

PNC FINANCIAL SERVICES GROUP, INC.

Form 10-Q

August 08, 2013

[Table of Contents](#)

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2013

or

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

For the transition period from to

Commission file number 001-09718

The PNC Financial Services Group, Inc.

(Exact name of registrant as specified in its charter)

Edgar Filing: PNC FINANCIAL SERVICES GROUP, INC. - Form 10-Q

Pennsylvania
(State or other jurisdiction of

25-1435979
(I.R.S. Employer

incorporation or organization)

Identification No.)

One PNC Plaza, 249 Fifth Avenue, Pittsburgh, Pennsylvania 15222-2707

(Address of principal executive offices, including zip code)

(412) 762-2000

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company

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

As of July 31, 2013, there were 531,511,981 shares of the registrant's common stock (\$5 par value) outstanding.

Table of Contents

THE PNC FINANCIAL SERVICES GROUP, INC.

Cross-Reference Index to Second Quarter 2013 Form 10-Q

	Pages
PART I FINANCIAL INFORMATION	
Item 1. Financial Statements (Unaudited).	
<u>Consolidated Income Statement</u>	76
<u>Consolidated Statement of Comprehensive Income</u>	77
<u>Consolidated Balance Sheet</u>	78
<u>Consolidated Statement Of Cash Flows</u>	79
<u>Notes To Consolidated Financial Statements (Unaudited)</u>	
<u>Note 1 Accounting Policies</u>	81
<u>Note 2 Acquisition and Divestiture Activity</u>	85
<u>Note 3 Loan Sale and Servicing Activities and Variable Interest Entities</u>	86
<u>Note 4 Loans and Commitments to Extend Credit</u>	92
<u>Note 5 Asset Quality</u>	92
<u>Note 6 Purchased Loans</u>	108
<u>Note 7 Allowances for Loan and Lease Losses and Unfunded Loan Commitments and Letters of Credit</u>	109
<u>Note 8 Investment Securities</u>	112
<u>Note 9 Fair Value</u>	118
<u>Note 10 Goodwill and Other Intangible Assets</u>	130
<u>Note 11 Capital Securities of Subsidiary Trusts and Perpetual Trust Securities</u>	133
<u>Note 12 Certain Employee Benefit And Stock Based Compensation Plans</u>	134
<u>Note 13 Financial Derivatives</u>	136
<u>Note 14 Earnings Per Share</u>	145
<u>Note 15 Total Equity And Other Comprehensive Income</u>	146
<u>Note 16 Income Taxes</u>	151
<u>Note 17 Legal Proceedings</u>	151
<u>Note 18 Commitments and Guarantees</u>	154
<u>Note 19 Segment Reporting</u>	158
<u>Note 20 Subsequent Events</u>	161
<u>Statistical Information (Unaudited)</u>	
<u>Average Consolidated Balance Sheet And Net Interest Analysis</u>	162
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations.</u>	
<u>Financial Review</u>	
<u>Consolidated Financial Highlights</u>	1
<u>Executive Summary</u>	3
<u>Consolidated Income Statement Review</u>	11
<u>Consolidated Balance Sheet Review</u>	14
<u>Off-Balance Sheet Arrangements And Variable Interest Entities</u>	27
<u>Fair Value Measurements</u>	27
<u>European Exposure</u>	28
<u>Business Segments Review</u>	30
<u>Critical Accounting Estimates And Judgments</u>	42
<u>Status Of Qualified Defined Benefit Pension Plan</u>	44
<u>Recourse And Repurchase Obligations</u>	44
<u>Risk Management</u>	48
<u>Internal Controls And Disclosure Controls And Procedures</u>	69
<u>Glossary Of Terms</u>	70
<u>Cautionary Statement Regarding Forward-Looking Information</u>	74
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk.</u>	48-69, 118-130 and 136-144
Item 4. <u>Controls and Procedures.</u>	69

PART II OTHER INFORMATION

<u>Item 1. Legal Proceedings.</u>	164
<u>Item 1A. RiskFactors.</u>	164
<u>Item 2. Unregistered Sales Of Equity Securities And Use Of Proceeds.</u>	164
<u>Item 6. Exhibits.</u>	165
<u>Exhibit Index.</u>	165
<u>Signature</u>	165
<u>Corporate Information</u>	166

Table of Contents

THE PNC FINANCIAL SERVICES GROUP, INC.

Cross-Reference Index to Second Quarter 2013 Form 10-Q (continued)

MD&A TABLE REFERENCE

Table	Description	Page
1	<u>Consolidated Financial Highlights</u>	1
2	<u>Summarized Average Balance Sheet</u>	8
3	<u>Results Of Businesses Summary</u>	9
4	<u>Net Interest Income and Net Interest Margin</u>	11
5	<u>Noninterest Income</u>	12
6	<u>Summarized Balance Sheet Data</u>	14
7	<u>Details Of Loans</u>	14
8	<u>Accretion Purchased Impaired Loans</u>	15
9	<u>Purchased Impaired Loans Accretable Yield</u>	15
10	<u>Valuation of Purchased Impaired Loans</u>	16
11	<u>Weighted Average Life of the Purchased Impaired Portfolios</u>	16
12	<u>Accretable Difference Sensitivity Total Purchased Impaired Loans</u>	17
13	<u>Net Unfunded Credit Commitments</u>	17
14	<u>Investment Securities</u>	18
15	<u>Vintage, Current Credit Rating and FICO Score for Asset-Backed Securities</u>	19
16	<u>Other-Than-Temporary Impairments</u>	20
17	<u>Net Unrealized Gains and Losses on Non-Agency Securities</u>	21
18	<u>Loans Held For Sale</u>	22
19	<u>Details Of Funding Sources</u>	23
20	<u>Shareholders Equity</u>	24
21	<u>Basel I Risk-Based Capital</u>	25
22	<u>Estimated Pro forma Basel III Tier 1 Common Capital Ratio</u>	26
23	<u>Fair Value Measurements Summary</u>	27
24	<u>Summary of European Exposure</u>	28
25	<u>Retail Banking Table</u>	31
26	<u>Corporate & Institutional Banking Table</u>	33
27	<u>Asset Management Group Table</u>	36
28	<u>Residential Mortgage Banking Table</u>	38
29	<u>BlackRock Table</u>	40
30	<u>Non-Strategic Assets Portfolio Table</u>	40
31	<u>Pension Expense Sensitivity Analysis</u>	44
32	<u>Analysis of Quarterly Residential Mortgage Repurchase Claims by Vintage</u>	45
33	<u>Analysis of Quarterly Residential Mortgage Unresolved Asserted Indemnification and Repurchase Claims</u>	46
34	<u>Analysis of Residential Mortgage Indemnification and Repurchase Claim Settlement Activity</u>	46
35	<u>Analysis of Home Equity Unresolved Asserted Indemnification and Repurchase Claims</u>	47
36	<u>Analysis of Home Equity Indemnification and Repurchase Claim Settlement Activity</u>	47
37	<u>Nonperforming Assets By Type</u>	50
38	<u>OREO and Foreclosed Assets</u>	51
39	<u>Change in Nonperforming Assets</u>	51
40	<u>Accruing Loans Past Due 30 To 59 Days</u>	52
41	<u>Accruing Loans Past Due 60 To 89 Days</u>	52
42	<u>Accruing Loans Past Due 90 Days Or More</u>	53
43	<u>Home Equity Lines of Credit Draw Period End Dates</u>	54
44	<u>Consumer Real Estate Related Loan Modifications</u>	55
45	<u>Consumer Real Estate Related Loan Modifications Re-Default by Vintage</u>	56
46	<u>Summary of Troubled Debt Restructurings</u>	57

Edgar Filing: PNC FINANCIAL SERVICES GROUP, INC. - Form 10-Q

47	<u>Loan Charge-Offs And Recoveries</u>	58
48	<u>Allowance for Loan and Lease Losses</u>	59
49	<u>Credit Ratings as of June 30, 2013 for PNC and PNC Bank, N.A.</u>	63
50	<u>Contractual Obligations</u>	64
51	<u>Other Commitments</u>	64
52	<u>Interest Sensitivity Analysis</u>	65
53	<u>Net Interest Income Sensitivity to Alternative Rate Scenarios (Second Quarter 2013)</u>	65
54	<u>Alternate Interest Rate Scenarios: One Year Forward</u>	66
55	<u>Enterprise-Wide Trading-Related Gains/Losses Versus Value-at-Risk</u>	66
56	<u>Trading Revenue</u>	67
57	<u>Equity Investments Summary</u>	67
58	<u>Financial Derivatives Summary</u>	69

Table of Contents

THE PNC FINANCIAL SERVICES GROUP, INC.

Cross-Reference Index to Second Quarter 2013 Form 10-Q (continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS TABLE REFERENCE

Table	Description	Page
59	<u>Certain Financial Information and Cash Flows Associated with Loan Sale and Servicing Activities</u>	87
60	<u>Consolidated VIEs Carrying Value</u>	88
61	<u>Assets and Liabilities of Consolidated VIEs</u>	89
62	<u>Non-Consolidated VIEs</u>	89
63	<u>Loans Outstanding</u>	92
64	<u>Net Unfunded Credit Commitments</u>	92
65	<u>Age Analysis of Past Due Accruing Loans</u>	93
66	<u>Nonperforming Assets</u>	94
67	<u>Commercial Lending Asset Quality Indicators</u>	96
68	<u>Home Equity and Residential Real Estate Balances</u>	97
69	<u>Home Equity and Residential Real Estate Asset Quality Indicators Excluding Purchased Impaired Loans</u>	97
70	<u>Home Equity and Residential Real Estate Asset Quality Indicators Purchased Impaired Loans</u>	99
71	<u>Credit Card and Other Consumer Loan Classes Asset Quality Indicators</u>	101
72	<u>Summary of Troubled Debt Restructurings</u>	102
73	<u>Financial Impact and TDRs by Concession Type</u>	103
74	<u>TDRs which have Subsequently Defaulted</u>	105
75	<u>Impaired Loans</u>	107
76	<u>Purchased Impaired Loans Balances</u>	108
77	<u>Purchased Impaired Loans Accretable Yield</u>	108
78	<u>Rollforward of Allowance for Loan and Lease Losses and Associated Loan Data</u>	110
79	<u>Rollforward of Allowance for Unfunded Loan Commitments and Letters of Credit</u>	111
80	<u>Investment Securities Summary</u>	112
81	<u>Gross Unrealized Loss and Fair Value of Securities Available for Sale</u>	113
82	<u>Credit Impairment Assessment Assumptions Non-Agency Residential Mortgage-Backed and Asset-Backed Securities</u>	114
83	<u>Other-Than-Temporary Impairments</u>	115
84	<u>Rollforward of Cumulative OTTI Credit Losses Recognized in Earnings</u>	115
85	<u>Gains (Losses) on Sales of Securities Available for Sale</u>	116
86	<u>Contractual Maturity of Debt Securities</u>	116
87	<u>Weighted-Average Expected Maturity of Mortgage and Other Asset-Backed Debt Securities</u>	117
88	<u>Fair Value of Securities Pledged and Accepted as Collateral</u>	117
89	<u>Fair Value Measurements Summary</u>	119
90	<u>Reconciliation of Level 3 Assets and Liabilities</u>	120
91	<u>Fair Value Measurement Recurring Quantitative Information</u>	124
92	<u>Fair Value Measurements Nonrecurring</u>	126
93	<u>Fair Value Measurements Nonrecurring Quantitative Information</u>	126
94	<u>Fair Value Option Changes in Fair Value</u>	127
95	<u>Fair Value Option Fair Value and Principal Balances</u>	128
96	<u>Additional Fair Value Information Related to Financial Instruments</u>	129
97	<u>Changes in Goodwill by Business Segment</u>	130
98	<u>Other Intangible Assets</u>	130
99	<u>Amortization Expense on Existing Intangible Assets</u>	131
100	<u>Summary of Changes in Customer-Related Other Intangible Assets</u>	131
101	<u>Commercial Mortgage Servicing Rights</u>	131
102	<u>Residential Mortgage Servicing Rights</u>	131
103	<u>Commercial Mortgage Loan Servicing Rights Key Valuation Assumptions</u>	132

Edgar Filing: PNC FINANCIAL SERVICES GROUP, INC. - Form 10-Q

104	<u>Residential Mortgage Loan Servicing Rights</u> Key Valuation Assumptions	132
105	<u>Fees from Mortgage and Other Loan Servicing</u>	132
106	<u>Net Periodic Pension and Postretirement Benefits Costs</u>	134
107	<u>Option Pricing Assumptions</u>	135
108	<u>Stock Option Rollforward</u>	135

Table of Contents

THE PNC FINANCIAL SERVICES GROUP, INC.

Cross-Reference Index to Second Quarter 2013 Form 10-Q (continued)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS TABLE REFERENCE (continued)

Table	Description	Page
109	<u>Nonvested Incentive/Performance Unit Share Awards and Restricted Stock/Share Unit Awards Rollforward</u>	136
110	<u>Nonvested Cash-Payable Restricted Share Units Rollforward</u>	136
111	<u>Derivatives Total Notional or Contractual Amounts and Fair Values</u>	139
112	<u>Derivative Assets and Liabilities Offsetting</u>	140
113	<u>Derivatives Designated in GAAP Hedge Relationships Fair Value Hedges</u>	142
114	<u>Derivatives Designated in GAAP Hedge Relationships Cash Flow Hedges</u>	142
115	<u>Derivatives Designated in GAAP Hedge Relationships Net Investment Hedges</u>	143
116	<u>Gains (Losses) on Derivatives Not Designated as Hedging Instruments under GAAP</u>	143
117	<u>Credit Default Swaps</u>	144
118	<u>Credit Ratings of Credit Default Swaps</u>	144
119	<u>Referenced/Underlying Assets of Credit Default Swaps</u>	144
120	<u>Risk Participation Agreements Sold</u>	144
121	<u>Internal Credit Ratings of Risk Participation Agreements Sold</u>	144
122	<u>Basic and Diluted Earnings per Common Share</u>	145
123	<u>Rollforward of Total Equity</u>	146
124	<u>Other Comprehensive Income</u>	147
125	<u>Accumulated Other Comprehensive Income (Loss) Components</u>	150
126	<u>Net Operating Loss Carryforwards and Tax Credit Carryforwards</u>	151
127	<u>Net Outstanding Standby Letters of Credit</u>	154
128	<u>Analysis of Commercial Mortgage Recourse Obligations</u>	155
129	<u>Analysis of Indemnification and Repurchase Liability for Asserted Claims and Unasserted Claims</u>	156
130	<u>Reinsurance Agreements Exposure</u>	157
131	<u>Reinsurance Reserves Rollforward</u>	157
132	<u>Resale and Repurchase Agreements Offsetting</u>	158
133	<u>Results Of Businesses</u>	160

Table of Contents**FINANCIAL REVIEW**

THE PNC FINANCIAL SERVICES GROUP, INC.

TABLE 1: CONSOLIDATED FINANCIAL HIGHLIGHTS

Dollars in millions, except per share data	Three months ended		Six months ended	
	June 30		June 30	
Unaudited	2013	2012	2013	2012
Financial Results (a)				
Revenue				
Net interest income	\$ 2,258	\$ 2,526	\$ 4,647	\$ 4,817
Noninterest income	1,806	1,097	3,372	2,538
Total revenue	4,064	3,623	8,019	7,355
Noninterest expense	2,435	2,648	4,830	5,103
Pretax, pre-provision earnings (b)	1,629	975	3,189	2,252
Provision for credit losses	157	256	393	441
Income before income taxes and noncontrolling interests	\$ 1,472	\$ 719	\$ 2,796	\$ 1,811
Net income	\$ 1,123	\$ 546	\$ 2,127	\$ 1,357
Less:				
Net income (loss) attributable to noncontrolling interests	1	(5)	(8)	1
Preferred stock dividends and discount accretion	53	25	128	64
Net income attributable to common shareholders	\$ 1,069	\$ 526	\$ 2,007	\$ 1,292
Diluted earnings per common share	\$ 1.99	\$.98	\$ 3.76	\$ 2.42
Cash dividends declared per common share	\$.44	\$.40	\$.84	\$.75
Performance Ratios				
Net interest margin (c)	3.58%	4.08%	3.69%	3.99%
Noninterest income to total revenue	44	30	42	35
Efficiency	60	73	60	69
Return on:				
Average common shareholders' equity	11.81	6.23	11.25	7.80
Average assets	1.49	.74	1.42	.94

See page 70 for a glossary of certain terms used in this Report.

Certain prior period amounts have been reclassified to conform with the current period presentation, which we believe is more meaningful to readers of our consolidated financial statements.

- The Executive Summary and Consolidated Income Statement Review portions of the Financial Review section of this Report provide information regarding items impacting the comparability of the periods presented.
- We believe that pretax, pre-provision earnings, a non-GAAP measure, is useful as a tool to help evaluate the ability to provide for credit costs through operations.
- Calculated as annualized taxable-equivalent net interest income divided by average earning assets. The interest income earned on certain earning assets is completely or partially exempt from federal income tax. As such, these tax-exempt instruments typically yield lower returns than taxable investments. To provide more meaningful comparisons of net interest margins for all earning assets, we use net interest income on a taxable-equivalent basis in calculating net interest margin by increasing the interest income earned on tax-exempt assets to make it fully equivalent to interest income earned on taxable investments. This adjustment is not permitted under generally accepted accounting principles (GAAP) in the Consolidated Income Statement. The taxable-equivalent adjustments to net interest income for the three months ended June 30, 2013 and June 30, 2012 were \$40 million and \$35 million, respectively. The taxable-equivalent adjustments to net interest income for the six months ended June 30, 2013 and June 30, 2012 were \$80 million and \$66 million, respectively.

The PNC Financial Services Group, Inc. Form 10-Q 1

Table of Contents**TABLE 1: CONSOLIDATED FINANCIAL HIGHLIGHTS (CONTINUED) (a)**

Unaudited	June 30 2013	December 31 2012	June 30 2012
Balance Sheet Data (dollars in millions, except per share data)			
Assets	\$ 304,415	\$ 305,107	\$ 299,575
Loans (b) (c)	189,775	185,856	180,425
Allowance for loan and lease losses (b)	3,772	4,036	4,156
Interest-earning deposits with banks (b)	3,797	3,984	3,995
Investment securities (b)	57,449	61,406	61,937
Loans held for sale (c)	3,814	3,693	3,333
Goodwill and other intangible assets	11,228	10,869	10,962
Equity investments (b) (d)	10,054	10,877	10,617
Other assets (b) (c)	24,297	23,679	24,559
Noninterest-bearing deposits	66,708	69,980	64,476
Interest-bearing deposits	145,571	143,162	142,447
Total deposits	212,279	213,142	206,923
Transaction deposits	175,564	176,705	166,043
Borrowed funds (b) (c)	39,864	40,907	43,689
Shareholders' equity	40,286	39,003	37,005
Common shareholders' equity	36,347	35,413	33,884
Accumulated other comprehensive income	45	834	402
Book value per common share	\$ 68.46	\$ 67.05	\$ 64.00
Common shares outstanding (millions)	531	528	529
Loans to deposits	89%	87%	87%
Client Assets (billions)			
Discretionary assets under management	\$ 117	\$ 112	\$ 109
Nondiscretionary assets under administration	116	112	105
Total assets under administration	233	224	214
Brokerage account assets	39	38	36
Total client assets	\$ 272	\$ 262	\$ 250
Capital Ratios			
Basel I capital ratios			
Tier 1 common	10.1%	9.6%	9.3%
Tier 1 risk-based (e)	12.0	11.6	11.4
Total risk-based (e)	15.2	14.7	14.2
Leverage (e)	10.9	10.4	10.1
Common shareholders' equity to assets	11.9	11.6	11.3
Pro forma Basel III Tier 1 common (f)	8.2%	7.5%	N/A(g)
Asset Quality			
Nonperforming loans to total loans	1.75%	1.75%	1.92%
Nonperforming assets to total loans, OREO and foreclosed assets	1.99	2.04	2.31
Nonperforming assets to total assets	1.24	1.24	1.39
Net charge-offs to average loans (for the three months ended) (annualized) (h)	.44	.67	.71
Allowance for loan and lease losses to total loans	1.99	2.17	2.30
Allowance for loan and lease losses to nonperforming loans (i)	114%	124%	120%
Accruing loans past due 90 days or more	\$ 1,762	\$ 2,351	\$ 2,483

(a) The Executive Summary and Consolidated Balance Sheet Review portions of the Financial Review section of this Report provide information regarding items impacting the comparability of the periods presented.

Edgar Filing: PNC FINANCIAL SERVICES GROUP, INC. - Form 10-Q

- (b) Amounts include consolidated variable interest entities. See Consolidated Balance Sheet in Part I, Item 1 of this Report for additional information.
- (c) Amounts include assets and liabilities for which we have elected the fair value option. See Consolidated Balance Sheet in Part I, Item 1 of this Report for additional information.
- (d) Amounts include our equity interest in BlackRock.
- (e) The minimum