

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Significant other items related to the Corporate and Other Segment are presented in the following table.
\begin{tabular}{|c|c|c|c|c|c|}
\hline (In millions) & 2006 & 1206 & 2 Q05 & 2006 & 2005 \\
\hline
\end{tabular}

Items impacting net interest income:
Cost to Carry Goodwill and Intangibles
Tax Equivalent Basis
\$ (25) \$ (25) \$ (25)
(25) \$ (50)
\$ (50)
(14)

Items impacting noninterest expense:
Goodwill and Intangibles Amortization
\$ 15
15
\$
13 \$
10 \$ 28
\$ 18

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 were allocated to the other two segments, it would be assigned on the basis of 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 the second quarter of 2006 , these included a charge of \(\$ 12\) million associated with the implementation of SFAS \(123(\mathrm{R})\) related to the retirement provisions of equity compensation programs. In the first quarter of 2006 , these included the impact of the \(\$ 6\) million cumulative adjustment in the Company's reserve position with the Federal Reserve Bank. Alternatively, this item could be allocated 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.



\begin{tabular}{|c|c|c|c|c|c|c|c|}
\hline \multirow[t]{2}{*}{(Dollars in millions)} & \multicolumn{4}{|c|}{Execution} & \multicolumn{3}{|c|}{Private} \\
\hline & Investor \& & \& & & & Sub-total & Bank \& & Corp \\
\hline For the Six Months & Broker-Dealer & Clearing & Issuer & Treasury & Institutional & BNY Asset & \\
\hline Ended June 30, 2006 & Services & Services & Services & Services & Services & Management & Ot \\
\hline
\end{tabular}
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|c|c|c|}
\hline Net Interest Income & \$ & 304 & \$ & 127 & \$ & 141 & \$ & 80 & \$ & 652 & \$ & 33 & \$ \\
\hline Noninterest Income & & 1,014 & & 749 & & 419 & & 136 & & 2,318 & & 266 & \\
\hline Total Revenue & & 1,318 & & 876 & & 560 & & 216 & & 2,970 & & 299 & \\
\hline Provision for Credit Losses & & 6 & & - & & 8 & & 18 & & 32 & & - & \\
\hline Noninterest Expense & & 896 & & 599 & & 257 & & 101 & & 1,853 & & 189 & \\
\hline Income Before Taxes & \$ & 416 & \$ & 277 & \$ & 295 & \$ & 97 & \$ & 1,085 & \$ & 110 & \$ \\
\hline Contribution & & & & & & & & & & & & & \\
\hline Percentage (1) & & 35\% & & 23\% & & 25\% & & 8\% & & 91\% & & 9\% & \\
\hline Average Assets & \$ & 39,006 & \$ & 036 & \$ & 071 & & 746 & & 0,859 & \$ & 495 & \$10 \\
\hline
\end{tabular}


\section*{35}

\section*{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" in the Company's 2005 Annual Report on Form 10-K. 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.

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 "Consolidated Balance Sheet Review" 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 June 30, 2006, the unallocated allowance was \(23 \%\) of the total allowance. If the unallocated allowance were five percent higher or lower, the allowance would have increased or decreased by \(\$ 24\) 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 \(\$ 75\) million, while if each credit were rated one grade worse, the allowance would have increased by \(\$ 134\) million.

Similarly, if the loss given default were one rating worse, the allowance would have increased by \(\$ 47\) million, while if the loss given default were one rating better, the allowance would have decreased by \(\$ 41\) million.

For impaired credits, if the fair value of the loans were \(10 \%\) higher or lower, the allowance would have decreased or increased by \(\$ 1\) million, respectively.

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Valuation of Derivatives and Securities Where Quoted Market Prices Are Not
Available
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When quoted market prices are not available for derivatives and securities values, such values are determined at 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 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 "Summary of Significant Accounting and Reporting Policies" of the Notes to Consolidated Financial Statement in the Company's 2005 Annual Report on Form 10-K.

To assist in assessing the impact of a change in valuation, at June 30, 2006, approximately \(\$ 2.5\) billion of the Company's portfolio of securities and derivatives is not priced based on quoted market prices because no such quoted market prices are available. A change of \(2.5 \%\) in the valuation of these securities and derivatives would result in a change in pre-tax income of \(\$ 62\) 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 FASB Statement No. 141 ("SFAS 141"), "Business Combinations". Goodwill (\$3,784 million at June 30, 2006) and indefinite-lived intangible assets (\$378 million at June 30, 2006) 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, indefinite-lived intangibles, and other intangibles requires subjective judgments concerning estimates of the fair value of acquired assets. The goodwill impairment test is performed in two phases. The first step of the goodwill impairment test 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 intangible assets (\$507 million at June 30, 2006) 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

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similar assets, market multiples, discounted cash flow analysis and other determinates. 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 that require amortization. See Note "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, indefinite-lived intangibles, or other intangible asset impairment charge, at June 30, 2006, the Company has \(\$ 4.7\) billion of goodwill, indefinite-lived intangibles, and other intangible assets. The impact of a \(5 \%\) impairment charge would result in reduction in pre-tax income of approximately \(\$ 233\) million.
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Pension Accounting

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The Company has defined benefit plans covering approximately 13,900 U.S. employees and approximately 3,175 non-U.S. employees at September 30, 2005.

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:
\begin{tabular}{|c|c|c|c|c|c|c|c|c|}
\hline (Dollars in millions, except per share amounts) & & 2006 & & 2005 & & 2004 & & 2003 \\
\hline \multicolumn{9}{|l|}{Domestic Plans:} \\
\hline Long-Term Rate of Return on Plan Assets & & \(7.88 \%\) & & 8.25\% & & 8.75\% & & 9.00\% \\
\hline Discount Rate & & 5.88 & & 6.00 & & 6.25 & & 6.50 \\
\hline Market-Related Value of Plan Assets(1) & \$ & 1,324 & \$ & 1,502 & \$ & 1,523 & \$ & 1,483 \\
\hline ESOP Stock Price(1) & & 30.46 & & 30.67 & & 27.88 & & 33.30 \\
\hline Net U.S Pension Credit/(Expense) & & & \$ & (17) & \$ & 31 & \$ & 46 \\
\hline All other Pension Credit/(Expense) & & & & (9) & & (7) & & (7) \\
\hline Total Pension Credit/(Expense) (2) & & & \$ & (26) & \$ & 24 & \$ & 39 \\
\hline
\end{tabular}
(1) Actuarially smoothed data. See "Summary of Significant Accounting and Reporting Policies" in Notes to the Consolidated Financial Statements in the 2005 Annual Report on Form 10-K.
(2) Includes discontinued operations expense. Pension benefits expense is estimated to include discontinued operations expense of \(\$ 6\) million for both 2006 and 2005.

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

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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.

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.
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|}
\hline (Dollars in millions) & \multicolumn{5}{|c|}{Increase in} & \multicolumn{4}{|r|}{Decrease in} \\
\hline Long-Term Rate of Return on Plan Assets & & 6.88\% & & 7.38\% & \(7.88 \%\) & & 8.38\% & & 8.88\% \\
\hline Change in Pension Expense & \$ & 16.0 & \$ & 7.9 & N/A & \$ & 7.9 & \$ & 15.7 \\
\hline Discount Rate & & 5.38\% & & 5.63\% & 5.88\% & & 6.13\% & & \(6.38 \%\) \\
\hline Change in Pension Expense & \$ & 14.9 & \$ & 7.2 & N/A & \$ & 6.9 & & 3. \\
\hline
\end{tabular}

Market-Related Value of
\begin{tabular}{lrlrrr} 
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 & \(\$ 6.7\) & \(\$ 12.9\)
\end{tabular}

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CONSOLIDATED BALANCE SHEET REVIEW
Total assets were \(\$ 108.9\) billion at June 30, 2006, compared with \(\$ 103.1\) billion at June 30, 2005 and \(\$ 103.6\) billion at March 31, 2006. The increase in assets from March 31, 2006 reflects increases in short-term high quality interest bearing deposits at banks as well as loans to the Company's securites servicing customers. Total shareholders' equity was \(\$ 10.1\) billion at June 30, 2006, compared with \(\$ 9.5\) billion at June 30,2005 and \(\$ 10.1\) billion at March 31, 2006. The retention of earnings in the second quarter of 2006 was offset by the repurchase of common stock.

Return on average common equity for the second quarter of 2006 was \(18.17 \%\), compared with \(17.12 \%\) in the second quarter of 2005 and \(17.31 \%\) in the first quarter of 2006 .

Return on average assets for the second quarter of 2006 was \(1.63 \%\), compared with \(1.59 \%\) in the second quarter of 2005 and \(1.61 \%\) in the first quarter of 2006 .

Investment Securities

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

Investment Securities (at Fair Value)
\begin{tabular}{|c|c|c|c|c|}
\hline (In millions) & \multicolumn{2}{|r|}{6/30/06} & \multicolumn{2}{|r|}{12/31/05} \\
\hline \multicolumn{5}{|l|}{Fixed Income:} \\
\hline Mortgage-Backed Securities & \$ & 23,397 & \$ & 22,484 \\
\hline Asset-Backed Securities & & 382 & & 305 \\
\hline Corporate Debt & & 1,287 & & 1,034 \\
\hline Short-Term Money Market Instruments & & 771 & & 975 \\
\hline U.S. Treasury Securities & & 221 & & 226 \\
\hline U.S. Government Agencies & & 646 & & 620 \\
\hline State and Political Subdivisions & & 206 & & 224 \\
\hline Emerging Market Debt (Collateralized By U.S. Treasury Zero Coupon Obligations) & & 117 & & 117 \\
\hline Other Foreign Debt & & 10 & & 363 \\
\hline Subtotal Fixed Income & & 27,037 & & 26,348 \\
\hline \multicolumn{5}{|l|}{Equity Securities:} \\
\hline Money Market Funds & & 333 & & 922 \\
\hline Other & & 30 & & 31 \\
\hline Subtotal Equity Securities & & 363 & & 953 \\
\hline Adjusted Securities & & 27,400 & & 27,301 \\
\hline Securities of Discontinued Operations (1) & & (104) & & (108) \\
\hline
\end{tabular}

\author{
Securities from Continuing Operations
}
\begin{tabular}{|c|c|c|c|}
\hline \$ & 27,296 & \$ & 27,193 \\
\hline
\end{tabular}
(1) Securities of State and Political Subdivisions.

Total investment securities were \(\$ 27.3\) billion at June 30, 2006, compared with \(\$ 25.7\) billion at June 30,2005 , and \(\$ 27.2\) billion at March 31, 2006. Average adjusted investment securities were \(\$ 27.3\) billion in the second quarter of 2006 , compared with \(\$ 24.7\) billion in the second quarter of last year and \(\$ 27.1\) billion in the first quarter of 2006 . The Company's portfolio of highly rated mortgage-backed securities, are \(89 \%\) rated AAA, \(8 \% A A\), and \(3 \% A\). In replacing securities that mature or are paid off, the Company has been adding either adjustable or short life classes of structured mortgage-backed securities, both of which have short durations. The effective duration of the Company's mortgage portfolio at June 30,2006 was approximately 2.1 years.

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\begin{abstract}
Net unrealized losses for securities available-for-sale was \(\$ 274\) million at June 30, 2006, compared with net unrealized gains of \(\$ 60\) million at June 30 , 2005, and net unrealized losses of \(\$ 195\) million at March 31, 2006. The change in the value of available-for-sale securities at June 30, 2006 from March 31 , 2006 reflects the increase in long-term interest rates over the quarter. 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 fixed rate portion 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 in value of the Company's fixed rate liabilities, even though economically these liabilities are more valuable as rates rise.
\end{abstract}

Loans
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(Dollars in billions)


Total loans were \(\$ 35.7\) billion at June 30,2006 , compared with \(\$ 32.9\) billion at December 31, 2005. The increase in total loans from December 31, 2005 primarily reflects increased lending to securities servicing customers partially offset by a decrease in margin loans reflecting the loss of a significant customer at Pershing. Average total loans were \(\$ 33.6\) billion in the second quarter of 2006 , compared with \(\$ 31.6\) billion in the second quarter
of 2005. The increase in average loans from June 30, 2005 results from increased lending to financial institutions.

The following tables provide additional details on the Company's credit exposures and outstandings for continuing operations at June 30, 2006 in comparison to December 31, 2005.

Overall Loan Portfolio
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|c|c|}
\hline & \multicolumn{6}{|c|}{June 30, 2006} & \multicolumn{6}{|c|}{December 31, 2005} \\
\hline (In billions) & \multicolumn{2}{|r|}{Loans} & \multicolumn{2}{|l|}{Unfunded Commitments} & \multicolumn{2}{|l|}{Total Exposure} & \multicolumn{2}{|r|}{Loans} & \multicolumn{2}{|l|}{Unfunded Commitments} & \multicolumn{2}{|l|}{Total Exposure} \\
\hline Financial Institutions & \$ & 15.8 & \$ & 24.6 & \$ & 40.4 & \$ & 13.0 & \$ & 22.4 & \$ & 35.4 \\
\hline Corporate & & 4.1 & & 19.8 & & 23.9 & & 3.7 & & 19.6 & & 23.3 \\
\hline & & 19.9 & & 44.4 & & 64.3 & & 16.7 & & 42.0 & & 58.7 \\
\hline Consumer \& Middle Market & & 3.8 & & 0.3 & & 4.1 & & 3.2 & & 0.3 & & 3.5 \\
\hline Leasing Financings & & 5.5 & & 0.1 & & 5.6 & & 5.5 & & 0.1 & & 5.6 \\
\hline Commercial Real Estate & & 1.4 & & 1.3 & & 2.7 & & 1.4 & & 1.2 & & 2.6 \\
\hline Margin loans & & 5.1 & & - & & 5.1 & & 6.1 & & - & & 6.1 \\
\hline Total & \$ & 35.7 & \$ & 46.1 & \$ & 81.8 & \$ & 32.9 & \$ & 43.6 & \$ & 76.5 \\
\hline
\end{tabular}

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Financial Institutions

The financial institutions portfolio exposure was \(\$ 40.4\) billion at June 30, 2006, compared to \(\$ 35.4\) billion at December 31, 2005. The increase in exposure from year-end 2005 reflects greater activity in the capital markets in the second quarter of 2006, which drove increased demands for credit from financial institutions. These exposures are of high quality with 86\% meeting the investment grade criteria of the Company's rating system. These exposures are generally short-term, with \(76 \%\) 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)


Included in the Company's corporate exposures are automotive and airline exposures. The Company continues to seek to selectively reduce automotive

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exposures given ongoing weakness in the domestic automotive industry. Total exposures reported in the Automotive Division were down \(\$ 229\) million at June 30,2006 compared with December 31, 2005. At June 30, 2006, this broadly defined industry portfolio consists of exposures of \(\$ 156\) million to Big Three automotive manufacturing, \(\$ 189\) million to finance subsidiaries, \(\$ 378\) million to highly rated asset-backed securitization vehicles, \(\$ 209\) million to suppliers, and \(\$ 140\) million of other.

The Company's exposure to the airline industry consists of a \(\$ 326\) million leasing portfolio (including a \(\$ 16\) million real estate lease exposure). The

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airline-leasing portfolio consists of \(\$ 127\) million to major U.S. carriers, \(\$ 136\) million to foreign airlines and \(\$ 63\) million to U.S. regionals.

During the second quarter of 2006, the airline industry continued to face liquidity issues driven by persistently high fuel prices and the inability to implement meaningful fare increases. The industry's considerable excess capacity and higher oil prices continue to negatively impact the valuations of aircraft, especially the less fuel-efficient models, 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.
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Counterparty Risk Ratings Profile

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The table below summarizes the risk ratings of the Company's foreign exchange and interest rate derivative counterparty credit exposure for the past year.
\begin{tabular}{|c|c|c|c|c|c|}
\hline \multirow[b]{2}{*}{Rating(1)} & \multicolumn{5}{|c|}{For the Quarter Ended} \\
\hline & 6/30/06 & 3/31/06 & 12/31/05 & 9/30/05 & 6/30/05 \\
\hline AAA to AA- & 77\% & 77\% & 74\% & 71\% & 68\% \\
\hline A+ to A- & 10 & 8 & 13 & 13 & 15 \\
\hline \(\mathrm{BBB}+\) to \(\mathrm{BBB}-\) & 6 & 9 & 9 & 13 & 14 \\
\hline Noninvestment Grade & 7 & 6 & 4 & 3 & 3 \\
\hline Total & 100\% & 100\% & 100\% & 100\% & 100\% \\
\hline
\end{tabular}
(1) Represents credit rating agency equivalent of internal credit ratings.

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Nonperforming Assets
\begin{tabular}{|c|c|c|c|c|c|c|c|}
\hline (Dollars in millions) & \multicolumn{2}{|l|}{6/30/2006} & \multicolumn{2}{|l|}{3/31/2006} & \multicolumn{2}{|l|}{\begin{tabular}{l}
Change \\
6/30/2006 vs. \\
3/31/2006
\end{tabular}} & \begin{tabular}{l}
Percent \\
Inc/ \\
(Dec)
\end{tabular} \\
\hline \multicolumn{8}{|l|}{Loans:} \\
\hline Commercial & \$ & 10 & \$ & 12 & \$ & (2) & (17) \(\%\) \\
\hline Foreign & & 10 & & 13 & & (3) & (23) \\
\hline Total Nonperforming Loans & & 20 & & 25 & & (5) & (20) \\
\hline Other Assets Owned & & 12 & & - & & 12 & - \\
\hline
\end{tabular}


The sequential quarter increase in nonperforming assets primarily reflects the buyout of debt associated with a lease on an aircraft that is being positioned for sale as part of a workout strategy.

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Activity in Nonperforming Assets
(In millions)
Balance at Beginning of Period
Additions
Charge-offs
Paydowns/Sales
Balance at End of Period
\begin{tabular}{|c|c|c|c|}
\hline \multicolumn{2}{|r|}{Quarter End} & \multicolumn{2}{|r|}{Year-to-date} \\
\hline \multicolumn{2}{|r|}{June 30, 2006} & & 2006 \\
\hline \$ & 25 & \$ & 39 \\
\hline & 12 & & 12 \\
\hline & - & & - \\
\hline & ( 5 ) & & (19) \\
\hline \$ & 32 & \$ & 32 \\
\hline
\end{tabular}

On a continuing operations basis, interest income would have been increased by \(\$ 0.3\) million and \(\$ 0.1\) million for the second quarters of 2006 and 2005 if loans on nonaccrual status at June 30,2006 and 2005 had been performing for the entire period. On a year-to-date basis, interest income would have increased by \(\$ 0.7\) million and \(\$ 1.1\) million for 2006 and 2005 had loans on nonaccrual status at June 30,2006 and 2005 been performing for the entire period.

\section*{Impaired Loans}

The table below sets forth information about the Company's impaired loans. The Company uses the discounted cash flow, collateral value, or market price methods for valuing its impaired loans:
\begin{tabular}{|c|c|c|c|c|c|c|}
\hline (In millions) & \multicolumn{2}{|r|}{\[
\begin{array}{r}
\text { June } 30, \\
2006
\end{array}
\]} & & \[
\begin{gathered}
\text { March 31, } \\
2006
\end{gathered}
\] & \multicolumn{2}{|r|}{June 30
\[
2005
\]} \\
\hline Impaired Loans with an Allowance & \$ & 12 & \$ & 17 & \$ & 20 \\
\hline Impaired Loans without an Allowance(1) & & - & & - & & 64 \\
\hline Impaired Loans on a Continuing Operations basis & & 12 & & 17 & & 84 \\
\hline Impaired Loans related to Discontinued Operations & & 27 & & 28 & & 35 \\
\hline Adjusted Total Impaired Loans & \$ & 39 & \$ & 45 & \$ & 119 \\
\hline
\end{tabular}

Continuing Operations
\begin{tabular}{|c|c|c|c|c|c|c|}
\hline Allowance for Impaired Loans(2) & \$ & 3 & \$ & 4 & \$ & 7 \\
\hline Average Balance of Impaired Loans during the Quarter & & 15 & & 17 & & 109 \\
\hline Interest Income Recognized on Impaired Loans during the Quarter & & - & & - & & 1.1 \\
\hline Adjusted & & & & & & \\
\hline Allowance for Impaired Loans(2) & \$ & 10 & \$ & 15 & \$ & 30 \\
\hline Average Balance of Impaired Loans during the Quarter & & 42 & & 43 & & 145 \\
\hline Interest Income Recognized on Impaired Loans during the Quarter & & 0.5 & & 0.4 & & 1.6 \\
\hline
\end{tabular}
(1) When the discounted cash flows, collateral value or market price equals or exceeds the carrying value of the loan, then the loan does not require an allowance under the accounting standard related to impaired loans.
(2) The allowance for impaired loans is included in the Company's allowance for credit losses.

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Allowance
\(\qquad\)


Margin Loans
\begin{tabular}{|c|c|c|c|c|c|c|}
\hline Non-Margin Loans & & 7,972 & & 7,863 & & 7,731 \\
\hline Loans Related to Discontinued Operations & & 7,972 & & 7,863 & & 7,731 \\
\hline Adjusted Total Loans & \$ & 43,622 & \$ & 40,054 & \$ & 40,681 \\
\hline Allowance for Loan Losses & \$ & 337 & \$ & 334 & \$ & 463 \\
\hline Allowance for Lending-Related Commitments & & 143 & & 140 & & 138 \\
\hline Allowance for Credit Losses on a Continuing Operations Basis & & 480 & & 474 & & 601 \\
\hline Allowance for Loan Losses & & 80 & & 85 & & 99 \\
\hline Allowance for Lending-Related Commitments & & 7 & & 7 & & 10 \\
\hline Allowance for Credit Losses Relate to Discontinued Operations & & 87 & & 92 & & 109 \\
\hline Adjusted Total Allowance for & & & & & & \\
\hline Credit Losses & \$ & 567 & \$ & 566 & \$ & 710 \\
\hline
\end{tabular}

Continuing Operations
Allowance for Loan Losses
As a Percent of Total Loans \(0.95 \% \quad 1.04 \%\)
Allowance for Loan Losses
As a Percent of Non-Margin Loans 1.10 1.24 1.72

Total Allowance for Credit Losses
As a Percent of Total Loans
1.35

Total Allowance for Credit Losses
As a Percent of Non-Margin Loans
1.57
1.82
1.76
2.23

\section*{Adjusted}

Allowance for Loan Losses
As a Percent of Total Loans
\(0.96 \%\)
\(1.05 \%\)
\(1.38 \%\)
Allowance for Loan Losses As a Percent of Non-Margin Loans
1.08

Total Allowance for Credit Losses As a Percent of Total Loans
1.30

Total Allowance for Credit Losses As a Percent of Non-Margin Loans
1.47
\begin{tabular}{ll}
1.21 & 1.62 \\
1.41 & 1.75 \\
1.63 & 2.05
\end{tabular}

On a continuing operations basis, the total allowance for credit losses was \(\$ 480\) million, or \(1.35 \%\) of total loans at June 30,2006 , compared with \(\$ 601\) million, or \(1.82 \%\) of total loans at June 30,2005 and \(\$ 474\) million, or \(1.47 \%\) of total loans at March 31, 2006. The decline from the second quarter of 2005 reflects the charge-off of aircraft leases in the fourth quarter of 2005.

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The Company has \(\$ 5.1\) billion of secured margin loans on its balance sheet at June 30,2006 . 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. As a result, the Company believes the ratio of total allowance for
credit losses to non-margin loans is a more appropriate metric to measure the adequacy of the reserve.

On a continuing operations basis, the ratio of the total allowance for credit losses to non-margin loans was \(1.57 \%\) at June 30,2006 , compared with 2.23\% at June 30,2005 and \(1.76 \%\) at March 31, 2006 , reflecting improvement in the credit quality since the second quarter of 2005 . The ratio of the allowance for loan losses to nonperforming assets was 1,053\% at June 30, 2006, compared with 532\% at June 30, 2005, and 1,336\% at March 31, 2006.

The allowance for loan losses and the allowance for lending-related commitments consists 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.

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 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, 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. The Company also applies this technique to its leasing and consumer portfolios. 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;

\begin{tabular}{|c|c|c|}
\hline & \[
\begin{array}{r}
\text { June } 30, \\
2006
\end{array}
\] & \[
\begin{array}{r}
\text { December 31, } \\
2005
\end{array}
\] \\
\hline \multicolumn{3}{|l|}{Domestic} \\
\hline Real Estate & 1\% & 1\% \\
\hline Commercial & 69 & 72 \\
\hline Consumer & 5 & 4 \\
\hline Foreign & 2 & 3 \\
\hline Unallocated & 23 & 20 \\
\hline & 100\% & 100\% \\
\hline
\end{tabular}

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.

\section*{Deposits}
_-_-_-_-_

\begin{abstract}
On a continuing operations basis, total deposits were \(\$ 56.7\) billion at June 30, 2006, compared with \(\$ 48.7\) billion at June 30, 2005, and \(\$ 50.8\) billion at March 31, 2006. The increase from June 30, 2005 was primarily due to increased market activity levels, which resulted in higher levels of customer deposits, and global payments services customers' increased use of compensating balances. Sequential quarter growth was primarily due to higher foreign deposits, principally in the Company's corporate trust and custody business. Noninterest-bearing deposits were \(\$ 15.9\) billion at June 30,2006 , compared with \(\$ 12.7\) billion at December 31, 2005. Interest-bearing deposits were \(\$ 40.8\) billion at June 30, 2006, compared with \(\$ 37.1\) billion at December 31, 2005.
\end{abstract}

\section*{48}

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 from the Company's securities servicing businesses and private banking and asset management 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 at The Bank of New York Company, Inc. parent company ("Parent").

On a continuing operations basis, non-core sources of funds such as money market rate accounts, certificates of deposits greater than \(\$ 100,000\), federal funds purchased, and other borrowings were \(\$ 14.1\) billion and \(\$ 12.4\) billion on an average basis for the first six months of 2006 and 2005 . Average foreign deposits, primarily from the Company's European based securities servicing business, were \(\$ 31.4\) billion and \(\$ 25.9\) billion for the first six months of 2006 and 2005. The increase in foreign deposits reflects greater liquidity from the Company's corporate trust and custody business. Domestic savings and other time deposits were \(\$ 1.3\) billion on an average basis for the first six months of 2006 compared to \(\$ 0.8\) billion in 2005. On a year-to-date basis, average payables to customers and broker-dealers decreased to \$5.1 billion from \$6.2 billion in 2005. The decline in payables to customers and broker-dealers reflects the loss of a significant customer at Pershing. Long-term debt averaged \(\$ 8.1\) billion and \(\$ 7.0\) billion for the first six months of 2006 and 2005, respectively. The increase in long-term debt reflects the movement of Pershing from a subsidiary of the Bank to a subsidiary of the Parent and the building of liquidity to pay debt maturing in 2007 . A significant reduction in the Company's securities servicing businesses would reduce its access to foreign deposits.

The Company's pending transaction with JPMorgan Chase will slightly alter the composition of the balance sheet. Approximately \(\$ 15\) billion of \(U . S\). dollar retail deposits will be replaced with approximately \(\$ 13\) billion of institutional corporate trust deposits. On the asset side of the balance sheet, approximately \(\$ 8\) billion of retail and middle market loans sold to JPMorgan Chase will be replaced with liquid assets and securities. Goodwill and intangibles are expected to increase approximately \(\$ 2.1\) billion. As a result of the transaction, the Company expects its balance sheet footings to decline slightly.

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.

At June 30, 2006, the Bank can pay dividends of approximately \(\$ 467\) million to the Parent without the need for regulatory waiver. This dividend capacity would 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 \(\$ 247\) million. These assets could be liquidated and the proceeds delivered by dividend or loan to the Parent.

For the quarter ended June 30, 2006 , the Parent's quarterly average commercial paper borrowings were \(\$ 510\) million compared with \(\$ 222\) million in 2005. At June 30, 2006, the Parent had cash of \(\$ 515\) million compared with \(\$ 858\) million at June 30,2005 and \(\$ 685\) million at March 31, 2006. Net of commercial paper outstanding, the Parent's cash position at June 30,2006 was down \(\$ 14\) million compared with June 30, 2005.

The Parent has a back-up line of credit of \(\$ 275\) million with 14 financial institutions. This line of credit matures in October 2006 . There were no borrowings under the line of credit at June 30, 2006 and June 30, 2005.

The Parent also has the ability to access the capital markets. On June 5, 2006, the Company filed a new S-3 automatic shelf registration statement with the SEC covering its existing debt, preferred stock, trust preferred securities, and common stock.

Access to the capital markets is partially dependent on the Company's credit ratings, which as of June 30, 2006 were as follows:
\begin{tabular}{|c|c|c|c|c|c|}
\hline & Parent Commercial Paper & Parent Subordinated Long-Term Debt & Parent Senior Long-Term Debt & \begin{tabular}{l}
The Bank of \\
New York Long-Term Deposits
\end{tabular} & Outlook \\
\hline Standard \& Poor's & A-1 & A & A+ & AA- & Stable \\
\hline Moody's & P-1 & A1 & Aa3 & Aa 2 & Stable \\
\hline Fitch & F1+ & A+ & AA- & AA & Stable \\
\hline Dominion Bond Rating Service & R-1 (mid & dle) A(high) & AA (low) & AA & Stable \\
\hline
\end{tabular}

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

The Parent does not have any long-term debt that becomes due in 2006 subsequent to June 30, 2006. The Parent has \(\$ 700 \mathrm{million}\) of long-term debt that is due in 2007. In addition, the Parent periodically has the option to call \(\$ 227\) million of subordinated debt in the remainder of 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 trust preferred 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 trust preferred securities, it expects to replace them with new trust preferred securities or senior or subordinated debt.

Double leverage is the ratio of investment in subsidiaries divided by the Company's consolidated equity plus trust preferred securities. The Company's double leverage ratio at June 30, 2006 and 2005 was \(105.7 \%\) and \(102.3 \%\), 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 2007. There were no borrowings against this line of credit during the second quarter of 2006. Pershing LLC has three separate uncommitted lines of credit amounting to \(\$ 1\) billion in aggregate. Average daily borrowing under these lines was \$3 million, in aggregate, during the second quarter of 2006.

Pershing Limited, an indirect subsidiary of the Company, has committed and uncommitted lines in place for liquidity purposes. The committed lines of credit of \(\$ 275\) million with four financial institutions mature in March 2007 . Average daily borrowings under these lines were \(\$ 75\) million, in aggregate, during the second quarter of 2006. Pershing Limited has three separate uncommitted lines of credit amounting to \(\$ 300\) million in aggregate. Average

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daily borrowing under these lines was \(\$ 118\) million, in aggregate, during the second quarter of 2006 .

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

Cash provided by operating activities was \(\$ 2.6\) billion for the six months of 2006, compared with \(\$ 0.7\) billion used by operating activities through June 30, 2005. The source of funds in 2006 was principally due to the changes in trading activities, changes in accruals and other, and net income. The use of funds from operations in 2005 was principally the result of changes in trading activities partially offset by net income.

In the first six months of 2006 , cash used for investing activities was \(\$ 6.3\) billion as compared to cash used for investing activities in the first six months of 2005 of \(\$ 8.3\) billion. In the first six months of 2006 , purchases of securities available-for-sale, principal disbursed on loans to customers, and change in interest-bearing deposits were a significant use of funds. Purchases of securities available-for-sale and principal disbursed on loans to customers were a significant use of funds in 2005.

Through June 30, 2006, cash provided by financing activities was \$3.8 billion, compared to \(\$ 7.8\) billion in the first six months of 2005 . Primary sources of funds in 2006 include deposits and long-term debt. Sources of funds in 2005 include deposits, other borrowed funds, and proceeds from the issuance of long-term debt.

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\section*{CAPITAL RESOURCES}

Shareholders' equity was \(\$ 10,056\) million at June 30,2006 , compared with \(\$ 10,101\) million at March 31, 2006, and \(\$ 9,876\) million at December 31, 2005. During the second quarter of 2006 , the Company retained \(\$ 289\) million of earnings. The Company repurchased 10.3 million shares during the quarter. The Company expects to repurchase 14 million shares upon the closing of the BNY CovergEx transaction. In July 2006 , the Company increased the quarterly common stock dividend to 22 cents per share, an increase of \(5 \%\) over the first quarter of 2006. Accumulated other comprehensive income declined \(\$ 97\) million from December 31, 2005 primarily reflecting higher unrealized mark-to-market losses in the securities available-for-sale portfolio.

In the second quarter of 2006 , the Company issued \(\$ 102\) million of callable medium-term subordinated notes bearing interest at rates from 6.05\% to 6.40\%. The notes are due in 2021 and 2031 and are callable by the Company after three to five years. The notes qualify as Tier 2 capital.

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, among other things, 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 June 30,2006 and 2005, 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:
\begin{tabular}{|c|c|c|c|c|c|c|c|}
\hline \multirow[t]{2}{*}{} & \multicolumn{2}{|l|}{June 30, 2006} & \multicolumn{2}{|l|}{June 30, 2005} & \multirow[b]{2}{*}{\begin{tabular}{l}
Company \\
Targets
\end{tabular}} & \multirow[t]{2}{*}{\begin{tabular}{l}
Well \\
Capitalized Guidelines
\end{tabular}} & \multirow[t]{2}{*}{\begin{tabular}{l}
Adequately \\
Capitalized Guidelines
\end{tabular}} \\
\hline & Company & Bank & Company & Bank & & & \\
\hline Tier 1 (1) & \(7.96 \%\) & 8. \(60 \%\) & 8.07\% & 8. \(48 \%\) & 7.75\% & 6\% & 4\% \\
\hline Total Capital (2) & 12.06 & 11.39 & 12.49 & 11.74 & 11.75 & 10 & 8 \\
\hline Leverage & 6.22 & 6.82 & 6.55 & 6.92 & & 5 & 3-5 \\
\hline Tangible Common Equity ("TCE") & 5.07 & 6.11 & 5.26 & 6.19 & 5.00-5.25 & N. A. & N. A. \\
\hline
\end{tabular}

The Company's Tier 1 capital and Total Capital ratios were \(7.96 \%\) and \(12.06 \%\) at June 30, 2006, compared with \(8.07 \%\) and \(12.49 \%\) at June 30 , 2005, and \(8.28 \%\) and \(12.44 \%\) at March 31, 2006 . The leverage ratio was \(6.22 \%\) at June 30 , 2006, compared with 6.55\% at June 30, 2005, and 6.51\% at March 31, 2006. The Company's tangible common equity as a percentage of total assets was \(5.07 \%\) at June 30, 2006, compared with 5.26\% at June 30, 2005, and 5.42\% at March 31, 2006. The Company's pending transaction with JPMorgan Chase is expected to reduce its \(T C E\) ratio to approximately \(4.67 \%\) primarily due to the intangibles associated with the transaction. The tangible common equity ratio varies depending on the size of the balance sheet at quarter-end and the impact of interest rates on unrealized gains and losses among other things. The balance sheet size fluctuates from quarter to quarter based on levels of market activity. In general, when servicing clients are more actively trading securities, deposit balances and the balance sheet as a whole, are higher to finance these activities.

A billion dollar change in assets changes the TCE ratio by 5 basis points while a \(\$ 100\) million change in common equity changes the TCE ratio by 10 basis points.

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On April 4, 2006, pursuant to a \(10 b 5-1\) plan, the Company repurchased 10 million shares of its common stock at an initial price of \(\$ 35.85\) from a brokerdealer counterparty who borrowed the shares, as part of an accelerated share repurchase program. The repurchase was triggered by the non-issuance of a specified FSP for lease accounting for calendar year 2006 or prior periods. See "Accounting Changes and New Accounting Pronouncements" in the Notes to the Consolidated Financial Statements. The initial price is subject to a purchase price adjustment based on the price the counterparty pays for the Company's shares it purchases over time in the open market to cover the borrowed shares.

On March 1, 2005, the Board of Governors of the Federal Reserve System (the "FRB") adopted a final rule that allows the continued limited inclusion of trust preferred securities in the Tier 1 capital of bank holding companies (BHCs). Under the final rule, the Company will be subject to a 15 percent limit in the amount of trust preferred securities that can be included in Tier 1 capital, net of goodwill, less any related deferred tax liability. Amounts in excess of these limits will continue to be included in Tier 2 capital. The final rule provides a five-year transition period, ending March 31, 2009, for

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application of quantitative limits. Under the transition rules, the Company expects all its trust preferred securities to continue to qualify as Tier 1 capital. Both the Company and the Bank are expected to remain "well capitalized" under the final rule. At the end of the transition period, the Company expects all its current trust preferred securities will continue to qualify as Tier 1 capital.

The following table presents the components of the Company's risk-based capital at June 30, 2006 and 2005:
\begin{tabular}{|c|c|c|}
\hline & \multicolumn{2}{|c|}{June 30,} \\
\hline (In millions) & 2006 & 2005 \\
\hline Shareholders' Equity & \$10,056 & \$ 9,471 \\
\hline Securities Valuation Allowance & 155 & (49) \\
\hline Trust Preferred Securities & 1,150 & 1,150 \\
\hline Adjustments: Intangibles & \((4,775)\) & \((4,273)\) \\
\hline Merchant Banking Investments & (19) & ( 6 \\
\hline Tier 1 Capital & 6,567 & 6,293 \\
\hline Qualifying Subordinated Debt & 2,821 & 2,743 \\
\hline Qualifying Allowance for Loan Losses & 569 & 709 \\
\hline Tier 2 Capital & 3,390 & 3,452 \\
\hline Total Risk-Based Capital & \$ 9,957 & \$ 9,745 \\
\hline Risk-Adjusted Assets & \$82,544 & \$78,003 \\
\hline
\end{tabular}

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TRADING ACTIVITIES

The fair value and notional amounts of the Company's financial instruments held for trading purposes at June 30, 2006 and 2005 are as follows:
\begin{tabular}{|c|c|c|c|c|c|c|c|}
\hline \multirow[b]{2}{*}{(In millions)} & \multicolumn{4}{|c|}{June 30, 2006} & \multicolumn{3}{|l|}{2006 Average} \\
\hline & Notional & \multicolumn{3}{|c|}{Fair Value} & \multicolumn{3}{|c|}{Fair Value} \\
\hline Trading Account & Amount & Assets & L & ities & Assets & & ities \\
\hline \multicolumn{8}{|l|}{Interest Rate Contracts:} \\
\hline \multicolumn{8}{|l|}{Futures and Forward} \\
\hline Contracts & \$ 93,353 & \$ 57 & \$ & - & \$ 44 & \$ & - \\
\hline Swaps & 283,612 & 1,709 & & 1,208 & 2,045 & & 1,488 \\
\hline Written Options & 214,899 & - & & 1,011 & - & & 1,016 \\
\hline Purchased Options & 185,068 & 203 & & - & 199 & & - \\
\hline \multicolumn{8}{|l|}{Foreign Exchange Contracts:} \\
\hline Swaps & 2,640 & - & & - & - & & - \\
\hline Written Options & 10,137 & - & & 84 & - & & 77 \\
\hline Purchased Options & 12,801 & 237 & & - & 198 & & - \\
\hline Commitments to Purchase and Sell Foreign Exchange & 90,948 & 202 & & 303 & 209 & & 334 \\
\hline Debt Securities & - & 3,638 & & 295 & 4,452 & & 233 \\
\hline Credit Derivatives & 1,394 & 3 & & 8 & 2 & & 8 \\
\hline Equities & 11,459 & 16 & & 29 & 81 & & 62 \\
\hline Total Trading Account & & \$6,065 & \$ & 2,938 & \$7,230 & \$ & 3,218 \\
\hline
\end{tabular}
\begin{tabular}{|c|c|c|c|c|c|c|c|}
\hline (In millions) & Notional & \multicolumn{3}{|c|}{Fair Value} & \multicolumn{3}{|c|}{Fair Value} \\
\hline Trading Account & Amount & \multicolumn{3}{|l|}{Assets Liabilities} & Assets & \multicolumn{2}{|l|}{Liabilities} \\
\hline \multicolumn{8}{|l|}{Interest Rate Contracts:} \\
\hline \multicolumn{8}{|l|}{Futures and Forward} \\
\hline Contracts & \$ 32,949 & \$ - & \$ & - & \$ - & \$ & 5 \\
\hline Swaps & 249,997 & 1,809 & & 923 & 1,677 & & 831 \\
\hline Written Options & 182,793 & - & & 1,425 & - & & 1,337 \\
\hline Purchased Options & 143,793 & 274 & & - & 229 & & - \\
\hline \multicolumn{8}{|l|}{Foreign Exchange Contracts:} \\
\hline Swaps & 3,520 & - & & - & - & & - \\
\hline Written Options & 5,732 & - & & 18 & - & & 24 \\
\hline Purchased Options & 7,214 & 32 & & - & 70 & & - \\
\hline Commitments to Purchase and Sell Foreign Exchange & 75,276 & 582 & & 545 & 515 & & 546 \\
\hline Debt Securities & - & 3,824 & & 83 & 3,372 & & 245 \\
\hline Credit Derivatives & 1,708 & 1 & & 4 & 2 & & 7 \\
\hline Equities & 2,023 & 110 & & 90 & 126 & & 116 \\
\hline Total Trading Account & & \$6,632 & \$ & 3,088 & \$5,991 & \$ & 3,111 \\
\hline
\end{tabular}

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 nonlinear characteristics of options. The VAR model is used to calculate economic capital, which is allocated to the business units for computing risk-adjusted performance.

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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 periods indicated.
(Dollars in millions)

Interest rate
Foreign Exchange
Equity
Credit Derivatives
Diversification
Overall Portfolio

2nd Quarter 2006
\begin{tabular}{|c|c|c|}
\hline Average & Minimum & Maximum \\
\hline
\end{tabular}

Year-to-date 2006


Year-to-date 2005
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|c|}
\hline \multicolumn{2}{|l|}{Average} & \multicolumn{2}{|l|}{Minimum} & \multicolumn{2}{|l|}{Maximum} & \multicolumn{2}{|l|}{Average} & \multicolumn{2}{|l|}{Minimum} & \multicolumn{2}{|l|}{Maximum} \\
\hline \$ & 2.7 & \$ & 1.9 & \$ & 4.6 & \$ & 2.8 & \$ & 1.9 & \$ & 4.6 \\
\hline & 2.8 & & 1.6 & & 4.1 & & 1.9 & & 0.4 & & 4.1 \\
\hline & 0.6 & & 0.3 & & 1.0 & & 0.7 & & 0.3 & & 1.1 \\
\hline & 1.8 & & 1.5 & & 2.1 & & 1.7 & & 1.5 & & 2.1 \\
\hline & (1.4) & & NM & & NM & & (1.4) & & NM & & NM \\
\hline & 6.5 & & 3.8 & & 9.1 & & 5.7 & & 3.7 & & 9.1 \\
\hline
\end{tabular}
\$
\begin{tabular}{crrr}
3.3 & \(\$\) & 2.1 & \(\$\) \\
1.1 & & 0.6 & \\
1.0 & & 0.5 & \\
1.3 & & 0.9 & \\
\((1.7)\) & & NM & \\
5.0 & & 3.9 & \\
& & & \\
& & & NM \\
& &
\end{tabular}
(Dollars in millions)

Interest rate
Foreign Exchange
Equity
Credit Derivatives
Diversification
Overall Portfolio

\section*{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, and 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:
(Dollars in millions)
\begin{tabular}{|c|c|c|c|c|c|c|}
\hline & \[
\begin{gathered}
\text { June } 30, \\
\$
\end{gathered}
\] & \[
\begin{array}{r}
2006 \\
\%
\end{array}
\] & & \[
\begin{gathered}
\text { March } \\
\$
\end{gathered}
\] & \[
31,
\] & \[
\begin{gathered}
2006 \\
\%
\end{gathered}
\] \\
\hline \$ & (62) & (3.0) \% & \$ & (64) & & (3.1) \% \\
\hline & (28) & (1.3) & & (28) & & (1.3) \\
\hline & 15 & 0.7 & & (1) & & - \\
\hline & 9 & 0.5 & & (15) & & (0.7) \\
\hline
\end{tabular}

The base case scenario Fed Funds rate in the June 30, 2006 analysis was \(5.25 \%\) versus \(4.75 \%\) for the March 31, 2006 analysis. The 100 basis point ramp scenarios assumes short-term rates change 25 basis points in each of the next four quarters, while the 200 basis point ramp scenarios assumes a 50 basis point per quarter change. The +100 basis point June 30,2006 scenario assumes a flattening of the yield curve with 10 -year rates rising 80 basis points. The +200 basis point June 30,2006 scenario assumes a flattening of the yield curve with 10 -year rates rising 160 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. To the extent that

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actual behavior is different from that assumed in the models, there could be a change in interest rate sensitivity. The Company's pending transaction with JPMorgan Chase will initially result in a more liability-sensitive balance because corporate trust liabilities reprice more quickly than retail deposits. The Company is in the process of evaluating various alternatives to readjust its interest rate sensitivity.

56

STATISTICAL INFORMATION

Operating Leverage
\(\qquad\)

Operating leverage is measured by comparing the rate of increase in revenue to the rate of increase in expenses. The chart below shows the computation of operating leverage. The operating column for 2006 excludes onetime costs associated with SFAS \(123(R)\) and certain costs resulting from the application of discontinued operations accounting. The Company believes excluding these costs provides the reader with supplemental information with which to assess the Company's future performance.
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|}
\hline \multicolumn{10}{|c|}{Continuing Operations} \\
\hline (Dollars in millions) & \[
\text { S) } 2006
\] & \[
\begin{aligned}
& \text { Operatin } \\
& 2 Q 2006
\end{aligned}
\] & & 2Q 2005 & \% Change & \begin{tabular}{l}
Operating \\
\% Change(2)
\end{tabular} & 2Q2006 & \[
\begin{aligned}
& \text { Operating } \\
& 2 \text { Q2006(3) }
\end{aligned}
\] & 2Q \\
\hline Noninterest Income & \$ 1,366 & \$ 1,366 & \$ & 1,194 & \(14.4 \%\) & 14.4\% & \$ 1,426 & \$ 1,426 & \$ \\
\hline Net Interest Income & 358 & 358 & & 329 & 8.8 & 8.8 & 512 & 512 & \\
\hline Total Revenue & 1,724 & 1,724 & & 1,523 & 13.2 & 13.2 & 1,938 & 1,938 & \\
\hline Total Expense & 1,134 & 1,122 & & 1,021 & 11.1 & 9.9 & 1,248 & 1,231 & \\
\hline Operating Leverage & & & & & \(2.1 \%\) & 3.3\% & & & \\
\hline
\end{tabular}

Continuing Operations
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|c|c|c|c|}
\hline \multicolumn{3}{|l|}{(Dollars in millions)} & \multicolumn{6}{|l|}{Operating} & \multicolumn{3}{|l|}{Operating} & \multicolumn{3}{|l|}{Operating} \\
\hline & 22 & 2006 & & 2006 & & Q 2006 & \% & ange & \% Change (2) & & Q2006 & & 2006 & 12 \\
\hline Noninterest Income & \$ & 1,366 & \$ & 1,366 & \$ & 1,261 & & 8.3\% & 8.3\% & \$ & 1,426 & \$ & 1,426 & \$ \\
\hline Net Interest Income & & 358 & & 358 & & 339 & & 5.6 & 5.6 & & 512 & & 512 & \\
\hline Total Revenue & & 1,724 & & 1,724 & & 1,600 & & 7.8 & 7.8 & & 1,938 & & 1,938 & \\
\hline
\end{tabular}

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\begin{tabular}{|c|c|c|c|c|c|c|c|c|}
\hline Total Expense & 1,134 & 1,122 & 1,065 & 6.5 & 5.4 & 1,248 & 1,231 & \\
\hline \multirow[t]{2}{*}{Operating Leverage} & & & & 1.3\% & 2.4\% & & & \\
\hline & & \multicolumn{3}{|r|}{Continuing Operations} & & & & \\
\hline \multirow[t]{2}{*}{(Dollars in millions)} & & Operating & \multirow[b]{2}{*}{YTD2005} & \multirow[b]{2}{*}{\% Change} & \multirow[t]{2}{*}{Operating
\% Change (2)} & \multirow[b]{2}{*}{YTD2006} & \multirow[t]{2}{*}{Operating
YTD2006(3)} & \\
\hline & YTD2006 & YTD2006(2) & & & & & & Y \\
\hline Noninterest Income & \$ 2,627 & \$ 2,627 & \$ 2,310 & 13.7\% & 13.7\% & \$ 2,758 & \$ 2,758 & \$ \\
\hline Net Interest Income & 697 & 697 & 650 & 7.2 & 7.2 & 1,000 & 1,000 & \\
\hline Total Revenue & 3,324 & 3,324 & 2,960 & 12.3 & 12.3 & 3,758 & 3,758 & \\
\hline Total Expense & 2,199 & 2,187 & 1,992 & 10.4 & 9.8 & 2,426 & 2,409 & \\
\hline Operating Leverage & & & & 1.9\% & 2.5\% & & & \\
\hline
\end{tabular}
(1) Adjusted combines continuing and discontinued operations.
(2) Operating excludes the \(\$ 12\) million impact related to SFAS \(123(\mathrm{R})\).
(3) Operating excludes the \(\$ 12\) million impact related to SFAS \(123(\mathrm{R})\) and charges and accounting changes resulting from the JPMorgan Chase transaction.

The Company's record operating results in the second quarter of 2006 reflect net income of \(\$ 448\) million. The Company reported net income of \(\$ 773\) million in the third quarter of 1999. However, after excluding the \(\$ 573\) million gain on the sale of BNY Financial Corporation, operating net income in the third quarter of 1999 was \(\$ 200\) million.

\section*{57}

Average Balances and Rates on a Taxable Equivalent Basis

THE BANK OF NEW YORK COMPANY, INC. Average Balances and Rates on a Taxable Equivalent Basi (Dollars in millions)
\begin{tabular}{|c|c|c|c|c|}
\hline \multicolumn{3}{|l|}{For the three months ended June 30, 2006} & \multicolumn{2}{|l|}{For the three months ended June 30, 2005} \\
\hline Average & & Average & Average & \\
\hline Balance & Interest & Rate & Balance & Interest \\
\hline
\end{tabular}

ASSETS
------

Interest-Bearing
Deposits in Banks
(primarily foreign)
Federal Funds Sold and Securities
Purchased Under Resale Agreements
Margin Loans
Loans
Domestic Offices
Foreign Offices

Non-Margin Loans

Securities
U.S. Government Obligations
U.S. Government Agency Obligations

Obligations of States and
Political Subdivisions
Other Securities
Trading Securities

Total Securities

Total Interest-Earning Assets
Allowance for Credit Losses
Cash and Due from Banks
Other Assets
Assets of Discontinued Operations Held for Sale

TOTAL ASSETS

LIABILITIES AND SHAREHOLDERS' EQUITY
Interest-Bearing Deposits
Money Market Rate Accoun
Savings
Certificates of Deposit
\$lo0,000 \& Over
Other Time Deposits
Foreign Offices
Total Interest-Bearing
Federal Funds Purchased a
Securities Sold Under Rep
Agreements
Other Borrowed Funds
Payables to Customers and
Long-Term Debt
Total Interest-Bearing
Noninterest-Bearing Depositin
Other Liabilities
Common Shareholders' Equit
Liabilities of Discontinuec
Held for Sale
TOTAL LIABILITIES AND
SHAREHOLDERS' EQUITY

Money Market Rate Accounts
Savings
Certificates of Deposit
\(\$ 100,000\) \& Over
Time Deposits

Total Interest-Bearing Deposits
Federal Funds Purchased and
Securities Sold Under Repurchase

Other Borrowed Funds
Payables to Customers and Broker-Dealers
Long-Term Debt
Total Interest-Bearing Liabilities

Noninterest-Bearing Deposits
Other Liabilities
Common Shareholders' Equity Held for Sale

ILABILITIES AND SHAREHOLDERS' EQUITY
\begin{tabular}{|c|c|}
\hline \multicolumn{2}{|l|}{\$ 12,432} \\
\hline & 1,565 \\
\hline & 5,506 \\
\hline & 16,786 \\
\hline & 11,317 \\
\hline & 28,103 \\
\hline & 216 \\
\hline & 4,009 \\
\hline & 109 \\
\hline & 18,848 \\
\hline & 4,469 \\
\hline & 27,651 \\
\hline & 75,257 \\
\hline & (344) \\
\hline & 3,089 \\
\hline & 18,391 \\
\hline & 13,993 \\
\hline \$ & 110,386 \\
\hline
\end{tabular}
\(\$\)
120
15
85
193
157
-------
350
\(3.88 \%\)
\$ 9,182
\$ 67
\(3.98 \quad 2.789 \quad 20\)

4.
5
4.9
4.


2

24


91

\begin{tabular}{|c|c|c|}
\hline 8.13 & 148 & 3 \\
\hline 5.21 & 15,499 & 166 \\
\hline 4.61 & 3,416 & 39 \\
\hline 5.03 & 23,149 & 248 \\
\hline 4.88 & 66,735 & 640 \\
\hline
\end{tabular}
(463)

2,282
16,445
5.47
15,462
--------1
, 461
\(\$ 809\)
=========
\(=\)
169

89
3

39

248

640

Net Interest Earnings
and Interest Rate Spread

Net Yield on Interest-Earning Assets

1.5

58

ASSETS
Interest-Bearing Deposits in Banks (primarily foreign)
Federal Funds Sold and Securities Purchased Under Resale Agreements
Margin Loans
Loans
Domestic Offices
Foreign Offices

Non-Margin Loans

Securities
U.S. Government Obligations
U.S. Government Agency Obligations

Obligations of States and
Political Subdivisions
Other Securities
Trading Securities

Total Securities

Total Interest-Earning Assets

Allowance for Credit Losses
Cash and Due from Banks
Other Assets
Assets of Discontinued Operations Held for Sale

TOTAL ASSETS
\begin{tabular}{|c|c|c|c|c|c|c|}
\hline \$ 11,036 & \$ & 206 & 3.76\% & \$ 9,502 & \$ & 138 \\
\hline 1,625 & & 30 & 3.81 & 2,619 & & 33 \\
\hline 5,580 & & 162 & 5.87 & 6,374 & & 117 \\
\hline 15,983 & & 360 & 4.51 & 14,933 & & 275 \\
\hline 11,142 & & 300 & 5.44 & 10,221 & & 201 \\
\hline 27,125 & & 660 & 4.89 & 25,154 & & 476 \\
\hline 220 & & 5 & 4.23 & 320 & & 5 \\
\hline 3,981 & & 90 & 4.53 & 3,554 & & 69 \\
\hline 113 & & 5 & 8.09 & 153 & & 6 \\
\hline 18,963 & & 477 & 5.03 & 15,009 & & 310 \\
\hline 4,591 & & 102 & 4.51 & 2,943 & & 61 \\
\hline 27,868 & & 679 & 4.88 & 21,979 & & 451 \\
\hline 73,234 & & 1,737 & 4.77 & 65,628 & & 1,215 \\
\hline (339) & & & & (474) & & \\
\hline 3,676 & & & & 2,918 & & \\
\hline 17,553 & & & & 16,281 & & \\
\hline 14,147 & & 376 & 5.36 & 15,503 & & 327 \\
\hline \$108,271 & \$ & 2,113 & & \$ 99,856 & \$ & 1,542 \\
\hline
\end{tabular}

LIABILITIES AND SHAREHOLDERS' EQUITY

Interest-Bearing Deposits

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ASSETS
Interest-Bearing Deposits in Banks (primarily foreign)
Federal Funds Sold and Securities
Purchased Under Resale Agreements
\begin{tabular}{rrrrrr}
\(\$ 12,432\) & \(\$\) & 120 & \(3.88 \%\) & \(\$ 9,182\) & \(\$\) \\
2,774 & 30 & 4.38 & 5,160 & 67 \\
5,506 & 85 & 6.20 & 6,341 & 66 \\
24,745 & 331 & 5.36 & 22,719 & 249
\end{tabular}

(584)

2,898
16,469
\$100,461
========


THE BANK OF NEW YORK COMPANY, INC.
Adjusted (1) Average Balances and Rates on a Taxable Equivalent Basis - Supplemental Data (Dollars in millions)

\section*{ASSETS}

Interest-Bearing
Deposits in Banks
(primarily foreign)
Federal Funds Sold and Securities
Purchased Under Resale Agreements
\$ 11,036
\(\$\)

206
3.76 \$
\(\$ 9,5\)
For the six months ended June 30, 2005
\begin{tabular}{|c|c|c|}
\hline Average & & Average \\
\hline Balance & Interest & Rate \\
\hline
\end{tabular}
\begin{tabular}{|c|c|}
\hline Average & \\
\hline Balance & Interest \\
\hline
\end{tabular}

Margin Loans
Loans
Domestic Offices
Foreign Offices

Non-Margin Loans

Securities
U.S. Government Obligations
U.S. Government Agency Obligations

Obligations of States and
Political Subdivisions
Other Securities
Trading Securities

Total Securities

Total Interest-Earning Assets

Allowance for Credit Losses
Cash and Due from Banks
Other Assets

TOTAL ASSETS

LIABILITIES AND SHAREHOLDERS' EQUITY
Interest-Bearing Deposits
Money Market Rate Accounts
Savings
Certificates of Deposit \(\$ 100,000\) \& Over
Other Time Deposits
Foreign Offices
Total Interest-Bearing Deposits
Federal Funds Purchased and
Securities Sold Under Repurchase
Agreements
Other Borrowed Funds
Payables to Customers and Broker-Dealers
\begin{tabular}{rrlrrr}
\(\$ 5,901\) & \(\$\) & 67 & \(2.28 \%\) & \(\$ 6,984\) & \(\$\) \\
7,993 & 63 & 1.60 & 8,920 & 47 \\
& & & & 45 \\
4,188 & 100 & 4.81 & 2,973 & 42 \\
1,542 & 29 & 3.78 & 896 & 9 \\
31,388 & 460 & 2.96 & 25,900 & 261 \\
------ & 719 & 2.84 & 45,673 & 404 \\
51,012 & & & & \\
& & & & \\
2,432 & 54 & 4.45 & 1,270 & 14 \\
2,153 & 42 & 3.91 & 1,890 & 20 \\
5,132 & 82 & 3.22 & 6,184 & 53
\end{tabular}

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\begin{tabular}{lrrr} 
Salaries and Employee Benefits & 656 & 67 & 723 \\
Net Occupancy & 68 & 18 & 86 \\
Furniture and Equipment & 48 & 2 & 50 \\
Clearing & 53 & - & 53 \\
Sub-custodian Expenses & 36 & - & 36 \\
Software & 53 & - & 53 \\
Communications & 22 & 1 & 23 \\
Amortization of Intangibles & 15 & - & 15 \\
Other & 183 & 26 & 209 \\
\multicolumn{1}{c}{ Total Noninterest Expense } & ----- & ----- & ----- \\
& 1,134 & 114 & 1,248 \\
Income Before Income Taxes & ----- & ----- & ----- \\
Income Taxes & 591 & 99 & 690 \\
& 200 & 42 & 242 \\
Net Income & ----- & ----- & ---- \\
---------- & \(\$ 391\) & 57 & \(\$ 48\) \\
& \(=====\) & \(====\) & \(=====\) \\
Diluted Earnings Per Share & \(\$ 0.52\) & \(\$ 0.07\) & \(\$ 0.59\)
\end{tabular}

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THE BANK OF NEW YORK COMPANY, INC. Consolidated Statements of Income- Supplemental Data (Dollars in millions, except per share amounts) (Unaudited)

\section*{Quarter Ended June 30, 2005}

\begin{tabular}{lll} 
Continuing & Discontinued & Adjusted \\
Operations & Operations & Results(1)
\end{tabular}
\begin{tabular}{|c|c|c|c|}
\hline Net Interest Income & \$ 329 & \$ 141 & \$ 470 \\
\hline Provision for Credit Losses & (3) & 8 & 5 \\
\hline \multicolumn{4}{|l|}{Net Interest Income After Provision for} \\
\hline Credit Losses & 332 & 133 & 465 \\
\hline \multicolumn{4}{|l|}{Noninterest Income} \\
\hline \multicolumn{4}{|l|}{Servicing Fees} \\
\hline Securities & 775 & - & 775 \\
\hline Global Payment Services & 67 & 9 & 76 \\
\hline & 842 & 9 & 851 \\
\hline \multicolumn{4}{|l|}{Private Banking and} \\
\hline Asset Management Fees & 112 & 11 & 123 \\
\hline Service Charges and Fees & 64 & 39 & 103 \\
\hline \multicolumn{4}{|l|}{Foreign Exchange and Other} \\
\hline Securities Gains & 23 & - & 23 \\
\hline
\end{tabular}
\begin{tabular}{|c|c|c|c|}
\hline Other & 52 & 1 & 53 \\
\hline Total Noninterest Income & 1,194 & 62 & 1,256 \\
\hline \multicolumn{4}{|l|}{Noninterest Expense} \\
\hline Salaries and Employee Benefits & 581 & 59 & 640 \\
\hline Net Occupancy & 65 & 17 & 82 \\
\hline Furniture and Equipment & 49 & 2 & 51 \\
\hline Clearing & 42 & - & 42 \\
\hline Sub-custodian Expenses & 24 & - & 24 \\
\hline Software & 55 & - & 55 \\
\hline Communications & 21 & 1 & 22 \\
\hline Amortization of Intangibles & 10 & - & 10 \\
\hline Other & 174 & 23 & 197 \\
\hline Total Noninterest Expense & 1,021 & 102 & 1,123 \\
\hline Income Before Income Taxes & 505 & 93 & 598 \\
\hline Income Taxes & 162 & 38 & 200 \\
\hline Net Income & \$ 343 & \$ 55 & \$ 398 \\
\hline Diluted Earnings Per Share & \$0.45 & \$0.07 & \$0.52 \\
\hline
\end{tabular}

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THE BANK OF NEW YORK COMPANY, INC. Consolidated Statements of Income- Supplemental Data (Dollars in millions, except per share amounts) (Unaudited)

\begin{tabular}{|c|c|c|c|}
\hline \multirow[t]{2}{*}{} & ----- & ----- & ----- \\
\hline & 893 & 8 & 901 \\
\hline \multicolumn{4}{|l|}{Private Banking and} \\
\hline Asset Management Fees & 130 & 11 & 141 \\
\hline Service Charges and Fees & 52 & 37 & 89 \\
\hline \multicolumn{4}{|l|}{Foreign Exchange and Other} \\
\hline Trading Activities & 113 & 2 & 115 \\
\hline Securities Gains & 17 & - & 17 \\
\hline Other & 56 & 13 & 69 \\
\hline Total Noninterest Income & 1,261 & 71 & 1,332 \\
\hline \multicolumn{4}{|l|}{Noninterest Expense} \\
\hline Salaries and Employee Benefits & 604 & 64 & 668 \\
\hline Net Occupancy & 68 & 20 & 88 \\
\hline Furniture and Equipment & 51 & 2 & 53 \\
\hline Clearing & 50 & - & 50 \\
\hline Sub-custodian Expenses & 34 & - & 34 \\
\hline Software & 55 & 1 & 56 \\
\hline Communications & 26 & 1 & 27 \\
\hline Amortization of Intangibles & 13 & - & 13 \\
\hline Other & 164 & 25 & 189 \\
\hline Total Noninterest Expense & 1,065 & 113 & 1,178 \\
\hline Income Before Income Taxes & 535 & 102 & 637 \\
\hline Income Taxes & 175 & 40 & 215 \\
\hline Net Income & \$ 360 & \$ 62 & \$ 422 \\
\hline Diluted Earnings Per Share & \$0.47 & \$0.08 & \$0.55 \\
\hline
\end{tabular}

THE BANK OF NEW YORK COMPANY, INC.
Consolidated Statements of Income- Supplemental Data (Dollars in millions, except per share amounts) (Unaudited)

Adjusted Results(1)
\begin{tabular}{|c|c|c|c|c|}
\hline \multicolumn{3}{|c|}{Quarter Ended} & 6/30/06 & 6/30/ \\
\hline June 30, & June 30, & March 31, & vs. & \\
\hline 2006 & 2005 & 2006 & 6/30/05 & 3/31/ \\
\hline
\end{tabular}
\begin{tabular}{|c|c|c|c|c|}
\hline Net Interest Income & \$ 512 & \$ 470 & \$ 488 & 9\% \\
\hline Provision for Credit Losses & - & 5 & 5 & \\
\hline Net Interest Income After Provision for & & & & \\
\hline
\end{tabular}
\begin{tabular}{|c|c|c|c|c|}
\hline Credit Losses & 512 & 465 & 483 & 10 \\
\hline \multicolumn{5}{|l|}{Noninterest Income} \\
\hline \multicolumn{5}{|l|}{Servicing Fees} \\
\hline Securities & 909 & 775 & 831 & 17 \\
\hline Global Payment Services & 70 & 76 & 70 & (8) \\
\hline & 979 & 851 & 901 & 15 \\
\hline \multicolumn{5}{|l|}{Private Banking and} \\
\hline Asset Management Fees & 150 & 123 & 141 & 22 \\
\hline Service Charges and Fees & 91 & 103 & 89 & (12) \\
\hline \multicolumn{5}{|l|}{Foreign Exchange and Other} \\
\hline Securities Gains & 23 & 23 & 17 & - \\
\hline Other & 51 & 53 & 69 & (4) \\
\hline Total Noninterest Income & 1,426 & 1,256 & 1,332 & 14 \\
\hline \multicolumn{5}{|l|}{Noninterest Expense} \\
\hline Salaries and Employee Benefits & 723 & 640 & 668 & 13 \\
\hline Net Occupancy & 86 & 82 & 88 & 5 \\
\hline Furniture and Equipment & 50 & 51 & 53 & (2) \\
\hline Clearing & 53 & 42 & 50 & 26 \\
\hline Sub-custodian Expenses & 36 & 24 & 34 & 50 \\
\hline Software & 53 & 55 & 56 & (4) \\
\hline Communications & 23 & 22 & 27 & 5 \\
\hline Amortization of Intangibles & 15 & 10 & 13 & 50 \\
\hline Other & 209 & 197 & 189 & 6 \\
\hline Total Noninterest Expense & 1,248 & 1,123 & 1,178 & 11 \\
\hline Income Before Income Taxes & 690 & 598 & 637 & 15 \\
\hline Income Taxes & 242 & 200 & 215 & 21 \\
\hline Net Income & \$ 448 & \$ 398 & \$ 422 & 13 \\
\hline Diluted Earnings Per Share & \$0.59 & \$0.52 & \$0.55 & 13 \\
\hline
\end{tabular}

THE BANK OF NEW YORK COMPANY, INC.
Consolidated Statements of Income- Supplemental Data (Dollars in millions, except per share amounts) (Unaudited)
\begin{tabular}{|c|c|c|c|c|}
\hline Net Interest Income & \$ 697 & \$ 303 & \$1,000 & \$ 925 \\
\hline Provision for Credit Losses & (1) & 6 & 5 & ( 5 ) \\
\hline Net Interest Income After Provision for Credit Losses & 698 & 297 & 995 & 930 \\
\hline Noninterest Income & & & & \\
\hline Servicing Fees & & & & \\
\hline Securities & 1,740 & - & 1,740 & 1,525 \\
\hline Global Payment Services & 125 & 15 & 140 & 151 \\
\hline & 1,865 & 15 & 1,880 & 1,676 \\
\hline Private Banking and & & & & \\
\hline Asset Management Fees & 268 & 23 & 291 & 245 \\
\hline Service Charges and Fees & 105 & 75 & 180 & 195 \\
\hline Foreign Exchange and Other Trading Activities & 243 & 4 & 247 & 199 \\
\hline Securities Gains & 40 & - & 40 & 35 \\
\hline Other & 106 & 14 & 120 & 84 \\
\hline Total Noninterest Income & 2,627 & 131 & 2,758 & 2,434 \\
\hline Noninterest Expense & & & & \\
\hline Salaries and Employee Benefits & 1,260 & 131 & 1,391 & 1,258 \\
\hline Net Occupancy & 136 & 38 & 174 & 160 \\
\hline Furniture and Equipment & 99 & 4 & 103 & 103 \\
\hline Clearing & 103 & - & 103 & 88 \\
\hline Sub-custodian Expenses & 70 & - & 70 & 47 \\
\hline Software & 108 & 1 & 109 & 108 \\
\hline Communications & 48 & 2 & 50 & 45 \\
\hline Amortization of Intangibles & 28 & - & 28 & 18 \\
\hline Other & 347 & 51 & 398 & 373 \\
\hline Total Noninterest Expense & 2,199 & 227 & 2,426 & 2,200 \\
\hline Income Before Income Taxes & 1,126 & 201 & 1,327 & 1,164 \\
\hline Income Taxes & 375 & 82 & 457 & 387 \\
\hline Net Income & \$ 751 & \$ 119 & \$ 870 & \$ 777 \\
\hline Diluted Earnings Per Share & \$0.98 & \$0.15 & \$1.13 & \$1.00 \\
\hline
\end{tabular}

Net Interest Income
Provision for Credit Losses

Net Interest Income After Provision for Credit Losses

Noninterest Income
--------------
Securities
Global Payment Services

Private Banking and
Asset Management Fees
Service Charges and Fees
Foreign Exchange and Other
Trading Activities
Securities Gains
Other

Total Noninterest Income

Noninterest Expense
Salaries and Employee Benefits
Net Occupancy
Furniture and Equipment
Clearing
Sub-custodian Expenses
Software
\[
1,13
\]

1,138

Communications
Amortization of Intangibles Other

Total Noninterest Expense

Income Before Income Taxes
988
Income Taxes

Net Income

Diluted Earnings Per Share

Six Months Ended June 30, 2005
\begin{tabular}{|c|c|c|}
\hline & & 2005 \\
\hline Continuing & Discontinued & Adjusted \\
\hline Operations & Operations & Results (1) \\
\hline
\end{tabular}
\$ 275

15
(20)

670

\begin{tabular}{rrr}
1,525 & - & 1,525 \\
133 & 18 & 151 \\
----- & ---- & ----- \\
1,658 & 18 & 1,676 \\
224 & 21 & 245 \\
118 & 77 & 195 \\
193 & 6 & 199 \\
35 & - & 35 \\
82 & 2 & 84 \\
----- & ---- & ----- \\
2,310 & 124 & 2,434
\end{tabular}

260

, 525
151
1,676

245
195

199
35
84

2,434
-----

930
(5)
30

THE BANK OF NEW YORK COMPANY, INC. Consolidated Balance Sheet - Supplemental Data
(In millions)
(Unaudited)



\section*{Assets}
_-----


Total Liabilities and Shareholders' Equity
\(\qquad\)
\(\qquad\)
\$ 95,150
\$13,731
\$108, 881
\$ 87,402
\(=======\)

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\section*{OTHER DEVELOPMENTS}

On July 11, 2006, the Board of Directors raised the quarterly dividend by 5\% to 22 cents per share payable August 4, 2006 to shareholders of record on July 26, 2006.

The Company was active in redeploying capital during the quarter to sharpen its focus, strengthen its business mix and enhance its long-term growth prospects. In addition to the swap transaction with JPMorgan Chase, the Company announced on June 30, 2006 that it agreed to join forces with Eze Castle Software and GTCR Golder Rauner, LLC, a private equity firm, to form a new company called BNY ConvergEx Group. BNY ConvergEx Group will bring together BNY Securities Group's trade execution, commission management, independent research and transition management business with Eze Castle Software, a leading provider of trade order management and related investment technologies. This transaction enables the Company to achieve several objectives including repositioning its execution services business for faster growth and enhancing the product offering for the Company's client base, while allowing the Company to withdraw capital committed to the business. The new firm is expected to be established by September or October, pending regulatory approval. The Bank of New York Company's Pershing subsidiary, a leading global provider of clearing and financial services outsourcing, is not included in this transaction. For further details see "Acquisitions and Dispositions" in the Notes to the Consolidated Financial Statements and "Capital Resources".

On June 12, 2006, the Company acquired the bond administration business of TD Banknorth, N.A. The TD Banknorth portfolio includes bond trustee, paying/fiscal agent, master trustee, transfer agent and registrar appointments. The transaction involves the purchase of approximately 350 bond trusteeships and agency appointments, representing \(\$ 5.2\) billion of principal debt outstanding for an estimated 230 clients.

\section*{69}

FORWARD-LOOKING STATEMENTS AND RISK FACTORS THAT COULD AFFECT FUTURE RESULTS
Much of the information in this document is forward-looking. This includes all statements about the Company's earnings and revenue outlook, projected business growth, the expected outcome of legal, regulatory and investigatory proceedings, predicted loan losses, and the Company's plans, objectives and strategies. Forward-looking statements represent the Company's current estimates or expectations of future events or results.

The Company, or its executive officers and directors on its behalf, may make additional forward-looking statements from time to time. When used in this report, any press release or any such oral statement, words such as "estimate," "forecast," "project," "anticipate," "confident," "target," "expect," "intend," "think," "continue," "seek," "believe," "plan," "goal," "could," "should," "may," "will," "strategy," and words of similar meaning,

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signify forward-looking statements.
}

Forward-looking statements are based on management's current expectations and assumptions and are subject to risks and uncertainties, some of which are discussed herein, that could cause actual results to differ materially from projected results. Forward-looking statements could be affected by a number of factors, some of which by their nature are dynamic and subject to rapid and possibly abrupt changes that the Company is necessarily unable to predict accurately, including the Risk Factors set forth in the section "ForwardLooking Statements and Risk Factors That Could Affect Future Results" in Part I, Item 1A of the Company's Annual Report on Form \(10-\mathrm{K}\) for the year ended December 31, 2005 and Quarterly Report on Form 10-Q for the quarter ended March 31, 2006.

Forward-looking statements speak only as of the date they are made. The Company will not update forward-looking statements to reflect new facts, changes in assumptions or circumstances, or subsequent events.

\section*{GOVERNEMENT MONETARY POLICIES AND COMPETITION}

\section*{Government Monetary Policies}

The Federal Reserve Board has the primary responsibility for United States monetary policy. Its actions have an important influence on the demand for credit and investments and the level of interest rates, and thus on the earnings of the Company.

\section*{Competition}

The businesses in which the Company operates are very competitive. Competition is provided by both unregulated and regulated financial services organizations, whose products and services span the local, national, and global markets in which the Company conducts operations.

A wide variety of domestic and foreign companies compete for processing services. For securities servicing and global payment services, international, national, and regional commercial banks, trust banks, investment banks, specialized processing companies, outsourcing companies, data processing companies, stock exchanges, and other business firms offer active competition. In the private banking and asset management markets, international, national, and regional commercial banks, standalone asset management companies, mutual funds, securities brokerage firms, insurance companies, investment counseling firms, and other business firms and individuals actively compete for business. Commercial banks, savings banks, savings and loan associations, and credit unions actively compete for deposits, and money market funds and brokerage houses offer deposit-like services. These institutions, as well as consumer and commercial finance companies, national retail chains, factors, insurance companies and pension trusts, are important competitors for various types of loans. Issuers of commercial paper compete actively for funds and reduce demand for bank loans.

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\section*{WEBSITE INFORMATION}

The Company makes available on its website, www.bankofny.com:
* All of its SEC filings, including annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to these reports, SEC Forms 3, 4 and 5 and its proxy statement as soon as reasonably practicable after such
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material is electronically filed with or furnished to the SEC;

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* Its earnings releases and management conference calls and presentations; and
* Its corporate governance guidelines and the charters of the Audit and Examining, Compensation and Organization, and Nominating and Governance Committees of its Board of Directors.

The corporate governance guidelines and committee charters are available in print to any shareholder who requests them. Requests should be sent to The Bank of New York Company, Inc., Corporate Communications, One Wall Street, NY, NY 10286.

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> THE BANK OF NEW YORK COMPANY, INC.
> Consolidated Balance Sheets
> (Dollars in millions, except per share amounts)
> (Unaudited)

June 30, 2006

\section*{Assets}
\begin{tabular}{|c|c|c|c|c|}
\hline Cash and Due from Banks & \$ & 3,010 & \$ & 2,882 \\
\hline Interest-Bearing Deposits in Banks & & 11,978 & & 8,644 \\
\hline Securities & & & & \\
\hline Held-to-Maturity (fair value of \$2,108 in 2006 and \(\$ 1,847\) in 2005) & & 2,167 & & 1,872 \\
\hline Available-for-Sale & & 25,188 & & 25,346 \\
\hline Total Securities & & 27,355 & & 27,218 \\
\hline Trading Assets at Fair Value & & 6,065 & & 5,930 \\
\hline Federal Funds Sold and Securities Purchased Under Resale Agreements & & 2,235 & & 2,425 \\
\hline Loans (less allowance for loan losses of \$337 in 2006 and \(\$ 326\) in 2005) & & 35,313 & & 32,601 \\
\hline Premises and Equipment & & 963 & & 960 \\
\hline Due from Customers on Acceptances & & 210 & & 212 \\
\hline Accrued Interest Receivable & & 394 & & 363 \\
\hline Goodwill & & 3,784 & & 3,510 \\
\hline Intangible Assets & & 885 & & 811 \\
\hline Other Assets & & 7,743 & & 7,710 \\
\hline Assets of Discontinued Operations Held for Sale & & 8,946 & & 8,808 \\
\hline Total Assets & \$ & 108,881 & \$ & 102,074 \\
\hline Liabilities and Shareholders' Equity & & & & \\
\hline Deposits & & & & \\
\hline Noninterest-Bearing (principally domestic offices) & \$ & 15,930 & \$ & 12,706 \\
\hline Interest-Bearing & & & & \\
\hline Domestic Offices & & 9,958 & & 10,415 \\
\hline Foreign Offices & & 30,853 & & 26,666 \\
\hline Total Deposits & & 56,741 & & 49,787 \\
\hline Federal Funds Purchased and Securities & & & & \\
\hline Sold Under Repurchase Agreements & & 1,177 & & 834 \\
\hline
\end{tabular}


Note: The balance sheet at December 31, 2005 has been derived from the audited financial statemen that date.

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Interest Income
\begin{tabular}{lrrrrrcc} 
Loans & \(\$ 350\) & \(\$\) & 243 & \(\$ 660\) & \(\$\) & 476 & \(44 \%\) \\
Margin loans & 85 & 62 & 162 & 117 & 37 \\
Securities & & & & & \\
\(\quad\) Taxable & 280 & 193 & 545 & 359 & 45 \\
Exempt from Federal Income Taxes & 9 & 10 & 18 & 18 & (10)
\end{tabular}


THE BANK OF NEW YORK COMPANY, INC. Consolidated Statements of Income (In millions, except per share amounts)
(Unaudited)

\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|}
\hline \multicolumn{10}{|l|}{Discontinued Operations} \\
\hline Income from Discontinued Operations & & 99 & & 93 & & 201 & & 176 & 6\% \\
\hline Income Taxes & & 42 & & 38 & & 82 & & 70 & 11 \\
\hline Discontinued Operations, net & & 57 & & 55 & & 119 & & 106 & 4 \\
\hline Net Income & \$ & 448 & \$ & 398 & \$ & 870 & \$ & 777 & 13 \\
\hline \multicolumn{10}{|l|}{Per Common Share Data:} \\
\hline \multicolumn{10}{|l|}{Basic Earnings} \\
\hline Income from Continuing Operations & \$ & 0.52 & \$ & 0.45 & \$ & 0.99 & \$ & 0.87 & 16 \\
\hline Income from Discontinued Operations, Net & & 0.07 & & 0.07 & & 0.15 & & 0.14 & - \\
\hline Net Income & & 0.59 & & 0.52 & & 1.14 & & 1.01 & 13 \\
\hline \multicolumn{10}{|l|}{Diluted Earnings} \\
\hline Income from Continuing Operations & \$ & 0.52 & \$ & 0.45 & \$ & 0.98 & \$ & 0.86 & 16 \\
\hline Income from Discontinued Operations, Net & & 0.07 & & 0.07 & & 0.15 & & 0.14 & - \\
\hline Net Income & & 0.59 & & 0.52 & & 1.13 & & 1.00 & 13 \\
\hline Cash Dividends Paid & & 0.21 & & 0.20 & & 0.42 & & 0.40 & 5 \\
\hline Diluted Shares Outstanding & & 765 & & 772 & & 769 & & 775 & (1) \\
\hline
\end{tabular}

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THE BANK OF NEW YORK COMPANY, INC.
Consolidated Statement of Changes in Shareholders' Equity For the six months ended June 30, 2006
(Dollars in millions)
(Unaudited)

Common Stock
Balance, January 1 \$, 838
Issuances in Connection with Employee Benefit Plans 29

Balance, June 30

Additional Capital

\begin{tabular}{|c|c|c|c|c|}
\hline & \multicolumn{4}{|l|}{```
For the six months
    ended June 30,
    2006 2005
```} \\
\hline \multicolumn{5}{|l|}{Operating Activities} \\
\hline Net Income & \$ & 870 & \$ & 777 \\
\hline \multicolumn{5}{|l|}{Adjustments to Determine Net Cash Attributable to} \\
\hline \multicolumn{5}{|l|}{Operating Activities:} \\
\hline \multicolumn{5}{|l|}{Provision for Credit Losses} \\
\hline Depreciation and Amortization & & 219 & & 248 \\
\hline Deferred Income Taxes & & 98 & & 131 \\
\hline Securities Gains & & (40) & & (35) \\
\hline Change in Trading Activities & & 484 & & \((1,977)\) \\
\hline Change in Accruals and Other, Net & & 971 & & 143 \\
\hline Net Cash Provided by (Used for) Operating Activities & & 2,607 & & (718) \\
\hline \multicolumn{5}{|l|}{Investing Activities} \\
\hline Change in Interest-Bearing Deposits in Banks & & \((2,981)\) & & 623 \\
\hline Change in Margin Loans & & 992 & & 4 \\
\hline Purchases of Securities Held-to-Maturity & & ( 506 ) & & (480) \\
\hline Paydowns of Securities Held-to-Maturity & & 140 & & 155 \\
\hline Maturities of Securities Held-to-Maturity & & 81 & & 23 \\
\hline Purchases of Securities Available-for-Sale & & \((6,331)\) & & \((8,402)\) \\
\hline Sales of Securities Available-for-Sale & & 1,780 & & 2,083 \\
\hline Paydowns of Securities Available-for-Sale & & 2,471 & & 3,160 \\
\hline Maturities of Securities Available-for-Sale & & 2,312 & & 1,315 \\
\hline Net Principal Disbursed on Loans to Customers & & \((3,915)\) & & \((5,376)\) \\
\hline Sales of Loans and Other Real Estate & & 97 & & 126 \\
\hline Change in Federal Funds Sold and Securities Purchased Under Resale Agreements & & 190 & & \((1,486)\) \\
\hline Purchases of Premises and Equipment & & (86) & & (42) \\
\hline Acquisitions, Net of Cash Acquired & & (349) & & (70) \\
\hline Proceeds from the Sale of Premises and Equipment & & 3 & & \\
\hline Other, Net & & (159) & & 19 \\
\hline Net Cash Used for Investing Activities & & \((6,261)\) & & \((8,348)\) \\
\hline \multicolumn{5}{|l|}{Financing Activities} \\
\hline Change in Deposits & & 5,135 & & 6,243 \\
\hline Change in Federal Funds Purchased and Securities Sold Under Repurchase Agreements & & 343 & & 210 \\
\hline Change in Payables to Customers and Broker-Dealers & & \((1,986)\) & & (17) \\
\hline Change in Other Borrowed Funds & & 337 & & 536 \\
\hline Proceeds from the Issuance of Long-Term Debt & & 1,114 & & 1,538 \\
\hline Repayments of Long-Term Debt & & (545) & & (102) \\
\hline Issuance of Common Stock & & 182 & & 81 \\
\hline Treasury Stock Acquired & & (452) & & (338) \\
\hline Cash Dividends Paid & & (323) & & (321) \\
\hline Net Cash Provided by Financing Activities & & 3,805 & & 7,830 \\
\hline Effect of Exchange Rate Changes on Cash & & (47) & & 307 \\
\hline Change in Cash and Due From Banks & & 104 & & (929) \\
\hline Cash and Due from Banks at Beginning of Period & & 3,515 & & 3,886 \\
\hline Cash Related to Discontinued Operations & & (609) & & (616) \\
\hline Cash and Due from Banks at End of Period & \$ & 3,010 & \$ & 2,341 \\
\hline
\end{tabular}

Supplemental Disclosure of Cash Flow Information
Cash Paid During the Period for:
Interest \$ 1,066 \$ 594
Income Taxes 140
Noncash Investing Activity
(Primarily Foreclosure of Real Estate)

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THE BANK OF NEW YORK COMPANY, INC. \\ Notes to Consolidated Financial Statements
}

\section*{1. General}

The accounting and reporting policies of The Bank of New York Company, Inc., a financial holding company, and its consolidated subsidiaries (the "Company") conform with generally accepted accounting principles and general practice within the banking industry. Such policies are consistent with those applied in the preparation of the Company's annual financial statements.

The accompanying consolidated financial statements are unaudited. In the opinion of management, all adjustments necessary for a fair presentation of financial position, results of operations and cash flows for the interim periods have been made. Certain other reclassifications have been made to prior periods to place them on a basis comparable with current period presentation.

\section*{2. Accounting Changes and New Accounting Pronouncements}

The Company adopted SFAS No. 123 ("SFAS 123"), "Accounting for Stock-Based Compensation," in 1995. At that time, as permitted by the standard, the Company elected to continue to apply the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and accounted for the options granted to employees using the intrinsic value method, under which no expense is recognized for stock options because they were granted at the stock price on the grant date and therefore have no intrinsic value.

On January 1, 2003, the Company adopted the fair value method of accounting for its options under SFAS 123 as amended by SFAS No. 148 ("SFAS 148"), "Accounting for Stock-Based Compensation-Transition and Disclosure." SFAS 148 permitted three different methods of adopting fair value: (1) the prospective method, (2) the modified prospective method, and (3) the retroactive restatement method. Under the prospective method, options issued after January 1, 2003 are expensed while all options granted prior to January 1,2003 are accounted for under APB 25 using the intrinsic value method. Consistent with industry practice, the Company elected the prospective method of adopting fair value accounting.

During the first six months ended June 30, 2006, approximately 6.2 million options were granted. In the second quarter and first six months of 2006 , the Company recorded \(\$ 14\) million and \(\$ 24\) million of stock option expense.

The retroactive restatement method requires the Company's financial statements to be restated as if fair value accounting had been adopted in 1995.

The following table discloses the pro forma effects on the Company's net income and earnings per share as if the retroactive restatement method had been adopted.
```

(Dollars in millions,
except per share amounts)
Reported net income
Stock based employee compensation costs,
using prospective method, net of tax
Stock based employee compensation costs,
using retroactive restatement method,
net of tax

```
Pro forma net income
Reported diluted earnings per share
Impact on diluted earnings per share
Pro forma diluted earnings per share
\begin{tabular}{|c|c|c|c|c|c|c|}
\hline \multirow[t]{2}{*}{\[
\begin{gathered}
\text { Second } \\
2006
\end{gathered}
\]} & \multicolumn{2}{|l|}{\multirow[t]{2}{*}{\[
\begin{gathered}
\text { Quarter } \\
2005
\end{gathered}
\]}} & \multicolumn{4}{|r|}{Year-to-date} \\
\hline & & & & 006 & & 005 \\
\hline \$ 448 & \$ & 398 & \$ & 870 & \$ & 777 \\
\hline 8 & & 8 & & 14 & & 14 \\
\hline (8) & & (11) & & (14) & & (21) \\
\hline \$ 448 & \$ & 395 & \$ & 870 & \$ & 770 \\
\hline \$ 0.59 & \$ & 0.52 & \$ & 1.13 & \$ & 1.00 \\
\hline - & & - & & - & & \(0.01)\) \\
\hline \$ 0.59 & \$ & 0.52 & \$ & 1.13 & & 0.99 \\
\hline
\end{tabular}

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The fair value of options granted in 2006 and 2005 were estimated at the grant date using the following weighted average assumptions:

Dividend yield
Expected volatility
Risk free interest rates
Expected options lives
\begin{tabular}{cccc}
\multicolumn{2}{c}{ Second } & Quarter & \multicolumn{2}{c}{ Year-to-date } \\
2006 & 2005 & 2006 & 2005 \\
---- & ----- & --- & --- \\
\(2.77 \%\) & \(2.95 \%\) & \(2.77 \%\) & \(2.77 \%\) \\
22.43 & 25.00 & 22.43 & 25.21 \\
4.72 & 3.94 & 4.72 & 4.18 \\
6 & 5 & 6 & 5
\end{tabular}

In December 2004, the FASB issued FASB Statement No. 123 (revised 2004) ("SFAS \(123(R)\) "), "Share-Based Payment," which is a revision of FASB Statement No. 123, "Accounting for Stock-Based Compensation." SFAS \(123(R)\) eliminates the ability to account for share-based compensation transactions using Accounting Principles Board Opinion No. 25 and requires that such transactions be accounted for using a fair value-based method. SFAS 123(R) covers a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans. The Company adopted SFAS \(123(R)\) on January 1, 2006 using the "modified prospective" method. Under this method, compensation cost is recognized beginning with the effective date (a) based on the requirements of SFAS \(123(R)\) for all share-based payments granted after the effective date and (b) based on the requirements of SFAS 123 for all awards granted to employees prior to the effective date of SFAS \(123(R)\) that remain unvested on the effective date.

The Company adopted the fair value method of accounting for stock-based compensation prospectively as of January 1, 2003. As of January 1, 2006, the Company was amortizing all of its unvested stock option grants.

Certain of the Company's stock compensation grants vest when the employee retires. SFAS \(123(R)\) requires the completion of expensing of new grants with this feature by the first date the employee is eligible to retire. For grants prior to January 1, 2006, the Company will continue to expense them over their stated vesting period. The adoption of SFAS \(123(R)\) increased pre-tax expense

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}
in 2006 by \(\$ 12\) million, which was recorded in the second quarter of 2006 .
In June 2004, the FASB issued an Exposure Draft of a proposed Statement, "Fair Value Measurements". The Exposure Draft, if adopted, will standardize fair value guidance by creating a comprehensive framework for measuring the fair value of most financial and nonfinancial assets and liabilities. The proposed Statement also requires expanded quantitative and qualitative disclosures about the use of fair value to remeasure assets and liabilities recognized in the statement of financial position. A final standard is expected to be issued in the third quarter of 2006. The final standard is expected to be effective for the Company's financial statements issued for 2008, and interim periods within that year. Upon issuance of the final standard, the Company will assess the impact of the new standard on the Company's consolidated financial statements.

In June 2005, the FASB ratified the consensus in EITF Issue No. 04-5("EITF 04-5"), "Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights", which provides guidance in determining whether a general partner controls a limited partnership. The adoption of EITF 04-5 did not have a significant impact on the Company's financial condition or results of operations.

In February 2006, the FASB issued FASB Statement No. 155 ("SFAS 155"), "Accounting for Certain Hybrid Financial Instruments", an amendment of SFAS 140 and SFAS 133. SFAS 155 permits the Company to elect to measure any hybrid financial instrument at fair value if the hybrid instrument contains an embedded derivative that otherwise would require bifurcation and be accounted for separately under SFAS 133. This statement clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS

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133 and that concentrations of credit risk in the form of subordination are not embedded derivatives. SFAS 155 is effective for all financial instruments acquired, issued, or subject to a remeasurement event after December 31, 2006. The Company does not expect the adoption of the standard will have a significant impact on its financial condition or results of operations.

In March 2006, the FASB issued an Exposure Draft, "Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans." The proposed standard would recognize as a component of other comprehensive income, net of tax, the actuarial gains and losses and prior service costs and credits that are not currently recognized as components of net period benefit cost pursuant to SFAS 87 or 106 . The standard would also recognize, as an adjustment to the opening balance of retained earnings, any transition asset or obligation, net of tax, arising from the initial application of SFAS 87 or 106 . The FASB has indicated it expects to issue a final statement in the third quarter of 2006. The Exposure Draft indicates that the new standard would be applicable to the Company for year-end 2006. The Company anticipates that the adoption of this statement will result in a material charge to equity, the amount of which is under assessment.

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes." The Interpretation clarifies the accounting for uncertain tax positions in accordance with FASB Statement No. 109, "Accounting for Income Taxes." The Interpretation requires that a tax position meet a "more-likely-than-not threshold" for the benefit of the uncertain tax position to be recognized in the financial statements. A tax position that fails to meet a more-likely-than-not recognition threshold will result in either reduction of current or deferred tax assets, and/or recording of current or deferred tax liabilities. The proposed Interpretation also provides guidance on measurement,
derecognition of tax benefits, classification, interim period accounting disclosure, and transition requirements in accounting for uncertain tax positions. The Company is assessing the impact of adopting the new pronouncement, which will become effective January 1, 2007 , but it is not expected to have a material impact.

In July 2006, the FASB issued FSP FAS 13-2, "Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leverage Lease Transaction," revising the accounting guidance under SFAS No. 13 ("SFAS 13"), "Accounting for Leases," for leveraged leases. This FSP modifies existing interpretations of SFAS 13 and associated industry practice. As a result, in January 2007 , the Company expects to recognize a one-time after-tax charge to capital of \(\$ 340\) to \(\$ 385\) million related to a change in the timing of its lease cash flows due to the LILO settlement. See Note "Commitments and Contingent Liabilities". However, an amount approximating this one-time charge will be taken into income over the remaining term of the affected leases.

Certain other prior year information has been reclassified to conform its presentation with the 2006 financial statements.

\section*{3. Acquisitions and Dispositions}

The Company continues to be an active acquirer of securities servicing and asset management businesses.

The Company announced four acquisitions in 2006. The total cost of completed acquisitions in the second quarter and six months of 2006 was \(\$ 2\) million and \(\$ 325\) million, primarily paid in cash. The Company frequently structures its acquisitions with both an initial payment and a later contingent payment tied to post-closing revenue or income growth. The Company records the fair value of contingent payments as an additional cost of the entity acquired in the period that the payment becomes probable.

Goodwill related to acquisitions in the second quarter of 2006 and first six months of 2006 was \(\$ 2\) million and \(\$ 214\) million, respectively. The taxdeductible portion of goodwill related to acquisitions in the second quarter and first six months of 2006 was \(\$ 2\) million and \(\$ 75\) million, respectively. At

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June 30, 2006, the Company was liable for potential contingent payments related to acquisitions in the amount of \(\$ 193\) million. During the second quarter and the first six months of 2006 , the Company paid or accrued \(\$ 5\) million and \(\$ 22\) million for contingent payments related to acquisitions made in prior years.

\section*{2006}

On January 3, 2006, the Company acquired Alcentra, an international asset management group focused on managing funds that invest in non-investment grade debt. Alcentra's management team retained a 20 percent interest. Alcentra has operations in London and Los Angeles and currently manages 15 different investment funds with over \(\$ 6.2\) billion of assets.

On March 2, 2006, the Company acquired Urdang, a real estate investment management firm that manages approximately \(\$ 3.0\) billion in direct investments and portfolios of REIT securities.

On April 8, 2006, the Company announced a definitive agreement to sell its retail and regional middle market banking businesses to JPMorgan Chase for \$3.1

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billion with a premium of \(\$ 2.3\) billion. For further details, see "Discontinued Operations" Note. JPMorgan Chase will sell its corporate trust business to the Company for \(\$ 2.8\) billion with a premium of \(\$ 2.15\) billion. The difference in premiums results in a net cash payment of \(\$ 150\) million to the Company. There is also a contingent payment of up to \(\$ 50\) million to the Company tied to customer retention.

The transaction further increases the Company's focus on the securities services and wealth management businesses that have fueled the Company's growth in recent years and that are at the core of its long-term business strategy.

The transaction has been approved by each company's board of directors and is expected to be completed in the fourth quarter of 2006 , subject to regulatory approvals. The Company expects to record an after-tax gain of \$1.3 billion on the businesses to be sold. The Company also expects to incur aftertax charges of \(\$ 90-120\) million related to the acquisition. The transaction is expected to be dilutive to GAAP earnings per share through 2009 ( 4.5 percent in 2007 to 1.5 percent in 2009), but to be accretive to cash earnings per share in 2009 when cost savings are fully phased in.

JPMorgan Chase's corporate trust business comprises issues representing \$5 trillion in total debt outstanding. It has 2,400 employees in more than 40 locations globally. The Company's corporate trust business comprises issues representing \(\$ 3\) trillion in total debt outstanding. It has 1,300 employees in 25 locations globally.

The Company's retail bank consists of 341 branches in the tri-state region, serving approximately 700,000 consumer households and small businesses with \(\$ 14.5\) billion in deposits and \(\$ 15.4\) billion in assets. The Company's regional middle market businesses provide financing, banking and treasury services for middle market clients, serving more than 2,000 clients in the tristate region. Together, the units have 4,000 employees located in New York, New Jersey, Connecticut and Delaware.

On June 12, 2006, the Company acquired the bond administration business of TD Banknorth, N.A. The TD Banknorth portfolio includes bond trustee, paying/fiscal agent, master trustee, transfer agent and registrar appointments. The transaction involves the purchase of approximately 350 bond trusteeships and agency appointments, representing \(\$ 5.2\) billion of principal debt outstanding for an estimated 230 clients.

On June 30, 2006, the Company announced that it agreed to join forces with Eze Castle Software and GTCR Golder Rauner, LLC, a private equity firm, to form a new company called BNY ConvergEx Group. BNY ConvergEx Group will bring together BNY Securities Group's trade execution, commission management, independent research and transition management business with Eze Castle Software, a leading provider of trade order management and related investment technologies. This transaction enables the Company to achieve several

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objectives including repositioning its execution services business for faster growth and enhancing the product offering for the Company's client base, while allowing the Company to withdraw capital committed to the business. The new firm is expected to be established by September or October, pending regulatory approval.

BNY ConvergEx Group will be a leading global agency brokerage and technology company offering a complete spectrum of pre-trade, trade, and posttrade solutions for traditional money managers, hedge funds, broker-dealers, corporations and plan sponsors. BNY ConvergEx Group will have a global presence in New York, Boston, San Francisco, Chicago, Dallas, Stamford, London, Bermuda,

Tokyo, Hong Kong, and Sydney.
Once the transaction is complete, the Company and GTCR Golder Rauner, LLC will each hold a 35.4 percent stake in BNY ConvergEx Group, with the balance held by Eze Castle Software's investors and BNY ConvergEx Group's management team. BNY ConvergEx Group, with proforma 2005 revenues of approximately \(\$ 340\) million, will be an affiliate of The Bank of New York and will be reflected on the Company's financial statements as an equity investment. The transaction is not expected to result in any net gain or loss for The Bank of New York and is expected to be neutral to earnings per share.

The BNY Securities Group businesses to be included in BNY ConvergEx Group will be BNY Brokerage, Lynch, Jones, \& Ryan, G-Port, Westminster Research and BNY Jaywalk. Each business will retain its respective brand name and continue to operate as it does today, while taking advantage of the combined capabilities of BNY ConvergEx Group. In addition, The Bank of New York's BTrade and G-Trade businesses are expected to become part of BNY ConvergEx Group in 2008, although in the interim they will continue to be owned by The Bank of New York. The Bank of New York Company's Pershing subsidiary, a leading global provider of clearing and financial services outsourcing, is not included in this transaction. See "Other Developments" in the MD\&A section for additional information.

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\section*{4. Discontinued Operations}

In the second quarter of 2006, the Company adopted discontinued operations accounting for its retail and regional middle market banking businesses to be sold to JPMorgan Chase.

Results for all the retail and regional middle market banking businesses are reported separately as discontinued operations for all periods presented. The assets and liabilities of the businesses being sold are included in assets of discontinued operations held for sale and liabilities of discontinued operations held for sale on the consolidated balance sheet. Net interest income has been computed by allocating investment securities and federal funds sold and related interest income to discontinued operations to match the amount and duration of the assets sold with the amount and duration of the liabilities sold.

Also included in the sales agreement between the Company and JPMorgan Chase are provisions related to transitional services that will be provided for a period of up to 8 months after closing, subject to extensions.

Summarized financial information for discontinued operations related to the sale of the retail and regional middle market banking businesses is as follows:
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|}
\hline \multirow[b]{2}{*}{(In millions)} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{\(2 Q 06\)}} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{1906}} & \multicolumn{2}{|r|}{\multirow[b]{2}{*}{\(2 Q 05\)}} & \multicolumn{4}{|r|}{Year-to-date} \\
\hline & & & & & & & & 06 & & 05 \\
\hline Net Interest Income & \$ & 154 & \$ & 149 & \$ & 141 & \$ & 303 & & 275 \\
\hline Noninterest Income & & 60 & & 71 & & 62 & & 131 & & 124 \\
\hline \begin{tabular}{l}
Total Revenues, \\
Net of Interest Expenses
\end{tabular} & \$ & 214 & \$ & & \$ & & \$ & 434 & & 399 \\
\hline \begin{tabular}{l}
Income from \\
Discontinued Operations
\end{tabular} & \$ & 99 & \$ & 102 & \$ & & \$ & 201 & & 176 \\
\hline Income Taxes & & 42 & & 40 & & 38 & & 82 & & 70 \\
\hline
\end{tabular}
Income from Discontinued
Operations, Net of Taxes \(\quad \$ \quad 57 \quad \$ \quad 62\)
O

The following is a summary of the assets and liabilities of discontinued operations held for sale as of June 30, 2006 and December 31, 2005:

\section*{(In millions)}

June 30, December 31, 2006

Assets
------
\begin{tabular}{|c|c|c|}
\hline Cash and Due from Banks & \$ 609 & \$ 633 \\
\hline Securities & 104 & 108 \\
\hline Loans & 7,892 & 7,714 \\
\hline Goodwill & 109 & 109 \\
\hline Other Assets & 232 & 244 \\
\hline Total Assets & \$ 8,946 & \$ 8,808 \\
\hline Liabilities & & \\
\hline Deposits & \$13,678 & \$14,637 \\
\hline Other Liabilities & 53 & 35 \\
\hline Total Liabilities & \$13,731 & \$14, 672 \\
\hline
\end{tabular}

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5. Goodwill and Intangibles

Goodwill by reportable segment is as follows:
(In millions)


The Company's reporting units are tested annually for goodwill impairment.

Intangible Assets
-------------------

June 30, 2006
\begin{tabular}{ccc} 
& & Weighted \\
Gross & Net & Average \\
Carrying Accumulated Carrying & Amortization \\
Amount Amortization Amount & Period in Years
\end{tabular}

December 31, 2005

\footnotetext{
Gross Net
Carrying Accumulated Carry Amount Amortization Amou
}
\begin{tabular}{|c|c|c|c|c|c|c|c|c|c|c|c|}
\hline Trade Names \$ & 378 & \$ & - & \$ & 378 & Indefinite & Life & \$ & 370 & \$ & - \$ \\
\hline Customer Relationships & 628 & & (125) & & 503 & 15 & & & 531 & & (99) \\
\hline Other Intangible Assets & 25 & & (21) & & 4 & 6 & & & 28 & & (19) \\
\hline
\end{tabular}

The aggregate amortization expense of intangibles was \(\$ 15\) million and \(\$ 10\) million for the quarters ended June 30, 2006 and 2005, respectively. The aggregate amortization expense of intangibles was \(\$ 28\) million and \(\$ 18\) million for the six months ended June 30, 2006 and 2005. Estimated amortization expense for current intangibles for the next five years is as follows:
\begin{tabular}{|c|c|c|}
\hline (In millions) & For the Year Ended December 31, & Amortization Expense \\
\hline & 2006 & \$57 \\
\hline & 2007 & 53 \\
\hline & 2008 & 52 \\
\hline & 2009 & 50 \\
\hline & 2010 & 48 \\
\hline
\end{tabular}
6. Allowance for Credit Losses

The allowance for credit losses is maintained at a level that, in management's judgment, is adequate to absorb probable losses associated with specifically identified loans, as well as estimated probable credit losses inherent in the remainder of the loan portfolio at the balance sheet date. Management's judgment includes the following factors, among others: risks of individual credits; past experience; the volume, composition, and growth of the loan portfolio; and economic conditions.

The Company conducts a quarterly portfolio review to determine the adequacy of its allowance for credit losses. All commercial loans over \$1 million are assigned to specific risk categories. Smaller commercial and consumer loans are evaluated on a pooled basis and assigned to specific risk categories. Following this review, senior management of the Company analyzes the results and determines the allowance for credit losses. The Risk Committee of the Company's Board of Directors reviews the allowance at the end of each quarter.

The portion of the allowance for credit losses allocated to impaired loans (nonaccrual commercial loans over \(\$ 1\) million) is measured by the difference between their recorded value and fair value. Fair value is the present value

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of the expected future cash flows from borrowers, the market value of the loan, or the fair value of the collateral.

Commercial loans are placed on nonaccrual status when collateral is insufficient and principal or interest is past due 90 days or more, or when there is reasonable doubt that interest or principal will be collected. Accrued interest is usually reversed when a loan is placed on nonaccrual status. Interest payments received on nonaccrual loans may be recognized as income or applied to principal depending upon management's judgment.
Nonaccrual loans are restored to accrual status when principal and interest are current or they become fully collateralized. Consumer loans are not classified as nonperforming assets, but are charged off and interest accrued is suspended based upon an established delinquency schedule determined by product. Real estate acquired in satisfaction of loans is carried in other assets at the
lower of the recorded investment in the property or fair value minus estimated costs to sell.

Transactions in the allowance for credit losses are summarized as follows:

\section*{Continuing Operations}
(In millions)
Balance, Beginning of Period
\(\quad\)\begin{tabular}{l} 
Charge-Offs \\
\(\quad\) Recoveries
\end{tabular}
\(\quad\)\begin{tabular}{l} 
Net Charge-Offs \\
Provision
\end{tabular}
Balance, End of Period
(In millions)
Balance, Beginning of Period
\(\quad\)\begin{tabular}{l} 
Charge-Offs \\
Recoveries
\end{tabular}
\(\quad\)\begin{tabular}{l} 
Net Charge-Offs \\
Provision
\end{tabular}
Balance, End of Period
\begin{tabular}{|c|c|c|c|c|c|}
\hline \multicolumn{2}{|l|}{Allowance for Loan Losses} & \multicolumn{2}{|l|}{Allowance for Lending-Related Commitments} & \multicolumn{2}{|l|}{Allowance for Credit Losses} \\
\hline \$ & 486 & \$ & 124 & \$ & 610 \\
\hline & (7) & & - & & (7) \\
\hline & 1 & & - & & 1 \\
\hline & (6) & & - & & (6) \\
\hline & (17) & & 14 & & (3) \\
\hline \$ & 463 & \$ & 138 & \$ & 601 \\
\hline
\end{tabular}

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(In millions)
Balance, Beginning of Period
\(\quad\)\begin{tabular}{l} 
Charge-Offs \\
Recoveries
\end{tabular}
\(\quad\)\begin{tabular}{l} 
Net Charge-Offs \\
Provision
\end{tabular}
Balance, End of Period
(In millions)
\begin{tabular}{|c|c|c|c|c|c|}
\hline \multicolumn{2}{|l|}{Allowance for Loan Losses} & \multicolumn{2}{|l|}{Allowance for Lending-Related Commitments} & \multicolumn{2}{|l|}{Allowance for Credit Losses} \\
\hline \$ & 326 & \$ & 145 & \$ & 471 \\
\hline & (4) & & - & & (4) \\
\hline & 14 & & - & & 14 \\
\hline & 10 & & - & & 10 \\
\hline & 1 & & (2) & & (1) \\
\hline \$ & 337 & \$ & 143 & \$ & 480 \\
\hline
\end{tabular}
\begin{tabular}{|c|c|c|c|c|c|c|}
\hline & \begin{tabular}{l}
All \\
Loa
\end{tabular} & \[
\begin{aligned}
& \text { for } \\
& \text { ses }
\end{aligned}
\] & \multicolumn{2}{|l|}{Allowance for Lending－Related Commitments} & \multicolumn{2}{|l|}{Allowance for Credit Losses} \\
\hline Balance，Beginning of Period & \＄ & 491 & \＄ & 136 & \＄ & 627 \\
\hline Charge－Offs & & （7） & & － & & （7） \\
\hline Recoveries & & 1 & & － & & 1 \\
\hline Net Charge－Offs & & （6） & & － & & （6） \\
\hline Provision & & （22） & & 2 & & （20） \\
\hline Balance，End of Period & \＄ & 463 & \＄ & 138 & \＄ & 601 \\
\hline
\end{tabular}

7．Capital Transactions

The Company has 5 million authorized shares of Class A preferred stock having a par value of \(\$ 2.00\) per share．At June 30,2006 and December 31，2005， 3,000 shares were outstanding．

In addition to the Class A preferred stock，the Company has 5 million authorized shares of preferred stock having no par value，with no shares outstanding at June 30,2006 and December 31,2005 ，respectively．

On July 11， 2006 ，the Board of Directors raised the quarterly dividend by \(5 \%\) to 22 cents per share payable August 4,2006 to shareholders of record on July 26， 2006.

The Company repurchased 10.3 million shares in the second quarter of 2006 ． Included in the buyback were 10.0 million shares that were repurchased on April 3， 2006 through the previously disclosed accelerated share repurchase program．

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8．Earnings Per Share
－ーーーー－

The following table illustrates the computations of basic and diluted earnings per share：
\begin{tabular}{|c|c|c|c|c|c|c|c|c|}
\hline \multirow[t]{2}{*}{（Dollars in millions， except per share amounts）} & \multicolumn{4}{|l|}{Three Months Ended June 30，} & \multicolumn{4}{|r|}{Six Months Ended June 30，} \\
\hline & \multicolumn{2}{|c|}{2006} & \multicolumn{2}{|c|}{2005} & \multicolumn{2}{|c|}{2006} & \multicolumn{2}{|r|}{2005} \\
\hline Income from Continuing Operations & \＄ & 391 & \＄ & 343 & \＄ & 751 & \＄ & 671 \\
\hline Income from Discontinued Operations & & 57 & & 55 & & 119 & & 106 \\
\hline Net Income（1） & \＄ & 448 & \＄ & 398 & \＄ & 870 & \＄ & 777 \\
\hline \multicolumn{9}{|l|}{Basic Weighted Average} \\
\hline Shares Outstanding & & 756 & & 765 & & 760 & & 768 \\
\hline Shares Issuable Upon Conversion of Employee Stock Options & & 9 & & 7 & & 9 & & 7 \\
\hline
\end{tabular}

Shares Outstanding
\begin{tabular}{|c|c|c|c|c|c|c|c|}
\hline & 765 & & 772 & & 769 & & 775 \\
\hline \multirow[t]{3}{*}{\$} & 0.52 & \$ & 0.45 & \$ & 0.99 & \$ & 0.87 \\
\hline & 0.07 & & 0.07 & & 0.15 & & 0.14 \\
\hline & 0.59 & & 0.52 & & 1.14 & & 1.01 \\
\hline \multirow[t]{3}{*}{\$} & 0.52 & \$ & 0.45 & \$ & 0.98 & \$ & 0.86 \\
\hline & 0.07 & & 0.07 & & 0.15 & & 0.14 \\
\hline & 0.59 & & 0.52 & & 1.13 & & 1.00 \\
\hline
\end{tabular}
9. Employee Benefit Plans

The components of net periodic benefit cost are as follows:


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\section*{10. Income Taxes}

The statutory federal income tax rate is reconciled to the Company's effective income tax rate on a continuing operations basis below:

Nondeductible Expenses
Credit for Synthetic Fuel Investments
Credit for Low-Income Housing Investments
Tax-Exempt Income From Municipal Securities
Other Tax-Exempt Income
Foreign Operations
Other - Net
Effective Rate
\begin{tabular}{cc}
0.2 & 0.3 \\
\((1.2)\) & \((2.0)\) \\
\((1.7)\) & \((2.3)\) \\
\((0.1)\) & \((0.2)\) \\
\((1.2)\) & \((1.3)\) \\
\((0.7)\) & 0.2 \\
1.1 & \((0.9)\) \\
\(-=-=--\) & \(-=-=-\) \\
\(33.3 \%\) & \(32.1 \%\) \\
\(======\) & \(=====\)
\end{tabular}

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11. Derivatives and Hedging Relationships

Derivative contracts, such as futures contracts, forwards, interest rate swaps, foreign currency swaps and options and similar products used in trading activities, are recorded at fair value. The Company does not recognize gains or losses at the inception of derivative transactions if the fair value is not determined based upon observable market transactions and market data. Gains and losses are included in foreign exchange and other trading activities in non-interest income. Unrealized gains and losses are reported on a gross basis in trading account assets and trading liabilities, after taking into consideration master netting agreements.

The Company enters into various derivative financial instruments for nontrading purposes primarily as part of its asset/liability management ("ALM") process. These derivatives are designated as fair value and cash flow hedges of certain assets and liabilities when the Company enters into the derivative contracts. Gains and losses associated with fair value hedges are recorded in income as well as any change in the value of the related hedged item. Gains and losses on cash flow hedges are recorded in other comprehensive income. If a derivative used in ALM does not qualify as a hedge it is marked to market and the gain or loss is included in net interest income.

The Company formally documents all relationships between hedging instruments and hedged items, as well as its risk-management objectives and strategy for undertaking various hedge transactions. This process includes linking all derivatives that are designated as fair value hedges to specific assets or liabilities on the balance sheet.

The Company formally assesses both at the hedge's inception and on an ongoing basis whether the derivatives that are used in hedging transactions are highly effective and whether those derivatives are expected to remain highly effective in future periods. The Company evaluates ineffectiveness in terms of amounts that could impact a hedge's ability to qualify for hedge accounting and the risk that the hedge could result in more than a de minimus amount of ineffectiveness. At inception, the potential causes of ineffectiveness related to each of its hedges is assessed to determine if the Company can expect the hedge to be highly effective over the life of the transaction and to determine the method for evaluating effectiveness on an ongoing basis. Recognizing that changes in the value of derivatives used for hedging or the value of hedged items could result in significant ineffectiveness, the Company has processes in place designed to identify and evaluate such changes when they occur. Quarterly, the Company performs a quantitative effectiveness assessment and records any ineffectiveness.

The Company utilizes interest rate swap agreements to manage its exposure to interest rate fluctuations. For hedges of fixed rate loans, asset-backed securities, deposits and long term debt, the hedge documentation specifies the terms of the hedged items and interest rate swaps and indicates that the derivative is hedging a fixed rate item and is a fair value hedge, that the
hedge exposure is to the changes in the fair value of the hedged item due to changes in benchmark interest rates, and that the strategy is to eliminate fair value variability by converting fixed rate interest payments to LIBOR.

The fixed rate loans hedged generally have a maturity of 1 to 10 years and are not callable. These loans are hedged with "pay fixed rate, receive variable rate" swaps with similar notional amounts, maturities, and fixed rate coupons. The swaps are not callable. At June 30, 2006 , \(\$ 163 \mathrm{million}\) of loans were hedged with interest rate swaps which had notional values of \(\$ 163\) million.

The securities hedged generally have a weighted average life of 10 years and are callable six months prior to maturity. These securities are hedged with pay fixed rate, receive variable rate swaps of like maturity, repricing and fixed rate coupon. The swaps are callable six months prior to maturity. At June 30,2006 , \(\$ 231\) million of securities were hedged with interest rate swaps which had notional values of \(\$ 231\) million.

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The fixed rate deposits hedged generally have original maturities of 1 to 12 years (65\% are one year deposits) and, except for three deposits, are not callable. These deposits are hedged with receive fixed rate, pay variable rate swaps of similar maturity, repricing and fixed rate coupon. The swaps are not callable except for the three that hedge the callable deposits. At June 30 , 2006, \(\$ 2,018\) million of deposits were hedged with interest rate swaps which had notional values of \(\$ 2,018\) million.

The fixed rate long-term debt hedged generally has an original maturity of 5 to 30 years. The company issues both callable and non-callable debt. The non-callable debt is hedged with simple interest rate swaps similar to those described for deposits. Callable debt is hedged with callable swaps where the call dates of the swaps exactly match the call dates of the debt. At June 30 , 2006, \(\$ 5,566\) million of debt was hedged with interest rate swaps which had notional values of \(\$ 5,587\) million.

In addition to the fair value hedges discussed above, the Company has three cash flow hedges utilizing interest rate swaps to hedge the variability in expected future cash flows attributable to floating rates on an interestonly strip, a deposit and a long-term debt issue. The hedge documentation specifies the terms of the hedged items and interest rate swaps and indicates that the derivative is hedging future variable interest payments and is a cash flow hedge, that the hedge exposure is the variability in interest payments, and that the strategy is to eliminate variability by converting floating rate interest payments to fixed payments. For cash flow hedges the interest rate swap is marked to market with the changes in value recorded in other comprehensive income. The amount recognized as other comprehensive income for the cash flow hedge is reclassified to net interest income as interest is realized on the hedged item.

The Company has a \(\$ 273\) million interest-only strip of which \(\$ 200\) million is hedged with a \(\$ 200\) million receive fixed rate, pay variable rate interest rate swaps to remove the variability in the cash flows received from the security. Payments on the interest-only strip are related to a money market fund. During the next twelve months, net gains of \(\$ 3\) million (pre-tax) included in other comprehensive income are expected to be reclassified to income.

The deposit hedged has a principal amount of \(\$ 275\) million and has a LIBOR based floating rate and an 18 month maturity. The deposit is hedged with a receive LIBOR, pay fixed rate swap with the same maturity and interest payment dates as the deposit to eliminate the variability in interest payment received on the deposit. During the next twelve months, net gains of less than \(\$ 1\) million (pre-tax) included in other comprehensive income are expected to be
reclassified to income.

The long term debt hedged has a principal amount of \(\$ 400\) million and has a LIBOR based floating rate and a 2 year maturity. The debt is hedged with a receive LIBOR, pay fixed rate swap with the same maturity and interest payment dates as the debt to eliminate the variability in interest payment received on the debt. During the next twelve months, net gains of less than \(\$ 1\) million (pre-tax) included in other comprehensive income are expected to be reclassified to income.

In addition, the Company enters into foreign exchange hedges. The Company uses forward foreign exchange contracts with maturities of 12 months or less to hedge its Sterling and Euro foreign exchange exposure with respect to forecasted expense transactions in non-U.S. entities which have the US dollar as their functional currency. As of June 30, 2006, the hedged forecasted foreign currency transactions and linked forwards were \(\$ 83\) million with \(\$ 3\) million gains recorded in other comprehensive income. These gains are expected to be reclassified to expense over the next twelve months.

Forward foreign exchange contracts are also used to hedge the value of the Company's investments in foreign subsidiaries. These forward contracts have a maturity of less than six months. The derivatives employed are designated as net investment hedges of changes in value of the Company's foreign investment due to exchange rates, such that changes in value of the forward exchange

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contracts offset the changes in value of the foreign investments due to changes in foreign exchange rates. The change in fair market value of these contracts is deferred and reported within accumulated translation adjustments in shareholders' equity, net of tax effects. At June 30, 2006, foreign exchange contracts, with notional amounts totaling \(\$ 1,658\) million, were designated as hedges of corresponding amounts of net investments.

The Company discontinues hedge accounting prospectively when it determines that a derivative is no longer an effective hedge, the derivative expires or is sold, or management discontinues the derivative's hedge designation.

Ineffectiveness related to derivatives and hedging relationships was recorded in income as follows:
\begin{tabular}{|c|c|c|c|c|}
\hline (In millions) & \multicolumn{2}{|r|}{\multirow[t]{2}{*}{Quarter End June 30, 2006}} & \multicolumn{2}{|r|}{Year-to-date} \\
\hline Hedges & & & & 006 \\
\hline Fair Value Hedge of Loans & \$ & (0.1) & \$ & 0.1 \\
\hline Fair Value Hedge of Securities & & (0.1) & & (0.1) \\
\hline Fair Value Hedge of Deposits and Long-Term Debt & & (1.2) & & (0.7) \\
\hline Cash Flow Hedges & & (0.2) & & (0.4) \\
\hline Other & & 0.2 & & (0.1) \\
\hline Total & \$ & (1.4) & \$ & (1.2) \\
\hline
\end{tabular}

Other includes ineffectiveness recorded on foreign exchange hedges.
12. Commitments and Contingent Liabilities

In the normal course of business, various commitments and contingent
liabilities are outstanding which are not reflected in the accompanying consolidated balance sheets. Management does not expect any material losses to result from these matters.

The Company's significant trading and off-balance-sheet risks are securities, foreign currency and interest rate risk management products, commercial lending commitments, letters of credit, and securities lending indemnifications. The Company assumes these risks to reduce interest rate and foreign currency risks, to provide customers with the ability to meet credit and liquidity needs, to hedge foreign currency and interest rate risks, and to trade for its own account. These items involve, to varying degrees, credit, foreign exchange, and interest rate risk not recognized in the balance sheet. The Company's off-balance-sheet risks are managed and monitored in manners similar to those used for on-balance-sheet risks. There are no significant industry concentrations of such risks.

A summary of the notional amount of the Company's off-balance-sheet credit transactions, net of participations, at June 30, 2006 and December 31, 2005 for continuing operations follows:

Off-Balance-Sheet Credit Risks
\begin{tabular}{|c|c|c|c|c|}
\hline (In millions) & & \[
\begin{array}{r}
\text { June } 30 \\
2006
\end{array}
\] & \multicolumn{2}{|l|}{\[
\begin{array}{r}
\text { December } 31, \\
2005
\end{array}
\]} \\
\hline Lending Commitments & \$ & 34,730 & \$ & 33,407 \\
\hline Standby Letters of Credit & & 10,603 & & 9,873 \\
\hline Commercial Letters of Credit & & 1,002 & & 1,122 \\
\hline Securities Lending Indemnifications & & 379,563 & & 310,970 \\
\hline
\end{tabular}

The total potential loss on undrawn commitments, standby and commercial letters of credit, and securities lending indemnifications is equal to the total notional amount if drawn upon, which does not consider the value of any

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collateral. Since many of the commitments are expected to expire without being drawn upon, the total amount does not necessarily represent future cash requirements. The allowance for lending-related commitments at June 30, 2006 and December 31, 2005 was \(\$ 143\) million and \(\$ 144\) million.

A securities lending transaction is a fully collateralized transaction in which the owner of a security agrees to lend the security through an agent (the Company) to a borrower, usually a broker/dealer or bank, on an open, overnight or term basis, under the terms of a prearranged contract, which generally matures in less than 90 days. The Company generally lends securities with indemnification against broker default. The Company generally requires the borrower to provide \(102 \%\) cash collateral which is monitored on a daily basis, thus reducing credit risk. Security lending transactions are generally entered into only with highly-rated counterparties. At June 30, 2006 and December 31, 2005, securities lending indemnifications were secured by collateral of \(\$ 389.9\) billion and \(\$ 317.4\) billion, respectively.

Standby letters of credit principally support corporate obligations and include \(\$ 0.1\) billion that were collateralized with cash and securities on June 30, 2006 and \(\$ 0.6\) billion on December 31, 2005. At June 30, 2006, approximately \(\$ 7.1\) billion of the standbys will expire within one year, and the balance between one to five years.

The notional amounts for other off-balance-sheet risks (See "Trading

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Activities" in the MD\&A section) express the dollar volume of the transactions; however, credit risk is much smaller. The Company performs credit reviews and enters into netting agreements to minimize the credit risk of foreign currency and interest rate risk management products. The Company enters into offsetting positions to reduce exposure to foreign exchange and interest rate risk.

Other

\begin{abstract}
The Company has provided standard representations for underwriting agreements, acquisition and divestiture agreements, sales of loans and commitments, and other similar types of arrangements and customary indemnification for claims and legal proceedings related to its provision of financial services. Insurance has been purchased to mitigate certain of these risks. The Company is a minority equity investor in, and member of, several industry clearing or settlement exchanges through which foreign exchange, securities, or other transactions settle. Certain of these industry clearing or settlement exchanges require their members to guarantee their obligations and liabilities or to provide financial support in the event other partners do not honor their obligations. It is not possible to estimate a maximum potential amount of payments that could be required with such agreements.
\end{abstract}

In the ordinary course of business, the Company makes certain investments that have tax consequences. From time to time, the IRS may question or challenge the tax position taken by the Company. The Company engaged in certain types of structured cross-border leveraged leasing investments, referred to as "LILOs", prior to mid-1999 that the IRS has challenged. In 2004, the IRS proposed adjustments to the Company's tax treatment of these transactions. As previously disclosed, beginning in the fourth quarter of 2004, the Company had several appellate conferences with the IRS in an attempt to settle the proposed adjustments related to these LILO transactions.

On February 28, 2006, the Company settled this matter with the IRS relating to LILO transactions closed in 1996 and 1997 . The settlement does not affect 2006 net income, as the impact of the settlement was fully reserved.

The Company's 1998 leveraged lease transactions are in a subsequent audit cycle and were not part of the settlement. The Company believes that a comparable settlement for 1998 will ultimately be possible, given the similarity between these leases and the settled leases. However, negotiations are not complete and the treatment of the 1998 leases may still be litigated. Under current generally accepted accounting principles, if the 1998 leases are settled on a basis comparable to the 1996 and 1997 leases, the Company would

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not expect the settlement of the 1998 leases to have an impact on net income, based on existing reserves.

In the fourth quarter of 2005 the Company deposited funds with the IRS in anticipation of reaching a settlement on all of its LILO investments.

On February 11, 2005, the IRS released Notice 2005-13, which identified certain lease investments known as "SILOs" as potentially subject to IRS challenge. The Company believes that certain of its lease investments entered into prior to 2004 may be consistent with transactions described in the notice. In response, the Company is reviewing its lease portfolio and evaluating the technical merits of the IRS' position. Although it is likely the IRS will challenge the tax benefits associated with these leases, the company remains confident that its tax treatment of the leases complied with statutory,
administrative and judicial authority existing at the time they were entered into.

The Company currently believes it has adequate tax reserves to cover its LILO exposure and any other potential tax exposures, based on a probability assessment of various potential outcomes. Probabilities and outcomes are reviewed as events unfold, and adjustments to the reserves are made when appropriate.

In the ordinary course of business, the Company and its subsidiaries are routinely defendants in or parties to a number of pending and potential legal actions, including actions brought on behalf of various classes of claimants, and regulatory matters. Claims for significant monetary damages are asserted in certain of these actions and proceedings. Due to the inherent difficulty of predicting the outcome of such matters, the company cannot ascertain what the eventual outcome of these matters will be; however, based on current knowledge and after consultation with legal counsel, the Company does not believe that judgments or settlements, if any, arising from pending or potential legal actions or regulatory matters, either individually or in the aggregate, after giving effect to applicable reserves, will have a material adverse effect on the consolidated financial position or liquidity of the Company although they could have a material effect on net income for a given period. The Company intends to defend itself vigorously against all of the claims asserted in these legal actions.

See discussion of contingent legal matters in the "Legal and Regulatory Proceedings" section.

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QUARTERLY REPORT ON FORM 10-Q THE BANK OF NEW YORK COMPANY, INC.

\author{
UNITED STATES \\ SECURITIES AND EXCHANGE COMMISSION WASHINGTON, D.C. 20549
}

Quarterly Report pursuant to Section 13 or \(15(\mathrm{~d})\) of the Securities Exchange Act of 1934 for the quarterly period ended June 30, 2006

Commission file number 001-06152

THE BANK OF NEW YORK COMPANY, INC.
Incorporated in the State of New York
I.R.S. Employer Identification No. 13-2614959

Address: One Wall Street
New York, New York 10286
Telephone: (212) 495-1784
As of July 31, 2006, The Bank of New York Company, Inc. had \(763,130,829\) shares of common stock (\$7.50 par value) outstanding.

The Bank of New York Company, Inc. (1) has filed all reports required to be filed by Section 13 or \(15(d)\) of the Securities Exchange Act of 1934 during the preceding 12 months (or such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

The registrant is a large accelerated filer (as defined in Rule \(12 b-2\) of the

Exchange Act).
The registrant is not a shell company (as defined in Rule \(12 \mathrm{~b}-2\) of the Exchange Act).

The following sections of the Financial Review set forth in the crossreference index are incorporated in the Quarterly Report on Form 10-Q.

\section*{Cross-reference}

Page (s)

PART I FINANCIAL INFORMATION

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Consolidated Balance Sheets as of June 30, 2006 and December 31, 2005

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ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Company's Disclosure Committee, whose members include the Chief Executive Officer and Chief Financial Officer, has responsibility for ensuring that there is an adequate and effective process for establishing, maintaining, and evaluating disclosure controls and procedures that are designed to ensure that information required to be disclosed by the Company in its SEC reports is timely recorded, processed, summarized and reported. In addition, the Company has established a Code of Conduct designed to provide a statement of the values and ethical standards to which the Company requires its employees and directors to adhere. The Code of Conduct provides the framework for maintaining the highest possible standards of professional conduct. The Company also maintains an ethics hotline for employees.

As of the end of the period covered by this report, an evaluation was carried out under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures as defined in Exchange Act Rule 13a-15(e) and 15d-15(e). Based on that evaluation,
the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective.

Changes in Internal Control Over Financial Reporting
In the ordinary course of business, the Company may routinely modify, upgrade and enhance its internal controls and procedures for financial reporting. However, there have not been any changes in the Company's internal controls over financial reporting as defined in Exchange Act Rule 13a-15(f) and 15d-15(f) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL AND REGULATORY PROCEEDINGS

In the ordinary course of business, the Company and its subsidiaries are routinely defendants in or parties to a number of pending and potential legal actions, including actions brought on behalf of various classes of claimants, and regulatory matters. Claims for significant monetary damages are asserted in certain of these actions and proceedings. In regulatory enforcement matters, claims for disgorgement and the imposition of penalties and/or other remedial sanctions are possible. Due to the inherent difficulty of predicting the outcome of such matters, the Company cannot ascertain what the eventual outcome of these matters will be; however, on the basis of current knowledge and after consultation with legal counsel, the Company does not believe that judgments or settlements, if any, arising from pending or potential legal actions or regulatory matters, either individually or in the aggregate, after giving effect to applicable reserves, will have a material adverse effect on the consolidated financial position or liquidity of the Company, although they could have a material effect on net income for a given period. The Company intends to defend itself vigorously against all of the claims asserted in these legal actions.

As previously disclosed in the Company's 2005 Annual Report on Form 10-K, the U.S. Securities and Exchange Commission ("SEC") is investigating 1) the appropriateness of certain expenditures made in connection with marketing and distribution of the Hamilton Funds; 2) possible market-timing transactions cleared by Pershing LLC ("Pershing"); and 3) the trading activities of Pershing Trading Company LP, a floor specialist, on two regional exchanges from 1999 to 2004.

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Because the conduct at issue in the Pershing market timing and floor specialist investigations is alleged to have occurred largely during the period when Pershing was owned by Credit Suisse First Boston (USA), Inc. ("CSFB"), the Company has made claims for indemnification against CSFB relating to these matters under the agreement relating to the acquisition of Pershing. CSFB is disputing these claims for indemnification.

As previously disclosed, the SEC has been investigating the Company's role as auction agent in connection with certain auction rate securities. The Company has entered into settlement negotiations with the SEC staff concerning the auction agent investigation. There can be no assurance that a settlement will be reached.

As disclosed in a report filed on Form 8-K, the Company entered into a written agreement with the Federal Reserve Bank of New York and the New York

State Banking Department on April 21, 2006. The agreement outlines a series of steps to strengthen and enhance the Bank's compliance practices, systems, controls, and procedures.

ITEM 1A. RISK FACTORS

\begin{abstract}
See "Forward-Looking Statements and Risk Factors That Could Affect Future Results" in "Management's Discussion and Analysis of Financial Condition and Results of Operations." There have been no material changes to the risk factors discussed in the Company's Annual Report on Form 10-K for the year ended December 31, 2005 and the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2006.
\end{abstract}

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ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES

\section*{AND USE OF PROCEEDS}

Shares of the Company's common stock were issued in the following transactions exempt from registration under the Securities Act of 1933 pursuant to Section 4(2) thereof:
(a) Shares of common stock were issued to former directors who had deferred receipt of such common stock pursuant to the Deferred Compensation Plan for Non-Employee Directors of The Bank of New York Company, Inc. These issuances amounted to 15,705 shares on June 15, 2006.

Under its stock repurchase program, the Company buys back shares from time to time. The following table discloses the Company's repurchases of the Company's common stock made during the second quarter of 2006.

Issuer Purchases of Equity Securities
\begin{tabular}{lcccc} 
& & & & Total Number
\end{tabular}

Shares were repurchased through the Company's stock repurchase programs announced on July 12, 2005 , which permits the repurchase of 20 million shares. Ten million shares were repurchased in April at an initial price of \(\$ 35.85\) from a broker-dealer counterparty who borrowed the shares, as part of an accelerated share repurchase program. The initial price is subject to a purchase price adjustment based on the price the counterparty actually pays for the shares. The remaining shares repurchased were from employee benefit plans.

\section*{ITEM 4. SUBMISSION OF MATTERS TO VOTE OF SECURITY HOLDERS}

The Company held its annual meeting on April 11, 2006 at The Bank of New York at 101 Barclay St. in New York, New York. The shareholders:
(1) elected fourteen persons to serve as directors of the Company;
(2) ratified the appointment of Ernst \& Young LLP as the Company's independent public accountants for 2006;
(3) approved a shareholder proposal with respect to cumulative voting;
(4) defeated a shareholder proposal with respect to reimbursement of expenses of opposition candidates for the Board of Directors.

The number of votes cast for, against or withheld, and the number of abstentions with respect to each such matter is set forth below, as are the number of broker non-votes, where applicable. Pursuant to New York law, abstentions and broker non-votes are not counted toward the election of directors.
\begin{tabular}{llc} 
& AGAINST/ & \\
FOR & WITHHELD & \\
& ABSTAINED & NON-VOTES
\end{tabular}
(1) Election of Directors:

Frank J. Biondi, Jr. Nicholas M. Donofrio
Gerald L. Hassell Richard J. Kogan Michael J. Kowalski
John A. Luke, Jr.
John C. Malone
Paul Myners
Catherine A. Rein
Thomas A. Renyi
William C. Richardson Brian L. Roberts Samuel C. Scott III Richard C. Vaughan
(2) Ratification of Auditors
(3) Approval of Shareholder Proposal With Respect to Cumulative Voting 293,349,783 280,461,065 26,258,595 101,238,256
(4) Defeat of Shareholder Proposal With Respect to Reimbursement of Expenses of Opposition Candidates for the Board 25,161,012 554,572,946 20,335,485 95,315,146

ITEM 6. EXHIBITS
\begin{tabular}{|c|c|}
\hline 3. & The By-Laws of The Bank of New York Company, Inc. as amended through April 12, 2005, incorporated by reference to Exhibit 3 (ii) to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2005. \\
\hline 3.2 & Restated Certificate of Incorporation of The Bank of New York Company, Inc. dated May 8, 2001, incorporated by reference to Exhibit 4 to the Company's Registration Statement on Form S-3 filed June 7, 2001 (File No. 333-62516, 333-62516-01, 333-62516-02, 333-62516-03 and 333-62516-04). \\
\hline 4 & None of the outstanding instruments defining the rights of holders of long-term debt of the Company represent long-term debt in excess of \(10 \%\) of the total assets of the Company. The Company hereby agrees to furnish to the Commission, upon request, a copy of any of such instrument. \\
\hline 10.1 & Letter Agreement with Releases, dated June 30, 2006, between The Bank of New York Company, Inc. and Joseph M. Velli, incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K as filed with the Commission on June 30, 2006. \\
\hline 10.2 & Employee Severance Agreement, dated July 11, 2000, between The Bank of New York Company, Inc. and Joseph M. Velli, incorporated by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K as filed with the Commission on June 30, 2006. \\
\hline 10.3 & Form of Stock Option Agreement under the Registrant's 2003 Long-Term Incentive Plan. \\
\hline 10.4 & Form of Performance Share Agreement under the Registrant's 2003 Long-Term Incentive Plan. \\
\hline 10.5 & Form of Restricted Stock Agreement under the Registrant's 2003 Long-Term Incentive Plan. \\
\hline 12 & Ratio of Earnings to Fixed Charges for the Three Months and Six Months Ended June 30, 2006 and 2005. \\
\hline 31 & Certification of Chairman and Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. \\
\hline 31.1 & Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. \\
\hline 32 & Certification of Chairman and Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. \\
\hline 32.1 & Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. \\
\hline
\end{tabular}

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934 , the

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}
registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

THE BANK OF NEW YORK COMPANY, INC.
(Registrant)
\begin{tabular}{|c|c|}
\hline \multirow[t]{3}{*}{Date: A
\[
99
\]} & 2006 \\
\hline & \\
\hline & \\
\hline \multicolumn{2}{|c|}{EXHIBIT INDEX} \\
\hline Exhibit & Description \\
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& \text { Form } \\
& 2003
\end{aligned}
\] \\
\hline 10.5 & Form \\
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32.1

2003 Long-Term Incentive Plan.
Ratio of Earnings to Fixed Charges for the Three Months and Six Months Ended June 30, 2006 and 2005.

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