WELLS FARGO & CO/MN
Form 10-Q
August 07, 2009

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2009
Commission file number 001-2979

WELLS FARGO & COMPANY
(Exact name of registrant as specified in its charter)

Delaware	No. 41-0449260
(State of incorporation)	(I.R.S. Employer Identification No.)

420 Montgomery Street, San Francisco, California 94163
(Address of principal executive offices) (Zip Code)
Registrant s telephone number, including area code: 1-866-249-3302

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 þ No o

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes þ No o

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	þ	Accelerated filer o
Non-accelerated filer	o (Do not check if a smaller reporting company)	Smaller reporting company o

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

	Shares Outstanding July 31, 2009
Common stock, $1-2/3 par value	4,671,609,008

FORM 10-Q
CROSS-REFERENCE INDEX

PART I	**Financial Information**	
Item 1.	Financial Statements	Page
	Consolidated Statement of Income	56
	Consolidated Balance Sheet	57
	Consolidated Statement of Changes in Equity and Comprehensive Income	58
	Consolidated Statement of Cash Flows	60
	Notes to Financial Statements	
	1 Summary of Significant Accounting Policies	61
	2 Business Combinations	66
	3 Federal Funds Sold, Securities Purchased under Resale Agreements and Other Short-Term Investments	67
	4 Securities Available for Sale	68
	5 Loans and Allowance for Credit Losses	78
	6 Other Assets	81
	7 Securitizations and Variable Interest Entities	82
	8 Mortgage Banking Activities	94
	9 Intangible Assets	96
	10 Guarantees and Legal Actions	98
	11 Derivatives	101
	12 Fair Values of Assets and Liabilities	109
	13 Preferred Stock	121
	14 Employee Benefits	123
	15 Earnings Per Common Share	124
	16 Operating Segments	125
	17 Condensed Consolidating Financial Statements	128
	18 Regulatory and Agency Capital Requirements	136
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations (Financial Review)	
	Summary Financial Data	2
	Overview	3
	Critical Accounting Policies	15
	Earnings Performance	17
	Balance Sheet Analysis	25
	Off-Balance Sheet Arrangements	28
	Risk Management	31
	Capital Management	49
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	42
Item 4.	Controls and Procedures	55
PART II	**Other Information**	
Item 1.	Legal Proceedings	137

Item 1A.	Risk Factors	137
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	137
Item 4.	Submission of Matters to a Vote of Security Holders	137
Item 6.	Exhibits	139
Signature		139
Exhibit Index		140

EX-4(b)
EX-10(a)
EX-12(a)
EX-12(b)
EX-31(a)
EX-31(b)
EX-32(a)
EX-32(b)
EX-101 INSTANCE DOCUMENT
EX-101 SCHEMA DOCUMENT
EX-101 CALCULATION LINKBASE DOCUMENT
EX-101 LABELS LINKBASE DOCUMENT
EX-101 PRESENTATION LINKBASE DOCUMENT
EX-101 DEFINITION LINKBASE DOCUMENT

Table of Contents

PART I FINANCIAL INFORMATION
FINANCIAL REVIEW
SUMMARY FINANCIAL DATA (1)(2)

($ in millions, except per share amounts)		Quarter ended June 30, 2009	Quarter ended March 31, 2009	Quarter ended June 30, 2008	Six months ended June 30, 2009	Six months ended June 30, 2008
For the Period						
Wells Fargo net income	$	**3,172**	3,045	1,753	**6,217**	3,752
Wells Fargo net income applicable to common stock		**2,575**	2,384	1,753	**4,959**	3,752
Diluted earnings per common share		**0.57**	0.56	0.53	**1.13**	1.13
Profitability ratios (annualized):						
Wells Fargo net income to average assets (ROA)		**1.00%**	0.96	1.19	**0.98**	1.29
Net income to average assets		**1.02**	0.97	1.20	**1.00**	1.30
Wells Fargo net income applicable to common stock to average Wells Fargo common stockholders equity (ROE)		**13.70**	14.49	14.58	**14.07**	15.71
Net income to average total equity		**11.56**	11.97	14.62	**11.76**	15.77
Efficiency ratio (3)		**56.4**	56.2	51.0	**56.3**	51.2
Total revenue	$	**22,507**	21,017	11,460	**43,524**	22,023
Pre-tax pre-provision profit (4)		**9,810**	9,199	5,615	**19,009**	10,736
Dividends declared per common share		**0.05**	0.34	0.31	**0.39**	0.62
Average common shares outstanding		**4,483.1**	4,247.4	3,309.8	**4,365.9**	3,306.1
Diluted average common shares outstanding		**4,501.6**	4,249.3	3,321.4	**4,375.1**	3,319.6
Average loans	$	**833,945**	855,591	391,545	**844,708**	387,732
Average assets		**1,274,926**	1,289,716	594,749	**1,282,280**	584,871
Average core deposits (5)		**765,697**	753,928	318,377	**759,845**	317,827
Average retail core deposits (6)		**596,648**	590,502	230,365	**593,592**	229,315
Net interest margin		**4.30%**	4.16	4.92	**4.23**	4.81
At Period End						
Securities available for sale	$	**206,795**	178,468	91,331	**206,795**	91,331
Loans		**821,614**	843,579	399,237	**821,614**	399,237
Allowance for loan losses		**23,035**	22,281	7,375	**23,035**	7,375
Goodwill		**24,619**	23,825	13,191	**24,619**	13,191
Assets		**1,284,176**	1,285,891	609,074	**1,284,176**	609,074
Core deposits (5)		**761,122**	756,183	310,410	**761,122**	310,410
Wells Fargo stockholders equity		**114,623**	100,295	47,964	**114,623**	47,964
Total equity		**121,382**	107,057	48,265	**121,382**	48,265
Tier 1 capital (7)		**102,721**	88,977	42,471	**102,721**	42,471
Total capital (7)		**144,984**	131,820	57,909	**144,984**	57,909
Capital ratios:						
Wells Fargo common stockholders equity to assets		**6.51%**	5.40	7.87	**6.51**	7.87

Total equity to assets	**9.45**	8.33	7.92	**9.45**	7.92
Average Wells Fargo common stockholders equity to average assets	**5.92**	5.17	8.13	**5.54**	8.21
Average total equity to average assets	**8.85**	8.11	8.18	**8.48**	8.26
Risk-based capital (7)					
Tier 1 capital	**9.80**	8.30	8.24	**9.80**	8.24
Total capital	**13.84**	12.30	11.23	**13.84**	11.23
Tier 1 leverage (7)	**8.32**	7.09	7.35	**8.32**	7.35
Book value per common share	**$ 17.91**	16.28	14.48	**17.91**	14.48
Team members (active, full-time equivalent)	**269,900**	272,800	160,500	**269,900**	160,500
Common stock price:					
High	**$ 28.45**	30.47	32.40	**30.47**	34.56
Low	**13.65**	7.80	23.46	**7.80**	23.46
Period end	**24.26**	14.24	23.75	**24.26**	23.75

(1) Wells Fargo & Company (Wells Fargo) acquired Wachovia Corporation (Wachovia) on December 31, 2008. Because the acquisition was completed on December 31, 2008, Wachovia s results are included in the income statement, average balances and related metrics beginning in 2009. Wachovia s assets and liabilities are included in the consolidated balance sheet beginning on December 31, 2008.

(2) On January 1, 2009, we adopted Statement of Financial Accounting Standards (FAS) No. 160, *Noncontrolling*

Interests in Consolidated Financial Statements an amendment of ARB No. 51 , on a retrospective basis for disclosure and, accordingly, prior period information reflects the adoption. FAS 160 requires that noncontrolling interests be reported as a component of total equity.

(3) The efficiency ratio is noninterest expense divided by total revenue (net interest income and noninterest income).

(4) Pre-tax pre-provision profit (PTPP) is total revenue less noninterest expense. Management believes that PTPP is a useful financial measure because it enables investors and others to assess the Company s ability to generate capital to cover credit losses through a credit cycle. Federal banking regulators used a similar measure, pre-provision net revenue, in connection with the Supervisory Capital

Assessment Program (SCAP) stress test to assess the capital adequacy of certain financial institutions. Under the SCAP guidelines, pre-provision net revenue is PTPP adjusted for certain items.

(5) Core deposits are noninterest-bearing deposits, interest-bearing checking, savings certificates, market rate and other savings, and certain foreign deposits (Eurodollar sweep balances).

(6) Retail core deposits are total core deposits excluding Wholesale Banking core deposits and retail mortgage escrow deposits.

(7) See Note 19 (Regulatory and Agency Capital Requirements) to Financial Statements in this Report for additional information.

This Report on Form 10-Q for the quarter ended June 30, 2009, including the Financial Review and the Financial Statements and related Notes, has forward-looking statements, which may include forecasts of our financial results and condition, expectations for our operations and business, and our assumptions for those forecasts and expectations. Do not unduly rely on forward-looking statements. Actual results might differ materially from our forecasts and expectations due to several factors. Some of these factors are described in the Financial Review and in the Financial Statements and related Notes. For a discussion of other factors, refer to the Risk Factors section in this Report and our Quarterly Report on Form 10-Q for the quarter ended March 31, 2009 (First Quarter 2009 Form 10-Q), and to the Risk Factors and Regulation and Supervision sections of our Annual Report on Form 10-K for the year ended December 31, 2008 (2008 Form 10-K), filed with the Securities and Exchange Commission (SEC) and available on the SEC s website at www.sec.gov.

OVERVIEW

Wells Fargo & Company is a $1.3 trillion diversified financial services company providing banking, insurance, trust and investments, mortgage banking, investment banking, retail banking, brokerage and consumer finance through banking stores, the internet and other distribution channels to individuals, businesses and institutions in all 50 states, the District of Columbia (D.C.) and in other countries. We ranked fourth in assets and second in the market value of our common stock among our peers at June 30, 2009. When we refer to Wells Fargo, the Company, we, our or us this Report, we mean Wells Fargo & Company and Subsidiaries (consolidated). When we refer to the Parent, we mean Wells Fargo & Company. When we refer to legacy Wells Fargo, we mean Wells Fargo excluding Wachovia Corporation (Wachovia).

Our vision is to satisfy all our customers financial needs, help them succeed financially, be recognized as the premier financial services company in our markets and be one of America s great companies. Our primary strategy to achieve this vision is to increase the number of products our customers buy from us and to give them all of the financial products that fulfill their needs. Our cross-sell strategy, diversified business model and the breadth of our geographic reach facilitate growth in both strong and weak economic cycles, as we can grow by expanding the number of products our current customers have with us, gain new customers in our extended markets, and increase market share in many businesses. We continued to earn more of our customers business in 2009 in both our retail and commercial banking businesses and in our equally customer-centric securities brokerage and investment banking businesses.

Wells Fargo net income was a record $3.2 billion in second quarter 2009, with net income applicable to common stock of $2.6 billion. Diluted earnings per common share were $0.57, after a $700 million credit reserve build ($0.10 per common share), a Federal Deposit Insurance Corporation (FDIC) special assessment of $565 million ($0.08 per common share) and merger-related and restructuring expenses of $244 million ($0.03 per common share).

On December 31, 2008, Wells Fargo acquired Wachovia. Because the acquisition was completed at the end of 2008, Wachovia s results are included in the income statement, average balances and related metrics beginning in 2009. Wachovia s assets and liabilities are included, at fair value, in the consolidated balance sheet beginning on December 31, 2008, but not in 2008 averages.

On January 1, 2009, we adopted Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (FAS) No. 160, *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51,* on a retrospective basis for disclosure and, accordingly, prior period information reflects the adoption. FAS 160 requires that noncontrolling interests be reported as a component of total equity. In addition, FAS 160 requires that the consolidated income statement disclose amounts attributable to both Wells Fargo interests and the noncontrolling interests.

Table of Contents

Despite the continuing turmoil in the credit markets, Wells Fargo remains one of the largest providers of credit to the U.S. economy. We have extended more than $471 billion of loans to creditworthy customers since October 2008, including $206 billion in new loan commitments and originations this quarter. The fundamentals of our time-tested business model are as sound as ever. Our cross-sell at legacy Wells Fargo set records for the tenth consecutive year an average of 5.84 Wells Fargo products for retail banking households and an average of 6.4 products for wholesale and commercial customers. One of every four of our legacy Wells Fargo retail banking households has eight or more Wells Fargo products and our average middle-market commercial banking customer has almost eight products. We believe there is potentially significant opportunity for growth as we increase the Wachovia retail bank household cross-sell. For example, while Wachovia has a similar number of retail banking stores and about 10 million retail bank households, Wachovia s retail bank household cross-sell of Wachovia products is currently 4.55 compared with legacy Wells Fargo retail bank cross-sell of Wells Fargo products of 5.84. Business banking household cross-sell offers another potential opportunity for growth, with a cross-sell of 3.69 products at legacy Wells Fargo. Our goal is eight products per customer, which is approximately half of our estimate of potential demand.

We continue to experience strong deposit growth, with average checking and savings deposits up 20% (annualized) from first quarter 2009, which contributed to the improvement in our net interest margin to 4.30% and provided increased funding diversity and stability. In addition to macro-economic factors such as money supply growth and higher consumer savings rates that are driving deposit growth industry-wide, we continue to see strong core deposit growth across all customer segments as we gain new customers, deepen our market penetration and expand relationships with existing customers. Average core deposits were $765.7 billion for second quarter 2009, up from $753.9 billion for first quarter 2009.

We took many actions to further strengthen our balance sheet, including building the allowance for credit losses to $23.5 billion, increasing Tier 1 common equity to $47.1 billion, or 4.49% of risk-weighted assets, and building Tier 1 capital to 9.80% of risk-weighted assets. While the Supervisory Capital Assessment Program (SCAP) will not be completed until after the end of the third quarter, we have already generated $14.2 billion from market and internal sources toward the $13.7 billion capital buffer required by the Federal Reserve. We expect to internally generate additional capital in third quarter 2009. See the Capital Management section in this Report for more information.

We are seeing some signs of moderation in the growth of consumer and small business credit losses, largely due to our efforts over the last two years to modify and restructure loans for our customers, our successful efforts to reduce high risk loan portfolios and the purchase accounting write-downs we have already taken in Wachovia s loan portfolios. The Wachovia integration remains on schedule, with business and revenue synergies already exceeding our expectations. We are on track to realize annual run-rate savings of $5 billion upon completion of the Wachovia integration. We further expect additional efficiency initiatives to lower expenses over the rest of 2009.

We have stated in the past that to consistently grow over the long term, successful companies must invest in their core businesses and maintain strong balance sheets. In second quarter 2009, we opened 12 banking stores throughout the combined company for a retail network total of 6,668 stores. Conversion of Wachovia stores to the Wells Fargo platform is scheduled to begin later this year.

We believe it is important to maintain a well-controlled environment as we integrate the Wachovia businesses and grow the combined company. We manage our credit risk by setting what we believe are sound credit policies for underwriting new business, while monitoring and reviewing the performance of our loan portfolio. We manage the interest rate and market risks inherent in our asset and liability balances within prudent ranges, while ensuring adequate liquidity and funding. We maintain strong capital levels to facilitate future growth.

Wachovia Merger

On December 31, 2008, Wells Fargo acquired Wachovia, one of the nation s largest diversified financial services companies. Wachovia s assets and liabilities were included in the December 31, 2008, consolidated balance sheet at their respective fair values on the acquisition date. Because the acquisition was completed on December 31, 2008, Wachovia s results of operations were not included in our 2008 income statement. Beginning in 2009, our consolidated results and associated metrics, as well as our consolidated average balances, include Wachovia. The Wachovia acquisition was material to us, and the inclusion of results from Wachovia s businesses in our 2009 financial statements is a material factor in the changes in our results compared with prior year periods.

Because the transaction closed on the last day of the annual reporting period, certain fair value purchase accounting adjustments were based on preliminary data as of an interim period with estimates through year end. We have validated and, where necessary, refined our December 31, 2008, fair value estimates and other purchase accounting adjustments. The impact of these refinements was recorded as an adjustment to goodwill in the first half of 2009. Based on the purchase price of $23.1 billion and the $12.4 billion fair value of net assets acquired, inclusive of refinements identified in the first half of 2009, the transaction resulted in goodwill of $10.7 billion.

The more significant fair value adjustments in our purchase accounting for the Wachovia acquisition were to loans. As of December 31, 2008, certain of the loans acquired from Wachovia had evidence of credit deterioration since origination, and it was probable that we would not collect all contractually required principal and interest payments. Such loans identified at the time of the acquisition are accounted for under American Institute of Certified Public Accountants (AICPA) Statement of Position 03-3, *Accounting for Certain Loans or Debt Securities Acquired in a Transfer* (SOP 03-3). SOP 03-3 requires that acquired credit-impaired loans be recorded at fair value and prohibits carryover of the related allowance for loan losses.

Loans subject to SOP 03-3 were written down to an amount estimated to be collectible. Accordingly, such loans are not classified as nonaccrual, even though they may be contractually past due, because we expect to fully collect the new carrying values of such loans (that is, the new cost basis arising out of our purchase accounting). Loans subject to SOP 03-3 are also not included in the disclosure of loans 90 days or more past due and still accruing interest even though certain of them are 90 days or more contractually past due.

As a result of the application of SOP 03-3 accounting to Wachovia s loan portfolios, certain credit-related ratios of the Company, including, for example, the growth rate in nonperforming assets since December 31, 2008, may not necessarily be directly comparable with periods prior to the merger or with credit-related ratios of other financial institutions. As noted above, SOP 03-3 loans were reclassified to accrual status in purchase accounting, and one effect of the elimination of nonaccrual loans is that, as certain non-SOP 03-3 loans begin to migrate to nonaccrual status, the percentage increase in nonaccrual loans can be higher because there are minimal loans transferring out of nonaccrual status. For further detail on the merger see the Loan Portfolio section and Note 2 (Business Combinations) to Financial Statements in this Report.

Table of Contents

Summary Results

Wells Fargo net income in second quarter 2009 was $3.2 billion ($0.57 per share), compared with $1.8 billion ($0.53 per share) in second quarter 2008. Net income for the first half of 2009 was $6.2 billion ($1.13 per share), compared with $3.8 billion ($1.13 per share) for the first half of 2008. Wells Fargo return on average total assets (ROA) was 1.00% and return on average common Wells Fargo stockholders equity (ROE) was 13.70% in second quarter 2009, compared with 1.19% and 14.58%, respectively, in second quarter 2008. ROA was 0.98% and ROE was 14.07% for the first half of 2009, and 1.29% and 15.71%, respectively, for the first half of 2008.

Revenue, the sum of net interest income and noninterest income, of $22.5 billion in second quarter 2009 included another quarter of record, double-digit revenue growth at legacy Wells Fargo, up 19% year over year, as well as a strong contribution from Wachovia, which accounted for 39% of combined revenue. Year-to-date revenue was $43.5 billion, almost double legacy Wells Fargo s revenue for the comparable period last year. Our results also reflected growth at legacy Wells Fargo in both net interest income and fee income resulting from our diversified business model. The breadth and depth of our business model resulted in strong and balanced growth in loans, deposits and fee-based products. The vast majority of our more than 80 businesses grew revenue again this quarter, including the following diverse businesses that all achieved greater than 8% (annualized) growth from first quarter 2009: regional banking, mortgage banking, investment banking, asset-based lending, auto lending, student lending, debit card, merchant card, wealth management, securities brokerage, retirement and international.

We believe our balance sheet is well positioned given the current economic environment. Our allowance for credit losses was $23.5 billion at June 30, 2009, compared with $21.7 billion at December 31, 2008. Our allowance covers expected consumer loan losses for approximately the next 12 months and inherent commercial and commercial real estate loan losses expected to emerge over approximately the next 24 months. We continued to reduce the higher risk assets on our balance sheet, with higher-risk loan portfolios (home equity loans originated through third party channels and indirect auto at legacy Wells Fargo, Pick-a-Pay and commercial real estate at Wachovia) down by $6.3 billion and trading assets down by $6.4 billion in the quarter. We recorded $979 million of other-than-temporary impairment (OTTI) on securities in the first half of 2009.

Our financial results included the following:

Net interest income on a taxable-equivalent basis was $11.9 billion in second quarter 2009, up from $6.3 billion in second quarter 2008, reflecting a strong combined net interest margin on average earning assets of $1.1 trillion. Average earning assets were up $1.3 billion in second quarter 2009 from first quarter 2009, with an increase of $30.7 billion in securities and mortgage loans held for sale. This increase was partially offset by a reduction of $3.7 billion in average trading assets and a reduction of $21.6 billion in average loans, including $6.3 billion in the higher-risk loan portfolios that we are exiting. At 4.30% in second quarter 2009, our net interest margin remained strong and the highest among our large bank peers. The net interest margin reflected the benefit of continued growth in core customer deposits, with about 80% of our core deposits now in checking and savings deposits.

Noninterest income reached $10.7 billion in second quarter 2009, up from $5.2 billion a year ago, largely driven by the Wachovia acquisition, as well as continued success in satisfying customers financial needs and the combined company s expanded breadth of products and services. Noninterest income included:

- Mortgage banking noninterest income of $3.0 billion in second quarter 2009:
  - $2.2 billion in revenue from mortgage loan originations/sales activities on $129 billion in new originations, including net write-downs of the mortgage warehouse for spread and other liquidity-related valuation adjustments

Table of Contents

Mortgage applications of $194 billion, one of our highest quarters, with an unclosed application pipeline of $90 billion at quarter end

$1.0 billion mortgage servicing rights (MSRs) mark-to-market gains, net of hedge results, reflecting a $2.3 billion increase in the fair value of the MSRs offset by a $1.3 billion economic hedge loss in the quarter, with the net difference largely due to hedge carry income reflecting low short-term rates, which are likely to continue; MSRs as a percentage of loans serviced of 0.91%

Trust and investment fees of $2.4 billion primarily reflected equity and bond origination fees and higher brokerage commissions as we continued to build our retail securities brokerage business; client assets in Wealth, Brokerage and Retirement were up 8% from first quarter 2009 driven largely by market value appreciation

Card and other fees of $1.9 billion reflected seasonally higher purchase volumes and higher customer penetration rates

Service charges on deposit accounts of $1.4 billion driven by continued strong checking account growth

Trading revenue of $749 million, with approximately two-thirds from customer transactions

Net losses on debt and equity securities totaling $38 million, including $463 million of OTTI write-downs. Net losses on debt securities of $78 million included OTTI of $308 million net of realized gains of $230 million. Net gains on equity securities totaled $40 million after $155 million of OTTI write-downs.

Net unrealized losses on securities available for sale declined to $400 million at June 30, 2009, from $9.9 billion at December 31, 2008. In second quarter 2009, the net unrealized losses were virtually eliminated as credit spreads narrowed during the quarter and as unrealized gains emerged on new mortgage-backed securities (MBS) purchased during the quarter at the peak in MBS yields.

Noninterest expense was $12.7 billion in second quarter 2009, up from $5.8 billion in second quarter 2008, largely attributable to the Wachovia acquisition, as well as the FDIC special assessment of $565 million and higher variable compensation in mortgage, brokerage and investment banking related to increased customer sales. Noninterest expense also reflected $244 million of merger-related costs. We continued to hire new sales professionals in the quarter in our regional bank and retail securities brokerage business while improving sales force productivity. In addition, we opened 12 banking stores during the quarter. Even though we continue to invest appropriately in our business for long-term revenue growth, expenses were relatively flat overall reflecting the benefit of the consolidation of the two companies, and ongoing expense management initiatives. Including the FDIC special assessment and merger costs, which together represented 6% of total noninterest expense during the quarter, the efficiency ratio was 56.4%, flat from first quarter s 56.2%.

Net charge-offs in second quarter 2009 were $4.4 billion (2.11% of average total loans outstanding, annualized), compared with $3.3 billion (1.54%) in first quarter 2009 and $1.5 billion (1.55%) in second quarter 2008. Legacy Wells Fargo net charge-offs were $3.4 billion compared with $2.9 billion in first quarter 2009 and Wachovia net charge-offs totaled $984 million, including $103 million related to SOP 03-3 loans, compared with $371 million in first quarter 2009. Wachovia loans accounted for under SOP 03-3 were written down to fair value at December 31, 2008, and, accordingly, charge-offs on that portfolio will only occur if the portfolio deteriorates subsequent to the acquisition.

Credit losses rose in the second quarter, as expected, due to the weak economy and higher unemployment in the quarter. We expect credit losses and nonperforming assets to increase further, although we are beginning to see some moderation in the growth rate of losses in a number of consumer portfolios, as evidenced by some stabilization in early stage delinquencies. This moderation is largely the result of actions we and Wachovia have taken over the last two years to reduce risk. While credit losses rose in

Table of Contents

second quarter 2009, the level of losses remained below the SCAP adverse scenario projections made by both the Company and the Federal Reserve.

Commercial and commercial real estate losses increased in the quarter as the effects of the current economic cycle challenged more of our commercial customers. Loss levels increased from prior periods, driven by losses from loans to customers whose businesses rely on the residential real estate industry and consumer goods and services. We expect this trend to continue until the economy improves. We believe our losses will be moderated by the effect of our long standing underwriting discipline and relationship-centric business strategy. Approximately one third of the commercial losses were generated from our legacy Wells Fargo Business Direct channel. This channel consists of small lines of credit to small business customers. Losses from Business Direct decreased slightly from first quarter 2009, and delinquency levels showed moderate signs of improvement during the quarter, indicating possible stabilization in this portfolio. Losses in our consumer portfolios increased as expected, as more of our customers were affected by unemployment and the prolonged residential real estate down cycle. In line with our first quarter trends, our consumer real estate and credit card portfolio losses increased, while losses in our auto secured portfolios improved as a result of vintage aging and price improvement in used car markets.

We continue to take actions to reduce risk in the portfolio and invest in loss mitigation activities. At year-end, we took significant write-downs in certain Wachovia loan portfolios in purchase accounting and we have exited several higher risk non-strategic businesses and are liquidating these portfolios, such as Pick-a-Pay, legacy Wells Fargo indirect auto and third party originated home equity portfolios. We continue to monitor credit standards to improve the credit quality of new loans, all in an effort to reduce the risk in the portfolio while continuing to originate appropriately priced new business for our customers. Even with the challenges that remain, our teams are effectively working together to manage the risk, and the Wells Fargo credit culture is being implemented across the combined company.

The provision for credit losses was $5.1 billion and $9.6 billion in the second quarter and first half of 2009, respectively, compared with $3.0 billion and $5.0 billion, respectively, in the same periods a year ago. The provision in the second quarter and first half of 2009 included $700 million and $2.0 billion, respectively, of credit reserve build due to higher credit losses inherent in the loan portfolio. The allowance for credit losses, which consists of the allowance for loan losses and the reserve for unfunded credit commitments, was $23.5 billion (2.86% of total loans) at June 30, 2009, compared with $21.7 billion (2.51%) at December 31, 2008.

Total nonaccrual loans were $15.8 billion (1.92% of total loans) at June 30, 2009, compared with $10.5 billion (1.25%) at March 31, 2009. Nonaccrual loans exclude loans acquired from Wachovia accounted for under SOP 03-3 since these loans were written down in purchase accounting as of December 31, 2008, to an amount expected to be collectible. The increase in nonaccrual loans represented increases in both the commercial and consumer portfolios, with $3.2 billion related to Wachovia in second quarter 2009. The increases in nonaccrual loans were concentrated in portfolios secured by real estate or with borrowers dependent on the housing industry. Total nonperforming assets (NPAs) were $18.3 billion (2.23% of total loans) at June 30, 2009, compared with $12.6 billion (1.50%) at March 31, 2009.

The increase in nonaccrual loans in both first and second quarter 2009 was in part a consequence of purchase accounting. Typically, changes to nonaccrual loans from period to period represent inflows for loans that reach a specified past due status, net of any reductions for loans that are charged off, sold, transferred to foreclosed properties, or are no longer classified as nonaccrual because they return to accrual status. Substantially all of Wachovia s nonaccrual loans were accounted for under SOP 03-3 in purchase accounting and, as a result, were reclassified to accrual status on December 31, 2008. As certain Wachovia non-SOP 03-3 loans reached the past due threshold to be classified as nonaccrual during second quarter 2009, there were minimal offsetting Wachovia loans already in nonaccrual status transferring out of nonaccrual status. The effect of this was a higher dollar and percentage increase in nonaccrual loans in the quarter due to the application of SOP 03-3.

The increase in nonaccrual loans is also attributable to other factors, including deterioration in certain portfolios, particularly commercial and consumer real estate, and an increase in restructured loans, which accelerates loss recognition and results in loans remaining in nonaccrual status for a longer period of time.

The Company and each of its subsidiary banks continued to remain well-capitalized. Our total risk-based capital (RBC) ratio at June 30, 2009, was 13.84% and our Tier 1 RBC ratio was 9.80%, exceeding the minimum regulatory guidelines of 8% and 4%, respectively, for bank holding companies. Our total RBC ratio was 11.83% and our Tier 1 RBC ratio was 7.84% at December 31, 2008. Our Tier 1 leverage ratio was 8.32% and 14.52% at June 30, 2009, and December 31, 2008, respectively, exceeding the minimum regulatory guideline of 3% for bank holding companies.

We continued to build capital in second quarter 2009. As a percentage of total risk-weighted assets, Tier 1 capital and Tier 1 common equity increased to 9.80% and 4.49%, respectively, at June 30, 2009, up from 8.30% and 3.12%, respectively, at March 31, 2009. As previously stated, the Federal Reserve asked us to generate a $13.7 billion regulatory capital buffer by November 9, 2009, based on their revenue assumptions in the adverse case scenario. At June 30, 2009, with over a quarter to go before the SCAP plan is completed, we have exceeded this requirement by $500 million. We accomplished this through an $8.6 billion equity raise and internally generated capital including $2.4 billion of pre-provision net revenue (pre-tax pre-provision profit plus certain SCAP adjustments) in excess of the Federal Reserve s estimate, $2.7 billion realization of deferred tax assets and $500 million of other internally generated sources of capital, including core deposit intangible amortization. We expect to realize additional internally generated SCAP-qualifying capital in third quarter 2009, including additional deferred tax asset realization, which will add to the amount already generated in the second quarter. See footnote 4 on page 2 and the Capital Management section in this Report for more information.

Table of Contents

Current Accounting Developments

In first quarter 2009, we adopted the following new accounting pronouncements:

- FAS 161, *Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133*;
- FAS 160, *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51*;
- FAS 141R (revised 2007), *Business Combinations*;
- FASB Staff Position (FSP) FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*;
- FSP FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*; and
- FSP Emerging Issues Task Force (EITF) 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities*.

In second quarter 2009, we adopted the following new accounting pronouncements:

- FSP FAS 107-1 and APB Opinion 28-1, *Interim Disclosures about Fair Value of Financial Instruments*; and
- FAS 165, *Subsequent Events*.

In addition, the following accounting pronouncements were issued by the FASB, but are not yet effective:

- FAS 168, *The* FASB Accounting Standards Codification™ *and the Hierarchy of Generally Accepted Accounting Principles a replacement of FASB Statement No. 162*;
- FAS 166, *Accounting for Transfers of Financial Assets an amendment of FASB Statement No. 140*;
- FAS 167, *Amendments to FASB Interpretation No. 46(R)*; and
- FSP FAS 132(R)-1, *Employers Disclosures about Postretirement Benefit Plan Assets*.

Each of these pronouncements is described in more detail below.

FAS 161 changes the disclosure requirements for derivative instruments and hedging activities. It requires enhanced disclosures about how and why an entity uses derivatives, how derivatives and related hedged items are accounted for, and how derivatives and hedged items affect an entity s financial position, performance and cash flows. We adopted FAS 161 for first quarter 2009 reporting. See Note 11 (Derivatives) to Financial Statements in this Report for complete disclosures under FAS 161. Because FAS 161 amends only the disclosure requirements for derivative instruments and hedged items, the adoption of FAS 161 does not affect our consolidated financial results.

FAS 160 requires that noncontrolling interests (previously referred to as minority interests) be reported as a component of equity in the balance sheet. Prior to adoption of FAS 160, they were classified outside of equity. This new standard also changes the way a noncontrolling interest is presented in the income statement such that a parent s consolidated income statement includes amounts attributable to both the parent s interest and the noncontrolling interest. FAS 160 requires a parent to recognize a gain or loss when a subsidiary is deconsolidated. The remaining interest is initially recorded at fair value. Other changes in ownership interest where the parent continues to have a majority ownership interest in the subsidiary are accounted for as capital transactions. FAS 160 was effective on January 1, 2009. Adoption is applied prospectively to all noncontrolling interests including those that arose prior to the adoption of FAS 160, with retrospective adoption required for disclosure of noncontrolling interests held as of the adoption date.

We hold a controlling interest in a joint venture with Prudential Financial, Inc. (Prudential). For more information, see the Contractual Obligations section in our 2008 Form 10-K. In connection with the adoption of FAS 160 on January 1, 2009, we reclassified Prudential s noncontrolling interest to equity. Under the terms of the original agreement under which the joint venture was established between Wachovia and Prudential, each party has certain rights such that changes in our ownership interest can occur. On December 4, 2008, Prudential publicly announced its intention to exercise its option to put its noncontrolling interest to us at the end of the lookback period, as defined (January 1, 2010). As a result of the issuance of FAS 160 and related interpretive guidance, along with this stated intention, on January 1, 2009, we increased the carrying value of Prudential s noncontrolling interest in the joint venture to the estimated maximum redemption amount, with the offset recorded to additional paid-in capital.

FAS 141R requires an acquirer in a business combination to recognize the assets acquired (including loan receivables), the liabilities assumed, and any noncontrolling interest in the acquiree at the acquisition date, at their fair values as of that date, with limited exceptions. The acquirer is not permitted to recognize a separate valuation allowance as of the acquisition date for loans and other assets acquired in a business combination. The revised statement requires acquisition-related costs to be expensed separately from the acquisition. It also requires restructuring costs that the acquirer expected but was not obligated to incur, to be expensed separately from the business combination. FAS 141R is applicable prospectively to business combinations completed on or after January 1, 2009.

FSP FAS 157-4 addresses measuring fair value under FAS 157 in situations where markets are inactive and transactions are not orderly. The FSP acknowledges that in these circumstances quoted prices may not be determinative of fair value. The FSP emphasizes, however, that even if there has been a significant decrease in the volume and level of activity for an asset or liability and regardless of the valuation technique(s) used, the objective of a fair value measurement has not changed. Prior to issuance of this FSP, FAS 157 had been interpreted by many companies, including Wells Fargo, to emphasize that fair value must be measured based on the most recently available quoted market prices, even for markets that have experienced a significant decline in the volume and level of activity relative to normal conditions and therefore could have increased frequency of transactions that are not orderly. Under the provisions of the FSP, price quotes for assets or liabilities in inactive markets may require adjustment due to uncertainty as to whether the underlying transactions are orderly.

For inactive markets, there is little information, if any, to evaluate if individual transactions are orderly. Accordingly, we are required to estimate, based upon all available facts and circumstances, the degree to which orderly transactions are occurring. The FSP does not prescribe a specific method for adjusting transaction or quoted prices; however, it does provide guidance for determining how much weight to give transaction or quoted prices. Price quotes based upon transactions that are not orderly are not considered to be determinative of fair value and should be given little, if any, weight in measuring fair value. Price quotes based upon transactions that are orderly shall be considered in determining fair value, with the weight given based upon the facts and circumstances. If sufficient information is not available to determine if price quotes are based upon orderly transactions, less weight should be given to the price quote relative to other transactions that are known to be orderly.

The provisions of FSP FAS 157-4 are effective for second quarter 2009; however, as permitted under the pronouncement, we early adopted in first quarter 2009. Adoption of this pronouncement resulted in an increase in the valuation of securities available for sale in first quarter 2009 of $4.5 billion ($2.8 billion after tax), which was included in other comprehensive income, and trading assets of $18 million, which was reflected in earnings. See the Critical Accounting Policies section in this Report for more information.

Table of Contents

FSP FAS 115-2 and FAS 124-2 states that an OTTI write-down of debt securities, where fair value is below amortized cost, is triggered in circumstances where (1) an entity has the intent to sell a security, (2) it is more likely than not that the entity will be required to sell the security before recovery of its amortized cost basis, or (3) the entity does not expect to recover the entire amortized cost basis of the security. If an entity intends to sell a security or if it is more likely than not the entity will be required to sell the security before recovery, an OTTI write-down is recognized in earnings equal to the entire difference between the security s amortized cost basis and its fair value. If an entity does not intend to sell the security or it is more likely than not that it will not be required to sell the security before recovery, the OTTI write-down is separated into an amount representing the credit loss, which is recognized in earnings, and the amount related to all other factors, which is recognized in other comprehensive income. The provisions of this FSP are effective for second quarter 2009; however, as permitted under the pronouncement, we early adopted on January 1, 2009, and increased the beginning balance of retained earnings by $85 million ($53 million after tax) with a corresponding adjustment to cumulative other comprehensive income for OTTI recorded in previous periods on securities in our portfolio at January 1, 2009, that would not have been required had the FSP been effective for those periods.

FSP EITF 03-6-1 requires that unvested share-based payment awards that have nonforfeitable rights to dividends or dividend equivalents be treated as participating securities and, therefore, included in the computation of earnings per share under the two-class method described in FAS 128, *Earnings per Share*. This pronouncement is effective on January 1, 2009, with retrospective adoption required. The adoption of FSP EITF 03-6-1 did not have a material effect on our consolidated financial statements.

FSP FAS 107-1 and APB 28-1 states that entities must disclose the fair value of financial instruments in interim reporting periods as well as in annual financial statements. The FSP also requires disclosure of the methods and assumptions used to estimate fair value as well as any changes in methods and assumptions that occurred during the reporting period. We adopted this pronouncement in second quarter 2009. See Note 12 (Fair Values of Assets and Liabilities) to Financial Statements in this Report for additional information. Because the FSP amends only the disclosure requirements related to the fair value of financial instruments, the adoption of this FSP does not affect our consolidated financial statements.

FAS 165 describes two types of subsequent events that previously were addressed in the auditing literature, one that requires post-period end adjustment to the financial statements being issued, and one that requires footnote disclosure only. FAS 165 also requires a company to disclose the date through which management has evaluated subsequent events, which for public companies is the date that financial statements are issued. FAS 165 is effective in second quarter 2009 with prospective application. See Note 1 (Summary of Significant Accounting Policies) to Financial Statements in this Report for our discussion of subsequent events. Our adoption of this standard did not have a material impact on our consolidated financial statements.

FAS 168 establishes the *FASB Accounting Standards Codification™* (Codification) as the source of authoritative generally accepted accounting principles (GAAP) in the United States for companies to use in the preparation of their financial statements. SEC rules and interpretive releases are also authoritative GAAP for SEC registrants. The Codification includes guidance that has been issued by the FASB, EITF and the SEC. All guidance contained in the Codification carries the same level of authority and will supersede all existing non-SEC accounting and reporting standards. Any accounting literature that is non-SEC and has not been grandfathered will become nonauthoritative. FAS 168 is effective for us in third quarter 2009. This standard will change our disclosures as references to existing accounting literature will be updated to reflect the Codification. However, the adoption of FAS 168 will not affect our consolidated financial statements.

Table of Contents

In June 2009, the FASB issued FAS 166 and FAS 167, which will require us, effective January 1, 2010, to consolidate certain qualifying special purpose entities (QSPEs) and variable interest entities (VIEs) that are not currently included in our consolidated financial statements.

FAS 166 modifies the guidance in FAS 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities.* This standard eliminates the concept of QSPEs and provides additional criteria transferors must use to evaluate transfers of financial assets. To determine if a transfer is to be accounted for as a sale, the transferor must assess whether it and all of the entities included in its consolidated financial statements have surrendered control of the assets. A transferor must consider all arrangements or agreements made or contemplated at the time of transfer before reaching a conclusion on whether control has been relinquished. FAS 166 addresses situations in which a portion of a financial asset is transferred. In such instances the transfer can only be accounted for as a sale when the transferred portion is considered to be a participating interest. FAS 166 also requires that any assets or liabilities retained from a transfer accounted for as a sale be initially recognized at fair value. This standard is effective for us as of January 1, 2010, with adoption applied prospectively for transfers that occur on and after the effective date.

FAS 167 amends several key provisions contained in FASB Interpretation No. 46 (Revised December 2003), *Consolidation of Variable Interest Entities* (FIN 46(R)). First, the scope of FAS 167 includes entities that were formerly designated as QSPEs under FAS 140. Second, FAS 167 changes the approach companies use to identify the VIEs for which they are deemed to be the primary beneficiary and are required to consolidate. Under FIN 46(R), the primary beneficiary is the entity that absorbs the majority of a VIE s losses and receives the majority of the VIE s returns. The guidance in FAS 167 identifies a VIE s primary beneficiary as the entity that has the power to direct the VIE s significant activities, and has an obligation to absorb losses or the right to receive benefits that could be potentially significant to the VIE. Third, FAS 167 requires companies to continually reassess whether they are the primary beneficiary of a VIE. Existing rules only require companies to reconsider primary beneficiary conclusions when certain triggering events have occurred. FAS 167 is effective for us as of January 1, 2010, and applies to all existing QSPEs and VIEs, and VIEs created after the effective date.

Application of FAS 166 and FAS 167 will result in the January 1, 2010, consolidation of certain QSPEs and VIEs that are not currently included in our consolidated financial statements. We have performed a preliminary analysis of these accounting standards with respect to QSPE and VIE structures currently applicable to us and have identified the following items that may potentially be consolidated.

(in billions)		Incremental GAAP assets	Incremental risk-weighted assets
Residential mortgage loans nonconforming (1) (2)	$	87	42
Other consumer loans		6	3
Commercial paper conduit		6	
Investment funds		8	5
Other		2	(4)
Total	$	109	46

(1) Represents certain of our residential mortgage loans that are not guaranteed by government-sponsored

entities (nonconforming). We have concluded that $1.1 trillion of conforming residential mortgage loans involved in securitizations are not subject to consolidation under FAS 166 and FAS 167.

(2) We are actively exploring the sale of certain interests we hold in securitized residential mortgage loans, which would reduce the amount of residential mortgage loans subject to consolidation under FAS 166 and FAS 167 by approximately $37 billion ($18 billion of risk-weighted assets). There is no assurance that we will be able to execute such sales prior to adoption of these accounting standards, although it is our intent to do so.

Table of Contents

FAS 166 and 167 are principles based and limited interpretive guidance is currently available. We will continue to evaluate QSPE and VIE structures applicable to us, monitor interpretive guidance, and work with our external auditors and other appropriate interested parties to properly implement these standards. Accordingly, the amount of assets that actually become consolidated on our financial statements upon implementation of these standards on January 1, 2010, may differ materially from our preliminary analysis presented in the previous table.

FSP FAS 132 (R)-1 requires new disclosures about plan assets that are applicable to the plan assets of our Cash Balance Plan and other postretirement benefit plans. The objectives of the new disclosures are to provide an understanding of how investment allocation decisions are made, the major categories of plan assets, the inputs and valuation techniques used to measure fair value, the effect of fair value measurements using significant unobservable inputs on the changes in plan assets and significant concentrations of risk within plan assets. The new disclosures under FSP FAS 132 (R)-1 will be provided for fiscal years ending after December 15, 2009, and disclosures are not required for earlier periods presented for comparative purposes.

Table of Contents

CRITICAL ACCOUNTING POLICIES

Our significant accounting policies are fundamental to understanding our results of operations and financial condition because they require that we use estimates and assumptions that may affect the value of our assets or liabilities, and our financial results. Six of these policies are critical because they require management to make difficult, subjective and complex judgments about matters that are inherently uncertain and because it is likely that materially different amounts would be reported under different conditions or using different assumptions. These policies govern:

- the allowance for credit losses;
- acquired loans accounted for under SOP 03-3;
- the valuation of residential mortgage servicing rights (MSRs);
- the fair valuation of financial instruments;
- pension accounting; and
- income taxes.

With respect to pension accounting, on April 28, 2009, the Board of Directors (the Board) approved amendments to freeze the benefits earned under the Wells Fargo qualified and supplemental cash balance plans and Wachovia s cash balance pension plan, and to merge Wachovia s plan into the Wells Fargo cash balance plan. These actions became effective on July 1, 2009. This will have the effect of reducing pension expense in future periods. See Note 14 (Employee Benefits) to Financial Statements in this Report for additional information.

Management has reviewed and approved these critical accounting policies and has discussed these policies with the Audit and Examination Committee of the Board. These policies are described in the Financial Review Critical Accounting Policies section and Note 1 (Summary of Significant Accounting Policies) to Financial Statements in our 2008 Form 10-K. Due to the adoption of FSP FAS 157-4, which affects the measurement of fair value of certain assets, principally securities and trading assets, we have updated the policy on the fair value of financial instruments, as described below.

FAIR VALUE OF FINANCIAL INSTRUMENTS

We use fair value measurements to record fair value adjustments to certain financial instruments and to develop fair value disclosures. See our 2008 Form 10-K for the complete critical accounting policy related to fair value of financial instruments.

In connection with the adoption of FSP FAS 157-4, we developed policies and procedures to determine when the level and volume of activity for our assets and liabilities requiring fair value measurements have declined significantly relative to normal conditions. For items that use price quotes, such as certain security classes within securities available for sale, the degree of market inactivity and distressed transactions is estimated to determine the appropriate adjustment to the price quotes from an external broker or pricing service. The methodology we use to adjust the quotes generally involves weighting the price quotes and results of internal pricing techniques, such as the net present value of future expected cash flows (with observable inputs, where available) discounted at a rate of return market participants require to arrive at the fair value. The more active and orderly markets for particular security classes are determined to be, the more weighting we assign to price quotes. The less active and the orderly markets are determined to be, the less weighting we assign to price quotes.

Approximately 24% of total assets ($313.3 billion) at June 30, 2009, and 19% of total assets ($247.5 billion) at December 31, 2008, consisted of financial instruments recorded at fair value on a recurring basis. Assets for which fair values were measured using significant Level 3 inputs (before derivative netting adjustments) represented approximately 20% of these financial instruments (5% of total assets) at June 30, 2009, and approximately 22% (4% of total assets) at December 31, 2008. The fair value of the remaining assets was measured using valuation methodologies involving market-based or market-derived information, collectively Level 1 and 2 measurements.

Approximately 2% of total liabilities ($21.0 billion) at June 30, 2009, and 2% ($18.8 billion) at December 31, 2008, consisted of financial instruments recorded at fair value on a recurring basis. Liabilities valued using Level 3 measurements (before derivative netting adjustments) were $8.7 billion and $9.3 billion at June 30, 2009, and December 31, 2008, respectively.

Table of Contents

EARNINGS PERFORMANCE

NET INTEREST INCOME

Net interest income is the interest earned on debt securities, loans (including yield-related loan fees) and other interest-earning assets minus the interest paid for deposits, short-term borrowings and long-term debt. The net interest margin is the average yield on earning assets minus the average interest rate paid for deposits and our other sources of funding. Net interest income and the net interest margin are presented on a taxable-equivalent basis to consistently reflect income from taxable and tax-exempt loans and securities based on a 35% federal statutory tax rate.

Net interest income was $11.8 billion in second quarter 2009, with approximately 39% contributed by Wachovia, and $6.3 billion in second quarter 2008. Net interest income reflected a strong combined net interest margin of 4.30%, and the benefit of continued growth in core deposits.

Average earning assets increased to $1.1 trillion in second quarter 2009 from $515.8 billion in second quarter 2008. Average loans increased to $833.9 billion in second quarter 2009 from $391.5 billion a year ago. Average mortgages held for sale increased to $43.2 billion in second quarter 2009 from $28.0 billion a year ago. Average debt securities available for sale increased to $179.0 billion in second quarter 2009 from $84.7 billion a year ago.

Core deposits are a low-cost source of funding and thus an important contributor to growth in net interest income and the net interest margin. Core deposits include noninterest-bearing deposits, interest-bearing checking, savings certificates, market rate and other savings, and certain foreign deposits (Eurodollar sweep balances). Average core deposits rose to $765.7 billion in second quarter 2009 from $318.4 billion in second quarter 2008, with over half of the increase from Wachovia, and funded 92% and 81% of average loans in second quarter 2009 and 2008, respectively. About 80% of our core deposits are now in checking and savings deposits, one of the highest percentages in the industry. Total average retail core deposits, which exclude Wholesale Banking core deposits and retail mortgage escrow deposits, grew to $596.6 billion for second quarter 2009 from $230.4 billion a year ago. Average mortgage escrow deposits were $32.0 billion, compared with $22.7 billion a year ago. Average certificates of deposits increased to $152.4 billion in second quarter 2009 from $37.6 billion a year ago and average checking and savings deposits increased to $613.3 billion in second quarter 2009 from $280.7 billion a year ago. Total average interest-bearing deposits increased to $638.0 billion in second quarter 2009 from $262.5 billion a year ago.

The following table presents the individual components of net interest income and the net interest margin.

Table of Contents

AVERAGE BALANCES, YIELDS AND RATES PAID (TAXABLE-EQUIVALENT BASIS) (1) (2)

						Quarter ended June 30,
			2009			2008
(in millions)	**Average balance**	**Yields/ rates**	**Interest income/ expense**	Average balance	Yields/ rates	Interest income/ expense
Earning assets						
Federal funds sold, securities purchased under resale agreements and other short-term investments	**$ 20,889**	**0.66%**	**$ 34**	3,853	2.32%	$ 22
Trading assets	**18,464**	**4.61**	**213**	4,915	3.24	39
Debt securities available for sale (3):						
Securities of U.S. Treasury and federal agencies	**2,102**	**3.45**	**17**	1,050	3.77	10
Securities of U.S. states and political subdivisions	**12,189**	**6.47**	**206**	7,038	6.62	118
Mortgage-backed securities:						
Federal agencies	**92,550**	**5.36**	**1,203**	40,630	5.92	588
Residential and commercial	**41,257**	**9.03**	**1,044**	22,419	5.87	340
Total mortgage-backed securities	**133,807**	**6.60**	**2,247**	63,049	5.90	928
Other debt securities (4)	**30,901**	**7.23**	**572**	13,600	6.30	226
Total debt securities available for sale (4)	**178,999**	**6.67**	**3,042**	84,737	6.00	1,282
Mortgages held for sale (5)	**43,177**	**5.05**	**545**	28,004	6.04	423
Loans held for sale (5)	**7,188**	**2.83**	**50**	734	5.63	10
Loans:						
Commercial and commercial real estate:						
Commercial	**187,501**	**4.11**	**1,922**	95,263	6.09	1,444
Other real estate mortgage	**104,297**	**3.46**	**900**	39,977	5.77	573
Real estate construction	**33,857**	**2.69**	**227**	19,213	5.01	240
Lease financing	**14,750**	**9.22**	**340**	7,087	5.64	100
Total commercial and commercial real estate	**340,405**	**3.99**	**3,389**	161,540	5.86	2,357
Consumer:						
Real estate 1-4 family first mortgage	**240,798**	**5.53**	**3,328**	73,663	6.79	1,250
Real estate 1-4 family junior lien mortgage	**108,422**	**4.77**	**1,290**	75,018	6.68	1,246

Credit card	**22,963**	**12.74**	**731**	19,037	11.81	561
Other revolving credit and installment	**90,729**	**6.64**	**1,502**	54,842	8.78	1,198
Total consumer	**462,912**	**5.93**	**6,851**	222,560	7.67	4,255
Foreign	**30,628**	**4.06**	**310**	7,445	10.61	197
Total loans (5)	**833,945**	**5.07**	**10,550**	391,545	6.98	6,809
Other	**6,079**	**2.91**	**45**	2,033	4.47	24
Total earning assets	**$ 1,108,741**	**5.21%**	**$ 14,479**	515,821	6.69%	$ 8,609
Funding sources						
Deposits:						
Interest-bearing checking	**$ 79,955**	**0.13%**	**$ 26**	5,487	1.18%	$ 16
Market rate and other savings	**334,067**	**0.40**	**336**	161,760	1.21	486
Savings certificates	**152,444**	**1.19**	**451**	37,634	3.06	287
Other time deposits	**21,660**	**2.00**	**108**	5,773	2.72	38
Deposits in foreign offices	**49,885**	**0.29**	**36**	51,884	1.83	236
Total interest-bearing deposits	**638,011**	**0.60**	**957**	262,538	1.63	1,063
Short-term borrowings	**59,844**	**0.39**	**58**	66,537	2.16	357
Long-term debt	**235,590**	**2.52**	**1,484**	100,552	3.41	856
Other liabilities	**4,604**	**3.45**	**40**			
Total interest-bearing liabilities	**938,049**	**1.08**	**2,539**	429,627	2.13	2,276
Portion of noninterest-bearing funding sources	**170,692**			86,194		
Total funding sources	**$ 1,108,741**	**0.91**	**2,539**	515,821	1.77	2,276
Net interest margin and net interest income on a taxable-equivalent basis (6)		**4.30%**	**$ 11,940**		4.92%	$ 6,333
Noninterest-earning assets						
Cash and due from banks	**$ 19,340**			10,875		
Goodwill	**24,261**			13,171		
Other	**122,584**			54,882		
Total noninterest-earning assets	**$ 166,185**			78,928		
Noninterest-bearing funding sources						
Deposits	**$ 174,529**			88,041		
Other liabilities	**49,570**			28,434		
Total equity	**112,778**			48,647		

Noninterest-bearing funding sources used to fund earning assets	**(170,692)**	(86,194)
Net noninterest-bearing funding sources	**$ 166,185**	78,928
Total assets	**$ 1,274,926**	594,749

(1) Our average prime rate was 3.25% and 5.08% for the quarters ended June 30, 2009 and 2008, respectively, and 3.25% and 5.65% for the first half of 2009 and 2008, respectively. The average three-month London Interbank Offered Rate (LIBOR) was 0.84% and 2.75% for the quarters ended June 30, 2009 and 2008, respectively, and 1.04% and 3.02% for the first half of 2009 and 2008, respectively.

(2) Interest rates and amounts include the effects of hedge and risk management activities associated with the respective asset and liability categories.

(3) Yields are based on amortized cost balances computed on a settlement

date basis.

(4) Includes certain preferred securities.

(5) Nonaccrual loans and related income are included in their respective loan categories.

(6) Includes taxable-equivalent adjustments primarily related to tax-exempt income on certain loans and securities. The federal statutory tax rate was 35% for the periods presented.

	Six months ended June 30,					
			2009			2008
(in millions)	**Average balance**	**Yields/ rates**	**Interest income/ expense**	Average balance	Yields/ rates	Interest income/ expense
Earning assets						
Federal funds sold, securities purchased under resale agreements and other short-term investments	**$ 22,472**	**0.75%**	**$ 84**	3,870	2.81%	$ 54
Trading assets	**20,323**	**4.81**	**488**	5,022	3.49	87
Debt securities available for sale (3):						
Securities of U.S. Treasury and federal agencies	**2,498**	**2.00**	**24**	1,012	3.81	19
Securities of U.S. states and political subdivisions	**12,201**	**6.45**	**419**	6,664	7.00	238
Mortgage-backed securities:						
Federal agencies	**84,592**	**5.51**	**2,271**	38,364	6.00	1,123
Residential and commercial	**39,980**	**8.80**	**2,061**	21,706	5.97	664
Total mortgage-backed securities	**124,572**	**6.71**	**4,332**	60,070	5.99	1,787
Other debt securities (4)	**30,493**	**7.02**	**1,123**	12,213	6.58	422
Total debt securities available for sale (4)	**169,764**	**6.68**	**5,898**	79,959	6.14	2,466
Mortgages held for sale (5)	**37,151**	**5.17**	**960**	27,138	6.02	817
Loans held for sale (5)	**7,567**	**3.13**	**117**	691	6.52	22
Loans:						
Commercial and commercial real estate:						
Commercial	**192,186**	**3.99**	**3,806**	93,174	6.50	3,013
Other real estate mortgage	**104,283**	**3.47**	**1,794**	38,701	6.09	1,173
Real estate construction	**34,174**	**2.86**	**485**	19,073	5.53	525
Lease financing	**15,277**	**8.99**	**687**	6,956	5.71	198
Total commercial and commercial real estate	**345,920**	**3.94**	**6,772**	157,904	6.25	4,909
Consumer:						
Real estate 1-4 family first mortgage	**243,133**	**5.59**	**6,772**	72,985	6.84	2,496
Real estate 1-4 family junior lien mortgage	**109,270**	**4.91**	**2,665**	75,140	6.99	2,614
Credit card	**23,128**	**12.42**	**1,435**	18,907	12.06	1,140

Other revolving credit and installment	**91,770**	**6.66**	**3,029**	55,376	8.94	2,462
Total consumer	**467,301**	**5.98**	**13,901**	222,408	7.86	8,712
Foreign	**31,487**	**4.22**	**659**	7,420	10.94	404
Total loans (5)	**844,708**	**5.08**	**21,332**	387,732	7.26	14,025
Other	**6,110**	**2.89**	**88**	1,930	4.50	44
Total earning assets	**$ 1,108,095**	**5.22**%	**$ 28,967**	506,342	6.94%	$ 17,515
Funding sources						
Deposits:						
Interest-bearing checking	**$ 80,173**	**0.14**%	**$ 56**	5,357	1.54%	$ 41
Market rate and other savings	**323,813**	**0.47**	**755**	160,812	1.59	1,270
Savings certificates	**161,234**	**1.05**	**838**	39,774	3.54	700
Other time deposits	**23,597**	**1.98**	**232**	5,269	3.09	80
Deposits in foreign offices	**47,901**	**0.32**	**75**	49,262	2.31	566
Total interest-bearing deposits	**636,718**	**0.62**	**1,956**	260,474	2.05	2,657
Short-term borrowings	**67,911**	**0.54**	**181**	59,754	2.63	782
Long-term debt	**247,209**	**2.65**	**3,267**	100,619	3.85	1,933
Other liabilities	**4,194**	**3.64**	**76**			
Total interest-bearing liabilities	**956,032**	**1.15**	**5,480**	420,847	2.56	5,372
Portion of noninterest-bearing funding sources	**152,063**			85,495		
Total funding sources	**$ 1,108,095**	**0.99**	**5,480**	506,342	2.13	5,372
Net interest margin and net interest income on a taxable-equivalent basis (6)		**4.23**%	**$ 23,487**		4.81%	$ 12,143
Noninterest-earning assets						
Cash and due from banks	**$ 19,795**			11,262		
Goodwill	**23,725**			13,166		
Other	**130,665**			54,101		