

US BANCORP \DE\  
Form 10-Q  
November 09, 2006

**Table of Contents**

---

**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 September 30, 2006**  
**OR**  
 **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934  
For the transition period from (not applicable)  
Commission File Number 1-6880**  
**U.S. BANCORP**  
(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**41-0255900**  
(I.R.S. Employer  
Identification No.)

**800 Nicollet Mall**  
**Minneapolis, Minnesota 55402**  
(Address of principal executive offices, including zip code)  
**651-466-3000**  
(Registrant's telephone number, including area code)  
**(not applicable)**  
(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, and (2) has been subject to such filing requirements for the past 90 days.

YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):  
Large accelerated filer  Accelerated filer  Non-accelerated filer

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

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

Class  
Common Stock, \$.01 Par Value

Outstanding as of October 31, 2006  
1,757,859,766 shares

**Table of Contents and Form 10-Q Cross Reference Index****Part I Financial Information**

1) <u>Management's Discussion and Analysis of Financial Condition and Results of Operations (Item 2)</u>	
a) <u>Overview</u>	3
b) <u>Statement of Income Analysis</u>	4
c) <u>Balance Sheet Analysis</u>	7
d) <u>Critical Accounting Policies</u>	26
e) <u>Controls and Procedures (Item 4)</u>	26
2) <u>Quantitative and Qualitative Disclosures About Market Risk/ Corporate Risk Profile (Item 3)</u>	
a) <u>Overview</u>	9
b) <u>Credit Risk Management</u>	10
c) <u>Residual Risk Management</u>	16
d) <u>Operational Risk Management</u>	16
e) <u>Interest Rate Risk Management</u>	16
f) <u>Market Risk Management</u>	19
g) <u>Liquidity Risk Management</u>	19
h) <u>Capital Management</u>	20
3) <u>Line of Business Financial Review</u>	21
4) <u>Financial Statements (Item 1)</u>	28

**Part II Other Information**

1) <u>Risk Factors (Item 1A)</u>	46
2) <u>Unregistered Sales of Equity Securities and Use of Proceeds (Item 2)</u>	46
3) <u>Exhibits (Item 6)</u>	46
4) <u>Signature</u>	47
5) <u>Exhibits</u>	48
<u>Computation of Ratio of Earnings to Fixed Charges</u>	
<u>Section 302 Certification of Chief Executive Officer</u>	
<u>Section 302 Certification of Chief Financial Officer</u>	
<u>Section 906 Certification of Chief Executive Officer and Chief Financial Officer</u>	

**Safe Harbor Statement under the Private Securities Litigation Reform Act of 1995.**

This Form 10-Q contains forward-looking statements about U.S. Bancorp. Statements that are not historical or current facts, including statements about beliefs and expectations, are forward-looking statements. These statements often include the words may, could, would, should, believes, expects, anticipates, estimates, intends, potentially, probably, projects, outlook or similar expressions. These forward-looking statements cover, among other things, anticipated future revenue and expenses and the future plans and prospects of the Company. Forward-looking statements involve inherent risks and uncertainties, and important factors could cause actual results to differ materially from those anticipated, including changes in general business and economic conditions, changes in interest rates, legal and regulatory developments, increased competition from both banks and non-banks, changes in customer behavior and preferences, effects of mergers and acquisitions and related integration, and effects of critical accounting policies and judgments. For discussion of these and other risks that may cause actual results to differ from expectations, refer to our Annual Report on Form 10-K for the year ended December 31, 2005, on file with the Securities and Exchange Commission, including the sections entitled Risk Factors and Corporate Risk Profile. Forward-looking statements speak only as of the date they are made, and the Company undertakes no obligation to update them in light of new information or future events.

**Table of Contents****Table 1** Selected Financial Data

(Dollars and Shares in Millions, Except Per Share Data)	Three Months Ended September 30,			Nine Months Ended September 30,		
	2006	2005	Percent Change	2006	2005	Percent Change
<b>Condensed Income Statement</b>						
Net interest income (taxable-equivalent basis)(a)	\$1,673	\$1,791	(6.6)%	\$5,095	\$5,303	(3.9)%
Noninterest income	1,748	1,575	11.0	5,114	4,556	12.2
Securities gains (losses), net		1	*	3	(57)	*
Total net revenue	3,421	3,367	1.6	10,212	9,802	4.2
Noninterest expense	1,538	1,473	4.4	4,568	4,399	3.8
Provision for credit losses	135	145	(6.9)	375	461	(18.7)
Income before taxes	1,748	1,749	(.1)	5,269	4,942	6.6
Taxable-equivalent adjustment	13	9	44.4	34	23	47.8
Applicable income taxes	532	586	(9.2)	1,678	1,573	6.7
Net income	\$1,203	\$1,154	4.2	\$3,557	\$3,346	6.3
Net income applicable to common equity	\$1,187	\$1,154	2.9	\$3,524	\$3,346	5.3
<b>Per Common Share</b>						
Earnings per share	\$.67	\$.63	6.3%	\$1.98	\$1.82	8.8%
Diluted earnings per share	.66	.62	6.5	1.95	1.80	8.3
Dividends declared per share	.33	.30	10.0	.99	.90	10.0
Book value per share	11.30	10.93	3.4			
Market value per share	33.22	28.08	18.3			
Average common shares outstanding	1,771	1,823	(2.9)	1,784	1,836	(2.8)
Average diluted common shares outstanding	1,796	1,849	(2.9)	1,809	1,862	(2.8)
<b>Financial Ratios</b>						
Return on average assets	2.23%	2.23%		2.24%	2.22%	
Return on average common equity	23.6	22.8		23.7	22.5	
Net interest margin (taxable-equivalent basis)(a)	3.56	3.95		3.68	4.00	
Efficiency ratio(b)	45.0	43.8		44.7	44.6	
<b>Average Balances</b>						
Loans	\$142,894	\$135,283	5.6%	\$141,059	\$131,432	7.3%
Loans held for sale	2,448	2,038	20.1	2,062	1,723	19.7
Investment securities	39,806	41,782	(4.7)	39,858	42,308	(5.8)

Edgar Filing: US BANCORP \DE\ - Form 10-Q

Earning assets	187,190	180,452	3.7	185,075	176,851	4.7
Assets	214,089	205,667	4.1	212,188	201,505	5.3
Noninterest-bearing deposits	28,220	29,434	(4.1)	28,666	29,003	(1.2)
Deposits	119,975	120,984	(.8)	120,456	120,552	(.1)
Short-term borrowings	23,601	22,248	6.1	23,398	18,313	27.8
Long-term debt	41,892	35,633	17.6	40,462	36,016	12.3
Shareholders equity	20,917	20,106	4.0	20,543	19,911	3.2

September	December
30,	31,
2006	2005

**Period End Balances**

Loans	\$144,408	\$137,806	4.8%
Allowance for credit losses	2,256	2,251	.2
Investment securities	39,520	39,768	(.6)
Assets	216,855	209,465	3.5
Deposits	120,961	124,709	(3.0)
Long-term debt	41,230	37,069	11.2
Shareholders equity	20,926	20,086	4.2
Regulatory capital ratios			
Tier 1 capital	8.8%	8.2%	
Total risk-based capital	13.0	12.5	
Leverage	8.3	7.6	
Tangible common equity	5.4	5.9	

\* *Not meaningful.*

(a) *Presented on a fully taxable-equivalent basis utilizing a tax rate of 35 percent.*

(b) *Computed as noninterest expense divided by the sum of net interest income on a taxable-equivalent basis and noninterest income excluding securities gains (losses), net.*

2

U.S. Bancorp

**Table of Contents**

## Management's Discussion and Analysis

**OVERVIEW**

**Earnings Summary** U.S. Bancorp and its subsidiaries (the Company) reported net income of \$1,203 million for the third quarter of 2006, compared with \$1,154 million for the third quarter of 2005. Net income of \$.66 per diluted common share in the third quarter of 2006 was higher than the same period of 2005 by \$.04 (6.5 percent). Return on average assets and return on average common equity were 2.23 percent and 23.6 percent, respectively, for the third quarter of 2006, compared with returns of 2.23 percent and 22.8 percent, respectively, for the third quarter of 2005. The Company's results for the third quarter of 2006 improved over the same period of 2005, as net income increased by \$49 million (4.2 percent), primarily due to strong growth in fee-based revenues and the benefit of a lower effective tax rate from a year ago. This was offset somewhat by lower net interest income and the additional operating costs of acquired businesses.

Total net revenue, on a taxable-equivalent basis, for the third quarter of 2006, was \$54 million (1.6 percent) higher than the third quarter of 2005, primarily reflecting a 10.9 percent increase in noninterest income, partially offset by a 6.6 percent decline in net interest income. Noninterest income growth was driven by organic business growth and expansion in trust and payment processing businesses. Noninterest income also included a gain related to the sale of equity interests in a card association. These favorable changes in noninterest income were partially offset by lower mortgage banking revenue due to the impact of adopting the fair value method of accounting under Statement of Financial Accounting Standards No. 156 Accounting for Servicing of Financial Assets (SFAS 156) in the first quarter of 2006.

Total noninterest expense in the third quarter of 2006 was \$65 million (4.4 percent) higher than the third quarter of 2005, primarily reflecting incremental operating and business integration costs associated with recent acquisitions, increased pension costs and higher operating costs related to investments in tax-advantaged projects from a year ago. This was partially offset by lower intangible expense due to the adoption of SFAS 156. The efficiency ratio (the ratio of noninterest expense to taxable-equivalent net revenue excluding net securities gains or losses) was 45.0 percent for the third quarter of 2006, compared with 43.8 percent for the third quarter of 2005.

The provision for credit losses for the third quarter of 2006 decreased \$10 million (6.9 percent), compared with the third quarter of 2005. The decrease in the provision for credit losses year-over-year primarily reflected strong credit quality and the near-term favorable impact of changes in bankruptcy law in the fourth quarter of 2005. Net charge-offs in the third quarter of 2006 were \$135 million, compared with \$156 million in the third quarter of 2005. The decline in credit losses from a year ago was principally due to the impact of changes in bankruptcy legislation that went into effect during the fourth quarter of 2005. Refer to Corporate Risk Profile for further information on the provision for credit losses, net charge-offs, nonperforming assets and factors considered by the Company in assessing the credit quality of the loan portfolio and establishing the allowance for credit losses.

The Company reported net income of \$3,557 million for the first nine months of 2006, compared with \$3,346 million for the first nine months of 2005. Net income of \$1.95 per diluted common share in the first nine months of 2006 was higher than the same period of 2005 by \$.15 (8.3 percent). Return on average assets and return on average common equity were 2.24 percent and 23.7 percent, respectively, for the first nine months of 2006, compared with returns of 2.22 percent and 22.5 percent, respectively, for the first nine months of 2005. The Company's results for the first nine months of 2006 improved over the same period of 2005, as net income rose by \$211 million (6.3 percent), primarily due to strong growth in fee-based revenues and lower credit-related costs. This was offset somewhat by lower net interest income and incremental operating and integration costs of acquired businesses.

Total net revenue, on a taxable-equivalent basis, for the first nine months of 2006, was \$410 million (4.2 percent) higher than the first nine months of 2005, primarily reflecting a 13.7 percent increase in noninterest income, partially offset by a 3.9 percent decline in net interest income. Noninterest income growth was driven by organic business growth, expansion in trust and payment processing businesses, higher trading income, and equity gains from the initial public offering and subsequent sale of the equity interest of a card association during the second and third quarters of 2006, respectively. These favorable changes in noninterest income categories were partially offset by





**Table of Contents**

lower mortgage banking revenue due to the impact of adopting SFAS 156, effective in the first quarter of 2006. In addition, there was a \$60 million favorable change in net securities gains (losses) as compared with the first nine months of 2005.

Total noninterest expense in the first nine months of 2006 was \$169 million (3.8 percent) higher than the first nine months of 2005, primarily reflecting incremental operating and business integration costs associated with recent acquisitions, increased pension costs and higher operating costs related to certain investments. This was partially offset by lower intangible expense due to the adoption of SFAS 156 and lower debt prepayment expense. The efficiency ratio was 44.7 percent for the first nine months of 2006, compared with 44.6 percent for the first nine months of 2005.

The provision for credit losses for the first nine months of 2006 decreased \$86 million (18.7 percent), compared with the first nine months of 2005. The decrease in the provision for credit losses year-over-year primarily reflected strong credit quality and lower net charge-offs relative to 2005. Net charge-offs in the first nine months of 2006 were \$375 million, compared with \$472 million in the first nine months of 2005. The decline in losses from a year ago was principally due to the impact of changes in bankruptcy legislation that went into effect during the fourth quarter of 2005 offset somewhat by lower commercial loan recoveries relative to the first nine months of 2005. Refer to

Corporate Risk Profile for further information on the provision for credit losses, net charge-offs, nonperforming assets and factors considered by the Company in assessing the credit quality of the loan portfolio and establishing the allowance for credit losses.

**STATEMENT OF INCOME ANALYSIS**

**Net Interest Income** Net interest income, on a taxable-equivalent basis, was \$1,673 million in the third quarter of 2006, compared with \$1,791 million in the third quarter of 2005. Net interest income, on a taxable-equivalent basis, was \$5,095 million in the first nine months of 2006, compared with \$5,303 million in the first nine months of 2005. Average earning assets increased \$6.7 billion (3.7 percent) and \$8.2 billion (4.7 percent) in the third quarter and first nine months of 2006, respectively, compared with the same periods of 2005. The increases in average earning assets were primarily driven by growth in total average loans, partially offset by a decrease in investment securities. The positive impact to net interest income from the growth in earning assets was more than offset by a lower net interest margin. The net interest margin for the third quarter and first nine months of 2006 was 3.56 percent and 3.68 percent, respectively, compared with 3.95 percent and 4.00 percent, respectively, for the same periods of 2005. The year-over-year decline in the net interest margin for the third quarter and first nine months of 2006 reflected the competitive lending environment, asset/liability management decisions and the impact of changes in the yield curve from a year ago. Compared with the same periods of 2005, credit spreads have tightened by approximately 24 basis points in the third quarter and 22 basis points in the first nine months of 2006 across most lending products due to competitive pricing and a change in mix reflecting growth in lower-spread, fixed-rate credit products and noninterest-bearing corporate card balances. The net interest margin also declined due to funding incremental asset growth with higher cost wholesale funding, share repurchases and asset/liability decisions designed to reduce the Company's interest rate sensitivity position. An increase in the margin benefit of net free funds and loan fees partially offset these factors. Beginning in the third quarter of 2006, the Federal Reserve Bank paused from its policies of increasing interest rates and tightening the money supply. If the Federal Reserve Bank leaves rates unchanged over the next several quarters, the Company expects net interest margin to stabilize as asset repricing occurs and funding costs moderate. Refer to the Consolidated Daily Average Balance Sheet and Related Yields and Rates table for further information on net interest income.

Average loans for the third quarter and first nine months of 2006 were higher by \$7.6 billion (5.6 percent) and \$9.6 billion (7.3 percent), respectively, compared with the same periods of 2005, reflecting growth in the majority of loan categories. During the first quarter of 2006, the Company began selling an increased proportion of its residential mortgage loan production and anticipates that residential mortgage loan balances will remain essentially flat in future periods.

Average investment securities in the third quarter and first nine months of 2006 were \$2.0 billion (4.7 percent) and \$2.5 billion (5.8 percent) lower, respectively, than the same periods of 2005. The change in the balance of the investment securities portfolio from a year ago principally reflected prepayments and maturities of securities and a

reduced focus on residential mortgage assets given the changing interest rate environment and mix of loan growth. Additionally, the Company reclassified approximately \$460 million of principal-only securities to its trading account effective January 1, 2006, in connection with the adoption of SFAS 156. Refer to the Interest Rate Risk

**Table of Contents**

Management section for further information on the sensitivity of net interest income to changes in interest rates.

Average noninterest-bearing deposits for the third quarter and first nine months of 2006 decreased \$1.2 billion (4.1 percent) and \$337 million (1.2 percent), respectively, compared with the same periods of 2005, reflecting a decline in business demand deposits as these customers reduce excess liquidity to fund business growth. The change also reflects a migration of customers to interest-bearing products given rising interest rates.

Average total savings products declined year-over-year by \$1.7 billion (3.0 percent) in the third quarter and \$2.4 billion (4.2 percent) in the first nine months of 2006, compared with the same periods of 2005, due to reductions in average money market savings and other savings accounts, partially offset by an increase in interest checking balances. Average money market savings balances declined year-over-year primarily due to a decline in balances within the branches. This decrease was partially offset by increases in broker dealer and corporate trust balances. The overall decrease in average money market savings balances year-over-year was primarily the result of the Company's deposit pricing decisions for money market products in relation to fixed-rate deposit products offered. A portion of branch-based money market savings accounts have migrated to fixed-rate time certificates to take advantage of higher interest rates for these products.

Average time certificates of deposit less than \$100,000 were higher by \$604 million (4.6 percent) and \$556 million (4.2 percent) in the third quarter and first nine months of 2006, respectively, compared with the same periods of 2005. Average time deposits greater than \$100,000 grew \$1.3 billion (6.2 percent) and \$2.1 billion (10.5 percent) in the third quarter and first nine months of 2006, respectively, compared with the same periods of 2005. This growth was broad-based across most areas of the Company including: branch banking, commercial banking, private client and corporate trust, as customers migrated balances to higher rate deposits.

**Provision for Credit Losses** The provision for credit losses for the third quarter and first nine months of 2006 decreased \$10 million (6.9 percent) and \$86 million (18.7 percent), respectively, compared with the same periods of 2005. The decrease in the provision for credit losses year-over-year primarily reflected stronger credit quality and the near-term favorable impact of changes in bankruptcy law in the fourth quarter of 2005. Net charge-offs in the third quarter and first nine months of 2006 were \$135 million and \$375 million, respectively, compared with \$156 million and \$472 million in the third quarter and first nine months of 2005, respectively. The decline in losses from a year ago was principally due to the impact of changes in bankruptcy legislation that went into effect during the fourth quarter of 2005. Refer to Corporate Risk Profile for further information on the provision for credit losses, net charge-offs, nonperforming assets and factors considered by the Company in assessing the credit quality of the loan portfolio and establishing the allowance for credit losses.

**Table 2** Noninterest Income

(Dollars in Millions)	Three Months Ended September 30,			Nine Months Ended September 30,		
	2006	2005	Percent Change	2006	2005	Percent Change
Credit and debit card revenue	\$206	\$185	11.4%	\$590	\$516	14.3%
Corporate payment products revenue	150	135	11.1	416	362	14.9
ATM processing services	63	64	(1.6)	183	168	8.9
Merchant processing services	253	200	26.5	719	576	24.8
Trust and investment management fees	305	251	21.5	916	751	22.0
Deposit service charges	268	246	8.9	764	690	10.7
Treasury management fees	111	109	1.8	334	333	.3
Commercial products revenue	100	103	(2.9)	311	299	4.0
Mortgage banking revenue	68	111	(38.7)	167	323	(48.3)
Investment products fees and commissions	34	37	(8.1)	114	115	(.9)

Securities gains (losses), net		1	*	3	(57)	*
Other	190	134	41.8	600	423	41.8
Total noninterest income	\$1,748	\$1,576	10.9%	\$5,117	\$4,499	13.7%

\* *Not meaningful.*

U.S. Bancorp

5

**Table of Contents**

**Noninterest Income** Noninterest income in the third quarter and first nine months of 2006 was \$1,748 million and \$5,117 million, respectively, compared with \$1,576 million and \$4,499 million in the same periods of 2005. The \$172 million (10.9 percent) increase during the third quarter and \$618 million (13.7 percent) increase during the first nine months of 2006, compared with the same periods in 2005, were driven by favorable variances in the majority of fee income categories and a gain on the sale of equity interests in a card association included in other income. The increase in noninterest income for the first nine months of 2006 also reflected the impact of higher trading income related to certain derivatives and a gain from the initial public offering of a card association recorded in the current year, and a favorable variance in securities gains (losses) of \$60 million related to net securities losses recorded in the prior year. This strong growth in fee-based revenue was partially offset by the accounting impact of SFAS 156 on mortgage banking revenue.

The growth in credit and debit card revenue was primarily driven by higher customer transaction volumes. The corporate payment products revenue growth reflected organic growth in sales volumes and card usage and acquired business expansion. ATM processing services revenue for the first nine months of 2006 was higher due to the acquisition of an ATM business in May of 2005. Merchant processing services revenue growth reflected an increase in sales volume driven by acquisitions, higher same store sales, rates and equipment fees. Trust and investment management fees increased in the third quarter and first nine months year-over-year, primarily due to the acquisition of the corporate and institutional trust business of a large national bank, account growth and favorable equity market conditions. Deposit service charges grew year-over-year due to increased transaction-related fees and the impact of net new checking accounts. Other income for the third quarter and first nine months of 2006 was higher than the same periods of 2005 due to a \$32 million gain on the sale of equity interests in a card association and an increase in other equity investment revenue. In addition, other income for the first nine months of 2006 was higher due to a \$44 million gain on certain interest rate swaps, a \$35 million gain from the initial public offering of a card association, end-of-term lease residual value improvement, higher student loan sales gains and the receipt of a favorable settlement within the merchant processing business. These favorable changes in fee-based revenue were partially offset by the decline in mortgage banking revenue, principally driven by the adoption of the fair value method of accounting for mortgage servicing rights (MSRs) under SFAS 156.

**Noninterest Expense** Noninterest expense was \$1,538 million and \$4,568 million, respectively, in the third quarter and first nine months of 2006, an increase of \$65 million (4.4 percent) and \$169 million (3.8 percent), respectively, from the same periods of 2005. Compensation expense was higher year-over-year in the third quarter and first nine months of 2006, primarily due to the corporate and institutional trust and payments processing acquisitions and other growth initiatives. Employee benefits increased year-over-year primarily as a result of higher pension costs. Net occupancy and equipment expense increased from the same periods of 2005 primarily due to business expansion. Professional services expense was higher year-over-year primarily due to business development initiatives, regulatory and legal costs. Technology and communications expense rose due to higher outside data

**Table 3** Noninterest Expense

(Dollars in Millions)	Three Months Ended September 30,			Nine Months Ended September 30,		
	2006	2005	Percent Change	2006	2005	Percent Change
Compensation	\$632	\$603	4.8%	\$1,892	\$1,782	6.2%
Employee benefits	123	106	16.0	379	330	14.8
Net occupancy and equipment	168	162	3.7	494	475	4.0
Professional services	54	44	22.7	130	119	9.2
Marketing and business development	58	61	(4.9)	156	171	(8.8)
Technology and communications	128	118	8.5	372	337	10.4

Edgar Filing: US BANCORP \DE\ - Form 10-Q

Postage, printing and supplies	66	64	3.1	198	190	4.2
Other intangibles	89	125	(28.8)	263	377	(30.2)
Debt prepayment				11	54	(79.6)
Other	220	190	15.8	673	564	19.3
<b>Total noninterest expense</b>	<b>\$1,538</b>	<b>\$1,473</b>	<b>4.4%</b>	<b>\$4,568</b>	<b>\$4,399</b>	<b>3.8%</b>
Efficiency ratio (a)	45.0%	43.8%		44.7%	44.6%	

(a) *Computed as noninterest expense divided by the sum of net interest income on a taxable-equivalent basis and noninterest income excluding securities gains (losses), net.*

6

U.S. Bancorp

---

**Table of Contents**

processing expense principally associated with expanding a prepaid gift card program and the corporate and institutional trust acquisition. Other expense increased in the third quarter and first nine months of 2006 from the same periods of 2005, primarily due to the increased investments in tax-advantaged projects relative to a year ago. Offsetting these expense increases was a year-over-year decline in other intangibles expense, reflecting the elimination of MSR amortization and impairment due to the adoption of SFAS 156. Debt prepayment expense was also lower in the first nine months of 2006, compared with the same period of 2005.

**Income Tax Expense** The provision for income taxes was \$532 million (an effective rate of 30.7 percent) for the third quarter and \$1,678 million (an effective rate of 32.1 percent) for the first nine months of 2006, compared with \$586 million (an effective rate of 33.7 percent) and \$1,573 million (an effective rate of 32.0 percent) for the same periods of 2005. The effective rate for the third quarter of 2006 reflected an expected increase in income tax credits from tax-advantaged investments through the remainder of the year. For further information on income taxes, refer to Note 9 of the Notes to Consolidated Financial Statements.

**BALANCE SHEET ANALYSIS**

**Loans** The Company's total loan portfolio was \$144.4 billion at September 30, 2006, compared with \$137.8 billion at December 31, 2005, an increase of \$6.6 billion (4.8 percent). The increase in total loans was driven by growth in commercial loans, retail loans, commercial real estate loans and residential mortgages. The \$3.7 billion (8.5 percent) increase in commercial loans was primarily driven by new customer relationships and growth in corporate payment card and commercial leasing balances.

Commercial real estate loans were \$29.0 billion at September 30, 2006, an increase of \$.5 billion (1.8 percent) compared with December 31, 2005. The increase was driven by growth in construction loans, partially offset by a decrease in commercial mortgage balances.

Residential mortgages held in the loan portfolio were \$21.2 billion at September 30, 2006, an increase of \$.5 billion (2.3 percent) compared with December 31, 2005. The growth was the result of an increase in consumer finance originations, partially offset by the Company selling an increased proportion of its residential mortgage loan production in 2006.

Total retail loans outstanding, which include credit card, retail leasing, home equity and second mortgages and other retail loans, were \$47.6 billion at September 30, 2006, an increase of \$2.0 billion (4.3 percent) compared with December 31, 2005. The increase was primarily driven by growth in installment, credit card and home equity and second mortgage loans, partially offset by decreases in retail leasing balances.

**Investment Securities** Investment securities, both available-for-sale and held-to-maturity, totaled \$39.5 billion at September 30, 2006, compared with \$39.8 billion at December 31, 2005, reflecting purchases of \$5.6 billion of securities, which were more than offset by maturities and prepayments and the reclassification of \$.5 billion of principal-only securities to the trading account effective January 1, 2006, in connection with the adoption of SFAS 156. As of September 30, 2006, approximately 39 percent of the investment securities portfolio represented adjustable-rate financial instruments, compared with 41 percent at December 31, 2005. Adjustable-rate financial instruments include variable-rate collateralized mortgage obligations, mortgage-backed securities, agency securities, adjustable-rate money market accounts, asset-backed securities and floating-rate preferred stock.

**Table of Contents****Table 4** Investment Securities

September 30, 2006 (Dollars in Millions)	Available-for-Sale				Held-to-Maturity			
	Amortized Cost	Fair Value	Weighted- Average Maturity in Years	Weighted- Average Yield (d)	Amortized Cost	Fair Value	Weighted- Average Maturity in Years	Weighted- Average Yield (d)
<b>U.S. Treasury and agencies</b>								
Maturing in one year or less	\$71	\$72	.5	5.27%	\$	\$		%
Maturing after one year through five years	29	29	2.5	7.14				
Maturing after five years through ten years	24	24	6.8	6.91				
Maturing after ten years	331	324	13.9	5.98				
Total	\$455	\$449	10.7	5.99%	\$	\$		%
<b>Mortgage-backed securities (a)</b>								
Maturing in one year or less	\$346	\$345	.9	5.33%	\$	\$		%
Maturing after one year through five years	17,496	17,038	3.5	4.58	7	7	3.1	5.75
Maturing after five years through ten years	12,623	12,289	7.0	5.22				
Maturing after ten years	4,513	4,535	13.1	6.46				
Total	\$34,978	\$34,207	6.0	5.06%	\$7	\$7	3.1	5.75%
<b>Asset-backed securities (a)</b>								
Maturing in one year or less	\$7	\$7	.2	5.32%	\$	\$		%
Maturing after one year through five years								



Maturing after five years through ten years									
Maturing after ten years									
Total	\$7	\$7	.2	5.32%	\$	\$			%
<b>Obligations of state and political subdivisions (b)</b>									
Maturing in one year or less	\$53	\$53	.3	6.94%	\$3	\$3	.4	6.94%	
Maturing after one year through five years	42	43	2.2	6.83	20	21	3.0	6.24	
Maturing after five years through ten years	3,276	3,332	8.9	6.76	14	16	7.9	7.18	
Maturing after ten years	324	330	11.1	6.74	34	37	15.4	6.54	
Total	\$3,695	\$3,758	8.9	6.76%	\$71	\$77	9.8	6.59%	
<b>Other debt securities</b>									
Maturing in one year or less	\$210	\$210	.2	4.46%	\$2	\$2	.8	6.94%	
Maturing after one year through five years	1	1	3.8	10.31	10	10	2.9	5.75	
Maturing after five years through ten years	15	15	9.8	6.19	1	1	5.5	6.09	
Maturing after ten years	627	626	20.9	6.35					
Total	\$853	\$852	15.6	5.89%	\$13	\$13	2.8	5.96%	
<b>Other investments</b>	\$151	\$156		5.20%	\$	\$			%
Total investment securities (c)	\$40,139	\$39,429	6.5	5.25%	\$91	\$97	8.2	6.44%	

- (a) Information related to asset and mortgage-backed securities included above is presented based upon weighted-average maturities anticipating future prepayments.
- (b) Information related to obligations of state and political subdivisions is presented based upon yield to first optional call date if the security is purchased at a premium, yield to maturity if purchased at par or a discount.
- (c) The weighted-average maturity of the available-for-sale investment securities was 6.1 years at December 31, 2005, with a corresponding weighted-average yield of 4.89 percent. The weighted-average maturity of the held-to-maturity investment securities was 7.2 years at December 31, 2005, with a corresponding

weighted-average yield of 6.44 percent.

(d) Average yields are presented on a fully-taxable equivalent basis under a tax rate of 35 percent. Yields on available-for-sale and held-to-maturity securities are computed based on historical cost balances. Average yield and maturity calculations exclude equity securities that have no stated yield or maturity.

(Dollars in Millions)	September 30, 2006		December 31, 2005	
	Amortized Cost	Percent of Total	Amortized Cost	Percent of Total
U.S. Treasury and agencies	\$455	1.1%	\$496	1.2%
Mortgage-backed securities	34,985	87.0	38,169	94.4
Asset-backed securities	7		12	.1
Obligations of state and political subdivisions	3,766	9.4	724	1.8
Other debt securities and investments	1,017	2.5	1,029	2.5
Total investment securities	\$40,230	100.0%	\$40,430	100.0%

**Table of Contents**

**Deposits** Total deposits were \$121.0 billion at September 30, 2006, compared with \$124.7 billion at December 31, 2005, a decrease of \$3.7 billion (3.0 percent). The decrease in total deposits was primarily the result of decreases in noninterest-bearing deposits, money market savings accounts and time deposits greater than \$100,000, partially offset by increases in interest checking and time certificates of deposits less than \$100,000. The \$1.7 billion (5.2 percent) decrease in noninterest-bearing deposits primarily reflected a decline in business demand deposits as these customers reduce excess liquidity to fund business growth. The change also reflected a migration of customers to interest-bearing products given rising interest rates. The \$2.5 billion (8.8 percent) decrease in money market savings account balances reflected the Company's deposit pricing decisions for money market products in relation to other fixed-rate deposit products offered. A portion of branch-based money market savings accounts have migrated to fixed-rate time certificates to take advantage of higher interest rates for these products. Time deposits greater than \$100,000 decreased \$1.2 billion (5.2 percent) at September 30, 2006, compared with December 31, 2005, due to a decrease in corporate banking balances, partially offset by increases in consumer and private banking balances due to customer migration of deposit balances. Time deposits greater than \$100,000 are largely viewed as purchased funds and are managed at levels deemed appropriate given alternative lending sources. Time certificates of deposit less than \$100,000 increased \$.6 billion (4.2 percent) at September 30, 2006, compared with December 31, 2005. Interest checking accounts increased \$1.1 billion (4.6 percent) due to an increase in trust and custody and government balances, partially offset by decreases in consumer and private banking balances.

**Borrowings** The Company utilizes both short-term and long-term borrowings to fund growth of earning assets in excess of deposit growth. Short-term borrowings, which include federal funds purchased, commercial paper, securities sold under agreements to repurchase and other short-term borrowings, were \$24.8 billion at September 30, 2006, compared with \$20.2 billion at December 31, 2005. Short-term funding is managed within approved liquidity policies. The increase of \$4.6 billion in short-term borrowings reflected wholesale funding associated with the Company's earning asset growth and asset/liability management activities. Long-term debt was \$41.2 billion at September 30, 2006, compared with \$37.1 billion at December 31, 2005, reflecting the issuances of \$8.0 billion of medium-term and bank notes, \$2.5 billion of junior subordinated debentures and the addition of \$2.8 billion of Federal Home Loan Bank advances, partially offset by \$8.2 billion of medium-term and bank note maturities and repayments, and \$.7 billion of junior subordinated debentures repayments. Refer to the Liquidity Risk Management section for discussion of liquidity management of the Company.

**CORPORATE RISK PROFILE**

**Overview** Managing risks is an essential part of successfully operating a financial services company. The most prominent risk exposures are credit, residual, operational, interest rate, market and liquidity risk. Credit risk is the risk of not collecting the interest and/or the principal balance of a loan or investment when it is due. Residual risk is the potential reduction in the end-of-term value of leased assets or the residual cash flows related to asset securitization and other off-balance sheet structures. Operational risk includes risks related to fraud, legal and compliance risk, processing errors, technology, breaches of internal controls and business continuation and disaster recovery risk. Interest rate risk is the potential reduction of net interest income as a result of changes in interest rates. Rate movements can affect the repricing of assets and liabilities differently, as well as their market value. Market risk arises from fluctuations in interest rates, foreign exchange rates, and equity prices that may result in changes in the values of financial instruments, such as trading and available-for-sale securities that are accounted for on a mark-to-market basis. Liquidity risk is the possible inability to fund obligations to depositors, investors or borrowers. In addition, corporate strategic decisions, as well as the risks described above, could give rise to reputation risk. Reputation risk is the risk that negative publicity or press, whether true or not, could result in costly litigation or cause a decline in the Company's stock value, customer base or revenue.

**Table of Contents****Table 5** Delinquent Loan Ratios as a Percent of Ending Loan Balances

	September 30, 2006	December 31, 2005
90 days or more past due <b>excluding</b> nonperforming loans		
<b>Commercial</b>		
Commercial	.07%	.06%
Lease financing		
Total commercial	.06	.05
<b>Commercial real estate</b>		
Commercial mortgages	.01	
Construction and development	.01	
Total commercial real estate	.01	
<b>Residential mortgages</b>	.36	.32
<b>Retail</b>		
Credit card	1.59	1.26
Retail leasing	.03	.04
Other retail	.19	.22
Total retail	.40	.36
Total loans	.20%	.18%

	September 30, 2006	December 31, 2005
90 days or more past due <b>including</b> nonperforming loans		
Commercial	.55%	.69%
Commercial real estate	.54	.55
Residential mortgages (a)	.53	.55
Retail	.51	.50
Total loans	.53%	.58%

(a) *Delinquent loan ratios exclude advances made pursuant to servicing agreements to Government National Mortgage Association ( GNMA ) mortgage pools whose repayments are insured by the Federal Housing Administration or guaranteed by the Department of Veterans Affairs. Including the guaranteed amounts, the ratio of residential mortgages 90 days or more past due was 2.78 percent at September 30, 2006, and 4.35 percent at December 31, 2005.*

**Credit Risk Management** The Company's strategy for credit risk management includes well-defined, centralized credit policies, uniform underwriting criteria, and ongoing risk monitoring and review processes for all commercial and consumer credit exposures. The strategy also emphasizes diversification on a geographic, industry and customer level, regular credit examinations and management reviews of loans experiencing deterioration of credit quality. The credit risk management strategy also includes a credit risk assessment process, independent of business line managers, that performs assessments of compliance with commercial and consumer credit policies, risk ratings, and other critical

credit information. The Company strives to identify potential problem loans early, take any necessary charge-offs promptly and maintain adequate reserve levels for probable loan losses inherent in the portfolio.

In evaluating its credit risk, the Company considers changes, if any, in underwriting activities, the loan portfolio composition (including product mix and geographic, industry or customer-specific concentrations), trends in loan performance, the level of allowance coverage relative to similar banking institutions and macroeconomic factors. Economic conditions during the third quarter and first nine months of 2006 have improved from the same periods of 2005, as reflected in strong expansion of the gross domestic product index, lower unemployment rates, favorable trends related to corporate profits and consumer spending for retail goods and services. Current economic conditions are relatively unchanged from December 31, 2005. Through the second quarter of 2006, the Federal Reserve Bank continued increasing short-term interest rates in an effort to prevent an acceleration of inflation and maintain the current rate of economic growth. Beginning in the third quarter of 2006, the Federal Reserve Bank paused from its policies of increasing interest rates and tightening the money supply.

Refer to Management's Discussion and Analysis - Credit Risk Management in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for a more detailed discussion on credit risk management processes.

***Loan Delinquencies*** Trends in delinquency ratios represent an indicator, among other considerations, of credit risk within the Company's loan portfolios. The entire balance of the account is considered delinquent if the minimum payment contractually required to be made is not received by the specified date on the billing statement. The Company measures delinquencies, both

**Table of Contents**

including and excluding nonperforming loans, to enable comparability with other companies. Accruing loans 90 days or more past due increased \$42 million to \$295 million at September 30, 2006, compared with \$253 million at December 31, 2005, due to the seasoning of the residential mortgage portfolio originated by the consumer finance division and the continued return to normalized delinquency levels after the bankruptcy legislation change that occurred in the fourth quarter of 2005. These loans are not included in nonperforming assets and continue to accrue interest because they are adequately secured by collateral, and/or are in the process of collection and are reasonably expected to result in repayment or restoration to current status. The ratio of delinquent loans to total loans was .20 percent at September 30, 2006, compared with .18 percent at December 31, 2005.

To monitor credit risk associated with retail loans, the Company monitors delinquency ratios in the various stages of collection including nonperforming status.

The following table provides summary delinquency information for residential mortgages and retail loans:

(Dollars in Millions)	Amount		As a Percent of Ending Loan Balances	
	September 30, 2006	December 31, 2005	September 30, 2006	December 31, 2005
<b>Residential mortgages</b>				
30-89 days	\$129	\$112	.61%	.55%
90 days or more	76	67	.36	.32
Nonperforming	36	48	.17	.23
<b>Total</b>	<b>\$241</b>	<b>\$227</b>	<b>1.14%</b>	<b>1.10%</b>
<b>Retail</b>				
<b>Credit card</b>				
30-89 days	\$168	\$147	2.14%	2.06%
90 days or more	125	90	1.59	1.26
Nonperforming	37	49	.47	.69
<b>Total</b>	<b>\$330</b>	<b>\$286</b>	<b>4.20%</b>	<b>4.01%</b>
<b>Retail leasing</b>				
30-89 days	\$30	\$43	.42%	.59%
90 days or more	2	3	.03	.04
Nonperforming				
<b>Total</b>	<b>\$32</b>	<b>\$46</b>	<b>.45%</b>	<b>.63%</b>
<b>Other retail</b>				
30-89 days	\$187	\$206	.57%	.66%
90 days or more	62	70	.19	.22
Nonperforming	16	17	.05	.06
<b>Total</b>	<b>\$265</b>	<b>\$293</b>	<b>.81%</b>	<b>.94%</b>

**Nonperforming Assets** The level of nonperforming assets represents another indicator of the potential for future credit losses. Nonperforming assets include nonaccrual loans, restructured loans not performing in accordance with modified terms, other real estate and other nonperforming assets owned by the Company. Interest payments collected from

assets on nonaccrual status are typically applied against the principal balance and not recorded as income. At September 30, 2006, total nonperforming assets were \$575 million, compared with \$644 million at December 31, 2005. The ratio of total nonperforming assets to total loans and other real estate decreased to .40 percent at September 30, 2006, compared with .47 percent at December 31, 2005.

Included in nonperforming loans were restructured loans of \$43 million at September 30, 2006, compared with \$75 million at December 31, 2005. At September 30, 2006, the Company had no commitments to lend additional funds under restructured loans, compared to commitments of \$9 million at December 31, 2005.

**Table of Contents****Table 6** Nonperforming Assets (a)

(Dollars in Millions)	September 30, 2006	December 31, 2005
<b>Commercial</b>		
Commercial	\$192	\$231
Lease financing	39	42
Total commercial	231	273
<b>Commercial real estate</b>		
Commercial mortgages	114	134
Construction and development	40	23
Total commercial real estate	154	157
<b>Residential mortgages</b>	36	48
<b>Retail</b>		
Credit card	37	49
Retail leasing		
Other retail	16	17
Total retail	53	66
Total nonperforming loans	474	544
<b>Other real estate (b)</b>	79	71
<b>Other assets</b>	22	29
Total nonperforming assets	\$575	\$644
Accruing loans 90 days or more past due	\$295	\$253
Nonperforming loans to total loans	.33%	.39%
Nonperforming assets to total loans plus other real estate (b)	.40%	.47%

**Changes in Nonperforming Assets**

(Dollars in Millions)	Commercial and Commercial Real Estate	Retail and Residential Mortgages (d)	Total
<b>Balance December 31, 2005</b>	\$457	\$187	\$644
Additions to nonperforming assets			
New nonaccrual loans and foreclosed properties	334	41	375
Advances on loans	30		30
Total additions	364	41	405
Reductions in nonperforming assets			
Paydowns, payoffs	(210)	(41)	(251)



Net sales	(21)		(21)
Return to performing status	(92)	(6)	(98)
Charge-offs (c)	(93)	(11)	(104)
Total reductions	(416)	(58)	(474)
Net additions to (reductions in) nonperforming assets	(52)	(17)	(69)
<b>Balance September 30, 2006</b>	<b>\$405</b>	<b>\$170</b>	<b>\$575</b>

- (a) Throughout this document, nonperforming assets and related ratios do not include accruing loans 90 days or more past due.
- (b) Excludes \$85 million of foreclosed GNMA loans which continue to accrue interest.
- (c) Charge-offs exclude actions for certain card products and loan sales that were not classified as nonperforming at the time the charge-off occurred.
- (d) Residential mortgage information excludes changes related to residential mortgages serviced by others.

**Restructured Loans Accruing Interest** On a case-by-case basis, management determines whether an account that experiences financial difficulties should be modified as to its interest rate or repayment terms to maximize the Company's collection of its balance.

Loans restructured at a rate equal to or greater than that of a new loan with comparable risk at the time the contract is modified are excluded from restructured loans once repayment performance, in accordance with the modified agreement, has been demonstrated over several payment cycles. Loans that have interest rates reduced below comparable market rates remain classified as restructured loans; however, interest income is accrued at the reduced rate as long as the customer complies with the revised terms and conditions.

**Table of Contents**

The following table provides a summary of restructured loans that continue to accrue interest:

(Dollars in Millions)	Amount		As a Percent of Ending Loan Balances	
	September 30, 2006	December 31, 2005	September 30, 2006	December 31, 2005
Commercial	\$19	\$5	.04%	.01%
Commercial real estate	1	1		
Residential mortgages	76	59	.36	.28
Credit card	236	218	3.00	3.05
Other retail	37	32	.09	.08
Total	\$369	\$315	.26%	.23%

Restructured loans that continue to accrue interest were higher at September 30, 2006, compared with December 31, 2005, reflecting the impact of the Company implementing higher minimum balance payment requirements for credit card customers in response to industry guidance issued by the banking regulatory agencies. **Analysis of Loan Net Charge-Offs** Total loan net charge-offs were \$135 million and \$375 million during the third quarter and first nine months of 2006, respectively, compared with net charge-offs of \$156 million and \$472 million, respectively, for the same periods of 2005. The ratio of total loan net charge-offs to average loans in the third quarter and first nine months of 2006 was .37 percent and .36 percent, respectively, compared with .46 percent and .48 percent, respectively, for the same periods of 2005.

Commercial and commercial real estate loan net charge-offs for the third quarter of 2006 were \$21 million (.11 percent of average loans outstanding), compared with \$23 million (.13 percent of average loans outstanding) for the third quarter of 2005. Commercial and commercial real estate loan net charge-offs for the first nine months of 2006 were \$55 million (.10 percent of average loans outstanding), compared with \$69 million (.13 percent of average loans outstanding) for the first nine months of 2005. The decrease in net charge-offs reflected lower gross charge-offs, partially offset by a lower level of recoveries as compared with the same periods of the prior year. The Company expects commercial net charge-offs to increase somewhat over the next several quarters due to an increase in gross chargeoffs from cyclical lows and declining commercial loan recoveries.

Retail loan net charge-offs for the third quarter of 2006 were \$103 million (.87 percent of average loans outstanding), compared with \$124 million (1.09 percent of average loans outstanding) for the third quarter of 2005. Retail loan net charge-offs for the first nine months of 2006 were \$291 million (.84 percent of average loans outstanding), compared with \$377 million (1.14 percent of average loans outstanding) for the first nine months of 2005. The decrease in retail loan net charge-offs reflected the impact of the bankruptcy legislation change that occurred in the fourth quarter of 2005 and improved retail portfolio performance. The Company anticipates that bankruptcy charge-offs will return to more normalized levels during the next several quarters.

The Company's retail lending business utilizes several distinct business processes and channels to

**Table 7** Net Charge-offs as a Percent of Average Loans Outstanding

		Three Months Ended	Nine Months Ended		
		September 30,	September 30,		
		2006	2005	2006	2005

<b>Commercial</b>				
Commercial	.18%	.07%	.12%	.11%
Lease financing	.23	1.29	.44	.95
Total commercial	.18	.21	.16	.21
<b>Commercial real estate</b>				
Commercial mortgages		.04	.01	.05
Construction and development		(.10)	.02	(.05)
Total commercial real estate			.01	.02
<b>Residential mortgages</b>	.21	.19	.18	.20
<b>Retail</b>				
Credit card	2.85	3.74	2.74	3.92
Retail leasing	.22	.27	.19	.33
Home equity and second mortgages	.31	.37	.33	.42
Other retail	.72	1.04	.74	1.05
Total retail	.87	1.09	.84	1.14
Total loans	.37%	.46%	.36%	.48%

**Table of Contents**

originate retail credit including traditional branch lending, indirect lending and a consumer finance division. Each distinct underwriting and origination activity manages unique credit risk characteristics and prices its loan production commensurate with the differing risk profiles. Within Consumer Banking, U.S. Bank Consumer Finance ( USBCF ) participates in substantially all facets of the Company s consumer lending activities. USBCF specializes in serving channel-specific and alternative lending markets in residential mortgages, home equity and installment loan financing. USBCF manages loans originated through a broker network, correspondent relationships and U.S. Bank branch offices. Generally, loans managed by the Company s consumer finance division exhibit higher credit risk characteristics, but are priced commensurate with the differing risk profile. The following table provides an analysis of net charge-offs as a percent of average loans outstanding managed by the consumer finance division, compared with traditional branch related loans:

(Dollars in Millions)	Three Months Ended September 30,				Nine Months Ended September 30,			
	Average Loan Amount		Percent of Average Loans		Average Loan Amount		Percent of Average Loans	
	2006	2005	2006	2005	2006	2005	2006	2005
<b>Consumer Finance (a)</b>								
Residential mortgages	\$7,627	\$6,292	.52%	.50%	\$7,245	\$5,734	.48%	.51%
Home equity and second mortgages	1,939	2,363	1.43	1.68	1,993	2,523	1.48	1.64
Other retail	397	400	5.00	4.96	401	390	4.67	4.80
<b>Traditional Branch</b>								
Residential mortgages	\$13,491	\$12,449	.03%	.03%	\$13,747	\$11,532	.03%	.05%
Home equity and second mortgages	13,227	12,621	.15	.13	13,054	12,421	.15	.17
Other retail	16,575	15,563	.62	.94	16,313	14,935	.64	.95
<b>Total Company</b>								
Residential mortgages	\$21,118	\$18,741	.21%	.19%	\$20,992	\$17,266	.18%	.20%
Home equity and second mortgages	15,166	14,984	.31	.37	15,047	14,944	.33	.42
Other retail	16,972	15,963	.72	1.04	16,714	15,325	.74	1.05

(a) Consumer finance category included credit originated and managed by USBCF, as well as home equity and second mortgages with a loan-to-value greater than 100 percent that were originated in the branches.

**Analysis and Determination of the Allowance for Credit Losses** The allowance for loan losses provides coverage for probable and estimable losses inherent in the Company s loan and lease portfolio. Management evaluates the allowance each quarter to determine that it is adequate to cover these inherent losses. The evaluation of each element and the overall allowance is based on a continuing assessment of problem loans, recent loss experience and other factors, including regulatory guidance and economic conditions. Because business processes and credit risks associated with unfunded credit commitments are essentially the same as for loans, the Company utilizes similar processes to estimate its liability for unfunded credit commitments, which is included in other liabilities in the Consolidated Balance Sheet. Both the allowance for loan losses and the liability for unfunded credit commitments are included in the Company s analysis of the allowance for credit losses.

At September 30, 2006, the allowance for credit losses was \$2,256 million (1.56 percent of loans), compared with an allowance of \$2,251 million (1.63 percent of loans) at December 31, 2005. The ratio of the allowance for credit losses to nonperforming loans was 476 percent at September 30, 2006, compared with 414 percent at December 31,

2005. The ratio of the allowance for credit losses to annualized loan net charge-offs was 421 percent at September 30, 2006, compared with 329 percent at December 31, 2005.

**14**

U.S. Bancorp

---

**Table of Contents****Table 8** Summary of Allowance for Credit Losses

(Dollars in Millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Balance at beginning of period	\$2,251	\$2,269	\$2,251	\$2,269
<b>Charge-offs</b>				
Commercial				
Commercial	34	37	86	111
Lease financing	12	24	37	62
Total commercial	46	61	123	173
Commercial real estate				
Commercial mortgages	1	5	7	15
Construction and development			1	3
Total commercial real estate	1	5	8	18
Residential mortgages	12	10	31	28
Retail				
Credit card	65	71	178	217
Retail leasing	6	8	19	27
Home equity and second mortgages	14	19	46	59
Other retail	51	55	141	160
Total retail	136	153	384	463
Total charge-offs	195	229	546	682
<b>Recoveries</b>				
Commercial				
Commercial	16	30	50	81
Lease financing	9	8	20	27
Total commercial	25	38	70	108
Commercial real estate				
Commercial mortgages	1	3	6	8
Construction and development		2		6
Total commercial real estate	1	5	6	14
Residential mortgages	1	1	2	2
Retail				
Credit card	9	8	26	25
Retail leasing	2	3	9	9
Home equity and second mortgages	2	5	9	12
Other retail	20	13	49	40
Total retail	33	29	93	86

Total recoveries	60	73	171	210
<b>Net Charge-offs</b>				
<b>Commercial</b>				
Commercial	18	7	36	30
Lease financing	3	16	17	35
Total commercial	21	23	53	65
<b>Commercial real estate</b>				
Commercial mortgages		2	1	7
Construction and development		(2)	1	(3)
Total commercial real estate			2	4
Residential mortgages	11	9	29	26
<b>Retail</b>				
Credit card	56	63	152	192
Retail leasing	4	5	10	18
Home equity and second mortgages	12	14	37	47
Other retail	31	42	92	120
Total retail	103	124	291	377
Total net charge-offs	135	156	375	472
Provision for credit losses	135	145	375	461
Acquisitions and other changes	5		5	
Balance at end of period	\$2,256	\$2,258	\$2,256	\$2,258
<b>Components</b>				
Allowance for loan losses	\$2,034	\$2,055		
Liability for unfunded credit commitments	222	203		
Total allowance for credit losses	\$2,256	\$2,258		
<b>Allowance for credit losses as a percentage of</b>				
Period-end loans	1.56%	1.65%		
Nonperforming loans	476	413		
Nonperforming assets	392	351		
Annualized net charge-offs	421	365		

**Table of Contents**

Several factors were taken into consideration in evaluating the allowance for credit losses at September 30, 2006, including the risk profile of the portfolios and loan net charge-offs during the period, the level of nonperforming assets, accruing loans 90 days or more past due, delinquency ratios and changes in restructured loan balances compared with December 31, 2005. Management also considered the uncertainty related to certain industry sectors, including the airline industry, and the extent of credit exposure to other borrowers within the portfolio. In addition, concentration risks associated with commercial real estate and the mix of loans, including credit cards, loans originated through the consumer finance division and residential mortgages, and their relative credit risk were evaluated. Finally, the Company considered current economic conditions that might impact the portfolio.

**Residual Risk Management** The Company manages its risk to changes in the residual value of leased assets through disciplined residual valuation setting at the inception of a lease, diversification of its leased assets, regular residual asset valuation reviews and monitoring of residual value gains or losses upon the disposition of assets. As of September 30, 2006, no significant change in the amount of residuals or concentration of the portfolios has occurred since December 31, 2005. Refer to Management's Discussion and Analysis - Residual Risk Management in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for further discussion on residual risk management.

**Operational Risk Management** The Company manages operational risk through a risk management framework and its internal control processes. Within this framework, the Corporate Risk Committee ( Risk Committee ) provides oversight and assesses the most significant operational risks facing the Company within its business lines. Under the guidance of the Risk Committee, enterprise risk management personnel establish policies and interact with business lines to monitor significant operational risks on a regular basis. Business lines have direct and primary responsibility and accountability for identifying, controlling, and monitoring operational risks embedded in their business activities. Refer to Management's Discussion and Analysis - Operational Risk Management in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for further discussion on operational risk management.

**Interest Rate Risk Management** In the banking industry, changes in interest rates is a significant risk that can impact earnings, market valuations and safety and soundness of the entity. To minimize the volatility of net interest income and the market value of assets and liabilities, the Company manages its exposure to changes in interest rates through asset and liability management activities within guidelines established by its Asset Liability Policy Committee ( ALPC ) and approved by the Board of Directors. ALPC has the responsibility for approving and ensuring compliance with ALPC management policies, including interest rate risk exposure. The Company uses Net Interest Income Simulation Analysis and Market Value of Equity Modeling for measuring and analyzing consolidated interest rate risk.

**Net Interest Income Simulation Analysis** One of the primary tools used to measure interest rate risk and the effect of interest rate changes on net interest income is simulation analysis. Through this simulation, management estimates the impact on net interest income of a 200 basis point upward or downward gradual change of market interest rates over a one-year period. This represents a change, effective in the first quarter of 2006, from a previous policy of estimating the effect of a 300 basis point upward or downward gradual change on net interest income. The simulation also estimates the effect of immediate and sustained parallel shifts in the yield curve of 50 basis points as well as the effect of immediate and sustained flattening or steepening of the yield curve.

Refer to Management's Discussion and Analysis - Net Interest Income Simulation Analysis in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for further discussion on net interest income simulation analysis.



**Table of Contents**

## Sensitivity of Net Interest Income:

	September 30, 2006				December 31, 2005			
	Down 50 Immediate	Up 50 Immediate	Down 200 Gradual	Up 200 Gradual	Down 50 Immediate	Up 50 Immediate	Down 200 Gradual*	Up 200 Gradual*
Net interest income	1.14%	(1.10)%	2.35%	(2.85)%	.66%	(.73)%	1.19%	(2.60)%

\* As of January 31, 2006, due to the change to a 200 basis point gradual change policy during the first quarter of 2006.

The table above summarizes the interest rate risk of net interest income based on forecasts over the succeeding 12 months. At September 30, 2006, the Company's overall interest rate risk position was liability sensitive to changes in interest rates. The Company manages the overall interest rate risk profile within policy limits. ALPC policy guidelines limit the estimated change in net interest income to 3.0 percent of forecasted net interest income over the succeeding 12 months. At September 30, 2006, and December 31, 2005, the Company was within its policy guidelines.

**Market Value of Equity Modeling** The Company also utilizes the market value of equity as a measurement tool in managing interest rate sensitivity. The market value of equity measures the degree to which the market values of the Company's assets and liabilities and off-balance sheet instruments will change given a change in interest rates. ALPC guidelines limit the change in market value of equity in a 200 basis point parallel rate shock to 15 percent of the market value of equity assuming interest rates at September 30, 2006. The up 200 basis point scenario resulted in a 5.4 percent decrease in the market value of equity at September 30, 2006, compared with a 6.8 percent decrease at December 31, 2005. The down 200 basis point scenario resulted in a 4.2 percent decrease in the market value of equity at September 30, 2006, compared with a 4.1 percent decrease at December 31, 2005. At September 30, 2006, and December 31, 2005, the Company was within its policy guidelines.

The Company also uses duration of equity as a measure of interest rate risk. The duration of equity is a measure of the net market value sensitivity of the assets, liabilities and derivative positions of the Company. The duration of assets was 1.8 years at September 30, 2006, compared with 1.6 years at December 31, 2005. The duration of liabilities was 2.0 years at September 30, 2006, compared with 1.6 years at December 31, 2005. At September 30, 2006, the duration of equity was .9 years, compared with 1.8 years at December 31, 2005. The duration of equity measure shows that sensitivity of the market value of equity of the Company was liability sensitive to changes in interest rates. Refer to Management's Discussion and Analysis - Market Value of Equity Modeling in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for further discussion on market value of equity modeling.

**Use of Derivatives to Manage Interest Rate Risk** In the ordinary course of business, the Company enters into derivative transactions to manage its interest rate, prepayment, credit and foreign currency risks (asset and liability management positions) and to accommodate the business requirements of its customers (customer-related positions). Refer to Management's Discussion and Analysis - Use of Derivatives to Manage Interest Rate Risk in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for further discussion on the use of derivatives to manage interest rate risk.

By their nature, derivative instruments are subject to market risk. The Company does not utilize derivative instruments for speculative purposes. Of the Company's \$32.6 billion of total notional amount of asset and liability management derivative positions at September 30, 2006, \$23.5 billion was designated as either fair value or cash flow hedges or net investment hedges of foreign operations. The cash flow hedge derivative positions are interest rate swaps that hedge the forecasted cash flows from the underlying variable-rate LIBOR loans and floating-rate debt. The fair value hedges are primarily interest rate swaps that hedge the change in fair value related to interest rate changes of underlying fixed-rate debt and subordinated obligations.

In addition, the Company uses forward commitments to sell residential mortgage loans to hedge its interest rate risk related to residential mortgage loans held for sale. Related to its mortgage banking operations, the Company held \$2.3 billion of forward commitments to sell mortgage loans and \$1.6 billion of unfunded mortgage loan commitments that were derivatives in accordance with the provisions of the Statement of Financial Accounting Standards No. 133,

Accounting for Derivative Instruments and Hedge Activities. The unfunded mortgage loan commitments are reported at fair value as options in Table 9. Beginning in March 2006, the Company entered into U.S. Treasury futures and options on U.S. Treasury futures contracts to hedge the change in fair value related to the election of fair value measurement for its residential MSRs.

U.S. Bancorp

17

---

**Table of Contents**

At September 30, 2006, the Company had \$95 million in accumulated other comprehensive income related to realized and unrealized losses on derivatives classified as cash flow hedges. Unrealized gains and losses are reflected in earnings when the related cash flows or hedged transactions occur and offset the related performance of the hedged items. The estimated amount to be reclassified from accumulated other comprehensive income into earnings during the remainder of 2006 and the next 12 months is a loss of \$7 million and \$32 million, respectively.

Gains or losses on customer-related derivative positions were not material for the third quarter and first nine months of 2006. The change in fair value of forward commitments attributed to hedge ineffectiveness recorded in noninterest income was a decrease of \$2 million and \$3 million for the third quarter and first nine months of 2006, respectively. The change in the fair value of all other asset and liability management derivative positions attributed to hedge ineffectiveness recorded in noninterest income was not material for the third quarter and first nine months of 2006.

The Company enters into derivatives to protect its net investment in certain foreign operations. The Company uses forward commitments to sell specified amounts of certain foreign currencies to hedge its capital volatility risk associated with fluctuations in foreign currency exchange rates. The net amount of gains or losses included in the cumulative translation adjustment for the third quarter and first nine months of 2006 was not material.

**Table 9** Derivative Positions

(Dollars in Millions)	September 30, 2006			December 31, 2005		
	Notional Amount	Fair Value	Weighted-Average Remaining Maturity In Years	Notional Amount	Fair Value	Weighted-Average Remaining Maturity In Years

**Asset and Liability Management Positions**

Interest rate contracts						
Receive fixed/pay floating swaps	\$6,610	\$13	22.36	\$16,370	\$(82)	7.79
Pay fixed/receive floating swaps	11,998	4	2.42	9,163	139	1.33
Futures and forwards						
Buy	3		.11	104		.07
Sell	6,469	(49)	.15	2,669	(15)	.09
Options						
Written	7,007	7	.12	1,086	3	.08
Foreign exchange contracts						
Cross-currency swaps	403	27	8.87	387	11	9.61
Forwards	16		.07	404	7	.05
Equity contracts	74	4	3.38	42	3	3.29
Credit default swaps	25		4.98			

**Customer-related Positions**

Interest rate contracts						
Receive fixed/pay floating swaps	\$10,499	\$(47)	5.33	\$9,753	\$(69)	5.25
Pay fixed/receive floating swaps	10,468	104	5.42	9,707	121	5.25
Options						

Purchased	1,877	4	2.00	1,453	6	2.26
Written	1,865	(3)	2.00	1,453	(5)	2.26
Risk participation agreements (a)						
Purchased	177		7.05	143		8.02
Written	320	(1)	6.26	169		4.64
Foreign exchange rate contracts						
Forwards and swaps						
Buy	1,954	47	.40	2,042	77	.43
Sell	1,918	(39)	.41	2,018	(73)	.46
Options						
Purchased	104	(1)	.40	56	1	.24
Written	104	1	.40	56	(1)	.24

(a) At September 30, 2006, the credit equivalent amount was \$2 million and \$45 million, compared with \$1 million and \$18 million at December 31, 2005, for purchased and written risk participation agreements, respectively.

**Table of Contents**

**Market Risk Management** In addition to interest rate risk, the Company is exposed to other forms of market risk as a consequence of conducting normal trading activities. Business activities that contribute to market risk include primarily residential mortgage related risks, but also other items, such as proprietary trading and foreign exchange positions. Value at Risk ( VaR ) is a key measure of market risk for the Company. Theoretically, VaR represents the maximum amount that the Company has placed at risk of loss, with a ninety-ninth percentile degree of confidence, to adverse market movements in the course of its risk taking activities. Due to the election of fair value measurement of its residential MSRs and related hedging strategy in the first quarter of 2006, the Company increased its VaR limit to \$40 million at March 31, 2006, compared with \$20 million at December 31, 2005. The Company's market valuation risk, as estimated by the VaR analysis, was \$25 million at September 30, 2006, compared with \$1 million at December 31, 2005. Refer to Management's Discussion and Analysis Market Risk Management in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for further discussion on market risk management.

**Liquidity Risk Management** ALPC establishes policies, as well as analyzes and manages liquidity, to ensure that adequate funds are available to meet normal operating requirements in addition to unexpected customer demands for funds, such as high levels of deposit withdrawals or loan demand, in a timely and cost-effective manner. Liquidity management is viewed from long-term and short-term perspectives, as well as from an asset and liability perspective. Management monitors liquidity through a regular review of maturity profiles, funding sources, and loan and deposit forecasts to minimize funding risk. Refer to Management's Discussion and Analysis Liquidity Risk Management in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for further discussion on liquidity risk management.

The Company's ability to raise negotiated funding at competitive prices is influenced by rating agencies' views of the Company's credit quality, liquidity, capital and earnings. On October 26, 2006, Dominion Bond Rating Service upgraded the Company's senior and unsecured subordinated debt ratings to AA and AA(low), respectively, from AA(low) and A(high), respectively. On November 1, 2006, Standard & Poor's Ratings Services changed its credit ratings outlook for the Company to Positive . At November 1, 2006, the credit ratings outlook for the Company was considered Positive by Fitch and Stable by Moody's Investors Service and Dominion Bond Ratings Service.

At September 30, 2006, parent company long-term debt outstanding was \$13.9 billion, compared with \$10.9 billion at December 31, 2005. The \$3.0 billion increase was primarily due to the issuances of \$2.5 billion of junior subordinated debentures and \$4.0 billion of medium-term notes, offset by long-term debt maturities and repayments during the first nine months of 2006. As of September 30, 2006, there was no parent company debt scheduled to mature in the remainder of 2006.

Federal banking laws regulate the amount of dividends that may be paid by banking subsidiaries without prior approval. The amount of dividends available to the parent company from its banking subsidiaries after meeting the regulatory capital requirements for well-capitalized banks was approximately \$1.2 billion at September 30, 2006.

**Off-Balance Sheet Arrangements** Off-balance sheet arrangements include any contractual arrangement to which an unconsolidated entity is a party, under which the Company has an obligation to provide credit or liquidity enhancements or market risk support. Off-balance sheet arrangements include certain defined guarantees, asset securitization trusts and conduits. Off-balance sheet arrangements also include any obligation under a variable interest held by an unconsolidated entity that provides financing, liquidity, credit enhancement or market risk support.

In the ordinary course of business, the Company enters into various forms of guarantees that may be considered off-balance sheet arrangements. The extent of these arrangements is provided in Note 10 of the Notes to Consolidated Financial Statements.

Asset securitizations and conduits represent a source of funding for the Company through off-balance sheet structures. The Company sponsors an off-balance sheet conduit to which it transferred high-grade investment securities, funded by the issuance of commercial paper. The conduit held assets and related commercial paper liabilities of \$2.7 billion at September 30, 2006, and \$3.8 billion at December 31, 2005. The Company provides a liquidity facility to the conduit. A liability for the estimate of the potential risk of loss for the Company as the liquidity facility provider is recorded on the balance sheet in other liabilities and was \$13 million at September 30, 2006, and \$20 million at December 31, 2005. In addition, the Company recorded at fair value its retained residual interest in the

investment securities conduit of \$19 million at September 30, 2006, and \$28 million at December 31, 2005.

U.S. Bancorp

**19**

---

**Table of Contents****Table 10** Capital Ratios

(Dollars in Millions)	September 30, 2006	December 31, 2005
Tier 1 capital	\$17,042	\$15,145
As a percent of risk-weighted assets	8.8%	8.2%
As a percent of adjusted quarterly average assets (leverage ratio)	8.3%	7.6%
Total risk-based capital	\$25,011	\$23,056
As a percent of risk-weighted assets	13.0%	12.5%
Tangible common equity	\$11,286	\$11,873
As a percent of tangible assets	5.4%	5.9%

The Company does not rely significantly on off-balance sheet arrangements for liquidity or capital resources. Refer to Management's Discussion and Analysis - Off-Balance Sheet Arrangements in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for further discussion on off-balance sheet arrangements.

**Capital Management** The Company is committed to managing capital for maximum shareholder benefit and maintaining strong protection for depositors and creditors. The Company has targeted returning 80 percent of earnings to its common shareholders through a combination of dividends and share repurchases. In the first nine months of 2006, the Company returned 120 percent of earnings. The Company continually assesses its business risks and capital position. The Company also manages its capital to exceed regulatory capital requirements for well-capitalized bank holding companies. To achieve these capital goals, the Company employs a variety of capital management tools including dividends, common share repurchases, and the issuance of subordinated debt and other capital instruments. Total shareholders' equity was \$20.9 billion at September 30, 2006, compared with \$20.1 billion at December 31, 2005. The increase was the result of corporate earnings and the issuance of \$1.0 billion of non-cumulative, perpetual preferred stock on March 27, 2006, partially offset by share repurchases and dividends.

Table 10 provides a summary of capital ratios as of September 30, 2006, and December 31, 2005. Tier 1 capital at September 30, 2006, was positively affected by the \$1.0 billion issuance of preferred stock and the \$2.5 billion issuance of junior subordinated debentures during the first nine months of 2006. All regulatory ratios continue to be in excess of regulatory well-capitalized requirements.

On December 21, 2004, the Board of Directors approved and announced an authorization to repurchase 150 million shares of common stock during the next 24 months. During 2006, the Company repurchased 62 million shares under this authorization.

On August 3, 2006, the Company announced that the Board of Directors approved an authorization to repurchase 150 million shares of common stock through December 31, 2008. This new authorization replaced the December 21, 2004, share repurchase program. The Company purchased 18 million shares under this authorization during the third quarter of 2006.

The following table provides a detailed analysis of all shares repurchased during the third quarter of 2006:

Time Period	Total Number of Shares Purchased as Part of Publicly Announced Programs	Average Price Paid	Maximum Number of Shares that May Yet Be Purchased Under the Programs

			per Share	
July 1	July 31 (a)	8,755,561	\$31.80	24,097,204
August 1	August 31 (b)	14,905,110	32.20	137,494,890
September 1	September 30 (c)	5,773,647	33.01	131,721,243
	Total	29,434,318	\$32.24	131,721,243

- (a) *All shares purchased during July of 2006 were purchased under the publicly announced December 21, 2004, authorization.*
- (b) *During August of 2006, 2.4 million shares were purchased under the publicly announced December 21, 2004, authorization and 12.5 million shares were purchased under the publicly announced August 3, 2006, authorization.*
- (c) *All shares purchased during September of 2006 were purchased under the publicly announced August 3, 2006, authorization.*



**Table of Contents****LINE OF BUSINESS FINANCIAL REVIEW**

Within the Company, financial performance is measured by major lines of business, which include Wholesale Banking, Consumer Banking, Wealth Management, Payment Services, and Treasury and Corporate Support. These operating segments are components of the Company about which financial information is available and is evaluated regularly in deciding how to allocate resources and assess performance.

**Basis for Financial Presentation** Business line results are derived from the Company's business unit profitability reporting systems by specifically attributing managed balance sheet assets, deposits and other liabilities and their related income or expense. Refer to Management's Discussion and Analysis - Line of Business Financial Review in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for further discussion on the business lines' basis for financial presentation.

Designations, assignments and allocations change from time to time as management systems are enhanced, methods of evaluating performance or product lines change or business segments are realigned to better respond to the Company's diverse customer base. During 2006, certain organization and methodology changes were made and, accordingly, 2005 results were restated and presented on a comparable basis, including a change in the allocation of risk adjusted capital to the business lines. Business lines are allocated risk adjusted capital based upon economic capital requirements, regulatory capital requirements, goodwill and intangibles. The allocations to the business lines are equal to the capital that is held by the Company. The capital allocations include credit and operational capital allocations which are performed using a Basel II approach with adjustments for regulatory Tier I leverage requirements.

**Wholesale Banking** offers lending, depository, treasury management and other financial services to middle market, large corporate, commercial real estate, equipment finance, small-ticket leasing and public sector clients, along with lending guaranteed by the Small Business Administration. Wholesale Banking contributed \$298 million of the Company's net income in the third quarter and \$907 million in the first nine months of 2006, or increases of \$11 million and \$41 million, respectively, compared with the same periods of 2005. The increases were primarily driven by growth in total net revenue.

Total net revenue increased \$15 million (2.2 percent) in the third quarter and \$60 million (2.9 percent) in the first nine months of 2006, compared with the same periods of 2005. Net interest income, on a taxable-equivalent basis, increased \$2 million in the third quarter and \$40 million in the first nine months of 2006, compared with the same periods of 2005. The increases in net interest income were driven by growth in average loan balances and a wider spread on total deposits due to their funding benefit during a rising interest rate environment, partially offset by reduced loan spreads due to competitive pricing. The increase in average loans was due to stronger commercial loan and commercial real estate loan demand in the first nine months of 2006.

Noninterest income increased \$13 million (6.3 percent) and \$20 million (3.1 percent) in the third quarter and first nine months of 2006, respectively, compared with the same periods of 2005. The third quarter 2006 increase from a year ago was due to higher revenue from equity investments. The increase during the first nine months of 2006 was related to higher commercial products revenue including improvement in equipment leasing, partially offset by lower other commercial loan fees and letter of credit fees.

Noninterest expense was flat in the third quarter of 2006, compared with the third quarter of 2005. Noninterest expense increased \$2 million (.3 percent) in the first nine months of 2006, compared with the same period of 2005. The increase was primarily driven by higher personnel-related costs.

The provision for credit losses decreased \$2 million in the third quarter and \$7 million in the first nine months of 2006, compared with the same periods of 2005. The decrease in the provision for credit losses in the third quarter of 2006, was due to lower net charge-offs compared with the third quarter of 2005 caused by lower levels of nonperforming assets during this growth stage of the business cycle and strong credit underwriting. Nonperforming assets within Wholesale Banking were \$213 million at September 30, 2006, \$218 million at June 30, 2006, and \$304 million at September 30, 2005. Nonperforming assets as a percentage of period-end loans were .42 percent at September 30, 2006, .43 percent at June 30, 2006, and .62 percent at September 30, 2005. Refer to the Corporate Risk Profile section for further information on factors impacting the credit quality of the loan portfolios.

**Consumer Banking** delivers products and services through banking offices, telephone servicing and sales, on-line services, direct mail and ATMs. It encompasses community banking, metropolitan banking, in-store banking, small business banking, consumer lending, mortgage banking, consumer finance, workplace

**Table of Contents****Table 11** Line of Business Financial Performance

Three Months Ended September 30 (Dollars in Millions)	Wholesale Banking			Consumer Banking		
	2006	2005	Percent Change	2006	2005	Percent Change
<b>Condensed Income Statement</b>						
Net interest income (taxable-equivalent basis)	\$478	\$476	.4%	\$986	\$965	2.2%
Noninterest income	219	206	6.3	458	488	(6.1)
Securities gains (losses), net						
Total net revenue	697	682	2.2	1,444	1,453	(.6)
Noninterest expense	224	224		623	622	.2
Other intangibles	4	4		12	63	(81.0)
Total noninterest expense	228	228		635	685	(7.3)
Income before provision and income taxes	469	454	3.3	809	768	5.3
Provision for credit losses	1	3	(66.7)	59	65	(9.2)
Income before income taxes	468	451	3.8	750	703	6.7
Income taxes and taxable-equivalent adjustment	170	164	3.7	273	256	6.6
Net income	\$298	\$287	3.8	\$477	\$447	6.7
<b>Average Balance Sheet Data</b>						
Commercial	\$33,764	\$31,643	6.7%	\$6,447	\$6,283	2.6%
Commercial real estate	17,139	17,091	.3	10,805	10,385	4.0
Residential mortgages	61	68	(10.3)	20,592	18,263	12.8
Retail	44	31	41.9	35,586	34,710	2.5
Total loans	51,008	48,833	4.5	73,430	69,641	5.4
Goodwill	1,329	1,329		2,131	2,108	1.1
Other intangible assets	51	69	(26.1)	1,490	1,193	24.9
Assets	56,359	53,809	4.7	82,164	78,059	5.3
Noninterest-bearing deposits	11,264	12,201	(7.7)	12,663	13,319	(4.9)
Interest checking	3,737	2,847	31.3	17,437	17,333	.6
Savings products	5,481	5,181	5.8	20,591	23,809	(13.5)
Time deposits	12,022	14,080	(14.6)	18,831	17,326	8.7
Total deposits	32,504	34,309	(5.3)	69,522	71,787	(3.2)
Shareholders equity	5,800	5,503	5.4	6,622	6,627	(.1)

Nine Months Ended September 30 (Dollars in Millions)	Wholesale Banking			Consumer Banking		
	2006	2005	Percent Change	2006	2005	Percent Change
<b>Condensed Income Statement</b>						
Net interest income (taxable-equivalent basis)	\$1,440	\$1,400	2.9%	\$2,903	\$2,824	2.8%
Noninterest income	668	654	2.1	1,306	1,361	(4.0)
Securities gains (losses), net	2	(4)	*			
<b>Total net revenue</b>	<b>2,110</b>	<b>2,050</b>	<b>2.9</b>	<b>4,209</b>	<b>4,185</b>	<b>.6</b>
Noninterest expense	678	676	.3	1,827	1,809	1.0
Other intangibles	12	12		37	189	(80.4)
<b>Total noninterest expense</b>	<b>690</b>	<b>688</b>	<b>.3</b>	<b>1,864</b>	<b>1,998</b>	<b>(6.7)</b>
Income before provision and income taxes	1,420	1,362	4.3	2,345	2,187	7.2
Provision for credit losses	(6)	1	*	176	202	(12.9)
<b>Income before income taxes</b>	<b>1,426</b>	<b>1,361</b>	<b>4.8</b>	<b>2,169</b>	<b>1,985</b>	<b>9.3</b>
Income taxes and taxable-equivalent adjustment	519	495	4.8	790	723	9.3
<b>Net income</b>	<b>\$907</b>	<b>\$866</b>	<b>4.7</b>	<b>\$1,379</b>	<b>\$1,262</b>	<b>9.3</b>

**Average Balance Sheet Data**

Commercial	\$33,164	\$31,020	6.9%	\$6,381	\$6,104	4.5%
Commercial real estate	17,262	16,779	2.9	10,691	10,252	4.3
Residential mortgages	61	62	(1.6)	20,478	16,808	21.8
Retail	43	36	19.4	35,247	33,859	4.1
<b>Total loans</b>	<b>50,530</b>	<b>47,897</b>	<b>5.5</b>	<b>72,797</b>	<b>67,023</b>	<b>8.6</b>
Goodwill	1,329	1,329		2,115	2,109	.3
Other intangible assets	55	73	(24.7)	1,425	1,159	23.0
Assets	56,032	53,068	5.6	81,003	74,868	8.2
Noninterest-bearing deposits	11,784	12,144	(3.0)	12,686	13,067	(2.9)
Interest checking	3,346	3,216	4.0	17,614	17,236	2.2
Savings products	5,449	5,308	2.7	21,425	24,587	(12.9)
Time deposits	12,470	12,575	(.8)	18,471	16,865	9.5
<b>Total deposits</b>	<b>33,049</b>	<b>33,243</b>	<b>(.6)</b>	<b>70,196</b>	<b>71,755</b>	<b>(2.2)</b>
Shareholders equity	5,689	5,424	4.9	6,509	6,486	.4

\* Not meaningful



**Table of Contents**

Wealth Management			Payment Services			Treasury and Corporate Support			Consolidated Company		
2006	2005	Percent Change	2006	2005	Percent Change	2006	2005	Percent Change	2006	2005	Percent Change
\$127	\$111	14.4%	\$164	\$154	6.5%	\$(82)	\$85	*%	\$1,673	\$1,791	(6.6)%
354	301	17.6	672	579	16.1	45	1	*	1,748	1,575	11.0
							1	*		1	*
481	412	16.7	836	733	14.1	(37)	87	*	3,421	3,367	1.6
230	205	12.2	313	274	14.2	59	23	*	1,449	1,348	7.5
20	15	33.3	53	45	17.8		(2)	*	89	125	(28.8)
250	220	13.6	366	319	14.7	59	21	*	1,538	1,473	4.4
231	192	20.3	470	414	13.5	(96)	66	*	1,883	1,894	(.6)
			74	88	(15.9)	1	(11)	*	135	145	(6.9)
231	192	20.3	396	326	21.5	(97)	77	*	1,748	1,749	(.1)
84	70	20.0	144	119	21.0	(126)	(14)	*	545	595	(8.4)
\$147	\$122	20.5	\$252	\$207	21.7	\$29	\$91	(68.1)	\$1,203	\$1,154	4.2
\$1,847	\$1,588	16.3%	\$3,880	\$3,570	8.7%	\$130	\$167	(22.2)%	\$46,068	\$43,251	6.5%
695	631	10.1				62	86	(27.9)	28,701	28,193	1.8
460	405	13.6				5	5		21,118	18,741	12.7
2,408	2,315	4.0	8,927	7,993	11.7	42	49	(14.3)	47,007	45,098	4.2
5,410	4,939	9.5	12,807	11,563	10.8	239	307	(22.1)	142,894	135,283	5.6
1,379	874	57.8	2,477	2,061	20.2	1		*	7,317	6,372	14.8
452	301	50.2	1,157	1,002	15.5		2	*	3,150	2,567	22.7
7,808	6,640	17.6	17,850	15,475	15.3	49,908	51,684	(3.4)	214,089	205,667	4.1
4,020	3,735	7.6	334	163	*	(61)	16	*	28,220	29,434	(4.1)
2,418	2,325	4.0				3	3		23,595	22,508	4.8
5,595	5,491	1.9	20	17	17.6	27	19	42.1	31,714	34,517	(8.1)
3,249	1,656	96.2	3	7	(57.1)	2,341	1,456	60.8	36,446	34,525	5.6
15,282	13,207	15.7	357	187	90.9	2,310	1,494	54.6	119,975	120,984	(.8)
2,337	1,654	41.3	4,782	4,063	17.7	1,376	2,259	(39.1)	20,917	20,106	4.0

Wealth Management

Payment Services

Treasury and Corporate Support

Consolidated Company

Edgar Filing: US BANCORP \DE\ - Form 10-Q

2006	Percent 2005 Change		2006	Percent 2005 Change		2006	Percent 2005 Change		2006	Percent 2005 Change	
\$379	\$316	19.9%	\$483	\$435	11.0%	\$(110)	\$328	*%	\$5,095	\$5,303	(3.9)%
1,073	897	19.6	1,916	1,610	19.0	151	34	*	5,114	4,556	12.2
						1	(53)	*	3	(57)	*
1,452	1,213	19.7	2,399	2,045	17.3	42	309	(86.4)	10,212	9,802	4.2
705	616	14.4	908	768	18.2	187	153	22.2	4,305	4,022	7.0
64	46	39.1	150	129	16.3		1	*	263	377	(30.2)
769	662	16.2	1,058	897	17.9	187	154	21.4	4,568	4,399	3.8
683	551	24.0	1,341	1,148	16.8	(145)	155	*	5,644	5,403	4.5
2	2		199	269	(26.0)	4	(13)	*	375	461	(18.7)
681	549	24.0	1,142	879	29.9	(149)	168	*	5,269	4,942	6.6
248	200	24.0	416	320	30.0	(261)	(142)	(83.8)	1,712	1,596	7.3
\$433	\$349	24.1	\$726	\$559	29.9	\$112	\$310	(63.9)	\$3,557	\$3,346	6.3
\$1,624	\$1,576	3.0%	\$3,726	\$3,401	9.6%	\$134	\$162	(17.3)%	\$45,029	\$42,263	6.5%
688	641	7.3				63	90	(30.0)	28,704	27,762	3.4
449	389	15.4				4	7	(42.9)	20,992	17,266	21.6
2,411	2,302	4.7	8,589	7,895	8.8	44	49	(10.2)	46,334	44,141	5.0
5,172	4,908	5.4	12,315	11,296	9.0	245	308	(20.5)	141,059	131,432	7.3
1,377	874	57.6	2,410	2,010	19.9	1		*	7,232	6,322	14.4
474	316	50.0	1,125	960	17.2		6	*	3,079	2,514	22.5
7,589	6,642	14.3	17,210	15,038	14.4	50,354	51,889	(3.0)	212,188	201,505	5.3
3,778	3,601	4.9	308	146	*	110	45	*	28,666	29,003	(1.2)
2,395	2,432	(1.5)				3	7	(57.1)	23,358	22,891	2.0
5,565	5,466	1.8	19	15	26.7	31	17	82.4	32,489	35,393	(8.2)
2,730	1,234	*	3	3		2,269	2,588	(12.3)	35,943	33,265	8.1
14,468	12,733	13.6	330	164	*	2,413	2,657	(9.2)	120,456	120,552	(.1)
2,337	1,666	40.3	4,620	3,971	16.3	1,388	2,364	(41.3)	20,543	19,911	3.2

**Table of Contents**

banking, student banking and 24-hour banking. Consumer Banking contributed \$477 million of the Company's net income in the third quarter and \$1,379 million in the first nine months of 2006, or increases of \$30 million and \$117 million, respectively, compared with the same periods of 2005. While the retail banking business grew net income 7.5 percent in the third quarter and 10.4 percent in the first nine months of 2006, the contribution of the mortgage banking business decreased 2.9 percent and 4.3 percent, respectively, compared with the same periods of 2005.

Total net revenue decreased \$9 million (.6 percent) in the third quarter and increased \$24 million (.6 percent) in the first nine months of 2006, compared with the same periods of 2005. Net interest income, on a taxable-equivalent basis, increased \$21 million in the third quarter and \$79 million in the first nine months of 2006, compared with the same periods of 2005. The year-over-year increases in net interest income were due to strong growth in average loans and the funding benefit of total deposits due to rising interest rates. Partially offsetting these increases were reduced spreads on commercial and retail loans due to competitive pricing. The increases in average loan balances reflected growth in residential mortgages, retail loans, commercial loans and commercial real estate loans. Residential mortgages, which include traditional residential mortgages, grew 12.8 percent in the third quarter and 21.8 percent in the first nine months of 2006, compared with the same periods of a year ago. Residential mortgage balances increased throughout 2005, reflecting the Company's retention of adjustable-rate residential mortgages. However, during the first nine months of 2006, residential mortgage balances have increased only slightly and are expected to remain essentially flat in future periods due to the Company's decision in the first quarter of 2006 to package and sell the majority of its residential mortgage loan production in the secondary markets. The growth in retail loans was principally driven by an increase in installment loans which increased 10.1 percent in the third quarter and 13.6 percent in the first nine months of 2006, over the same periods of 2005. The year-over-year decreases in average deposits were primarily due to a reduction in savings and noninterest-bearing deposit products, offset by growth in interest checking and time deposits. Average time deposit balances grew \$1.5 billion in the third quarter and \$1.6 billion in the first nine months of 2006, compared with the same periods of 2005, as a portion of noninterest-bearing and money market balances migrated to fixed-rate time deposit products. Average savings balances declined \$3.2 billion (13.5 percent) and \$3.2 billion (12.9 percent) in the third quarter and first nine months of 2006, respectively, compared with the same periods of 2005, principally related to money market accounts.

Fee-based noninterest income decreased \$30 million in the third quarter and \$55 million in the first nine months of 2006, compared with the same periods of 2005. The year-over-year decline in fee-based revenue was driven by a reduction in mortgage banking revenue, partially offset by an increase in deposit service charges due to increased transaction-related fees and net new checking accounts. The reduction in mortgage banking revenue principally reflected the adoption of fair value accounting for MSRs as of January 1, 2006.

Noninterest expense decreased \$50 million (7.3 percent) in the third quarter and \$134 million (6.7 percent) in the first nine months of 2006, compared with the same periods of 2005. The decreases were primarily attributable to the elimination of MSR amortization under SFAS 156 which resulted in a reduction of other intangible expense. Partially offsetting this decrease were increases in compensation and employee benefit expenses. The increases in compensation and employee benefit expenses reflected the impact of the net addition of 33 in-store and 33 traditional branches at September 30, 2006, compared with September 30, 2005.

The provision for credit losses decreased \$6 million and \$26 million in the third quarter and first nine months of 2006, respectively, compared with the same periods of 2005. The improvements were attributable to lower net charge-offs. As a percentage of average loans outstanding, net charge-offs declined to .32 percent in the third quarter of 2006, compared with .37 percent in the third quarter of 2005. The decline in net charge-offs included both the commercial and retail loan portfolios. Commercial and commercial real estate loan net charge-offs declined \$2 million in the third quarter of 2006, compared with the third quarter of 2005. Retail loan and residential mortgage net charge-offs declined by \$4 million in the third quarter of 2006, compared with the third quarter of 2005, primarily due to lower bankruptcy losses and slightly higher retail recoveries. Nonperforming assets within Consumer Banking were \$305 million at September 30, 2006, \$275 million at June 30, 2006, and \$302 million at September 30, 2005. Nonperforming assets as a percentage of period-end loans were .43 percent at September 30, 2006, .39 percent at June 30, 2006, and .45 percent at September 30, 2005. Refer to the Corporate Risk Profile section for further



information on factors impacting the credit quality of the loan portfolios.

**Table of Contents**

**Wealth Management** provides trust, private banking, financial advisory, investment management, retail brokerage services, insurance, custody and mutual fund servicing through six businesses: Private Client Group, Corporate Trust, U.S. Bancorp Investments and Insurance, FAF Advisors, Institutional Trust and Custody and Fund Services. Wealth Management contributed \$147 million of the Company's net income in the third quarter and \$433 million in the first nine months of 2006, or increases of \$25 million and \$84 million, respectively, compared with the same periods of 2005. The growth was primarily attributable to higher total net revenue, partially offset by an increase in noninterest expense.

Total net revenue increased \$69 million (16.7 percent) in the third quarter and \$239 million (19.7 percent) in the first nine months of 2006, compared with the same periods of 2005. Net interest income, on a taxable-equivalent basis, increased \$16 million in the third quarter and \$63 million in the first nine months of 2006, compared with the same periods of 2005. The increases in net interest income were due to growth in total average deposits and the favorable impact of rising interest rates on the funding benefit of customer deposits, partially offset by a decline in loan spreads. The increase in total deposits was attributable to growth in noninterest-bearing deposits and time deposits principally in Corporate Trust. Noninterest income increased \$53 million in the third quarter and \$176 million in the first nine months of 2006, compared with the same periods of 2005, driven by account growth, favorable equity market conditions and the acquisition of a corporate and institutional trust business in late 2005.

Noninterest expense increased \$30 million (13.6 percent) in the third quarter and \$107 million (16.2 percent) in the first nine months of 2006, compared with the same periods of 2005. The increases in noninterest expense were primarily attributable to the acquisition of the corporate and institutional trust business.

**Payment Services** includes consumer and business credit cards, stored-value cards, debit cards, corporate and purchasing card services, consumer lines of credit, ATM processing and merchant processing. Payment Services contributed \$252 million of the Company's net income in the third quarter and \$726 million in the first nine months of 2006, or increases of \$45 million and \$167 million, respectively, compared with the same periods of 2005. The increases were due to growth in total net revenue driven by higher transaction volumes and a lower provision for credit losses, partially offset by increases in total noninterest expense.

Total net revenue increased \$103 million (14.1 percent) in the third quarter and \$354 million (17.3 percent) in the first nine months of 2006, compared with the same periods of 2005. Net interest income increased \$10 million in the third quarter and \$48 million in the first nine months of 2006, compared with the same periods of 2005. The increases were primarily due to growth in higher yielding retail loan balances, partially offset by an increase in non-earning assets resulting in higher funding expense. Noninterest income increased \$93 million in the third quarter and \$306 million in the first nine months of 2006, compared with the same periods of 2005. The increases in fee-based revenue were driven by strong growth in credit and debit card revenue, corporate payment products revenue and merchant processing revenue. Credit and debit card revenue increased due to higher customer transaction volume. Corporate payment products revenue reflected organic growth in sales volumes and card usage as well as the acquisition of a freight payments company in July of 2006. Merchant processing revenue also grew from a year ago due to an increase in sales volume driven by acquisitions, higher same store sales and equipment fees. Noninterest income for the first nine months of 2006 also included the impact of a \$10 million settlement in the first quarter.

Noninterest expense increased \$47 million (14.7 percent) in the third quarter and \$161 million (17.9 percent) in the first nine months of 2006, compared with the same periods of 2005. The increases in noninterest expense were primarily attributable to the acquisition of merchant acquiring and corporate payments businesses, higher compensation and employee benefit costs for processing associated with increased credit and debit card transaction volumes, higher corporate payment products and merchant processing sales volumes, and higher ATM processing services volumes.

The provision for credit losses decreased \$14 million (15.9 percent) in the third quarter and \$70 million (26.0 percent) in the first nine months of 2006, compared with the same periods of 2005, due to lower net charge-offs. As a percentage of average loans outstanding, net charge-offs were 2.29 percent in the third quarter of 2006, compared with 3.02 percent in the third quarter of 2005. The favorable change in credit losses reflected the near-term impact of changes in bankruptcy legislation in the fourth quarter of 2005.

**Treasury and Corporate Support** includes the Company's investment portfolios, funding, capital management and asset securitization activities, interest rate risk management, the net effect of transfer pricing related to

U.S. Bancorp

25

---

**Table of Contents**

average balances and the residual aggregate of those expenses associated with corporate activities that are managed on a consolidated basis. In addition, prior to the adoption of SFAS 156, changes in MSR valuations due to interest rate changes were managed at a corporate level and, as such, reported within this business unit. Treasury and Corporate Support recorded net income of \$29 million in the third quarter and \$112 million in the first nine months of 2006, or decreases of \$62 million and \$198 million, respectively, compared with the same periods of 2005.

Total net revenue decreased \$124 million in the third quarter and \$267 million in the first nine months of 2006, compared with the same periods of 2005. The year-over-year decreases in total net revenue were primarily due to unfavorable variances in net interest income, partially offset by higher noninterest income. The decrease in net interest income reflected the impact of a flatter yield curve and asset/liability management decisions, including reducing the investment securities portfolio, changes in interest rate derivative positions and the issuance of wholesale funding. Noninterest income increased \$43 million in the third quarter and \$171 million in the first nine months of 2006, compared with the same periods of 2005. The increase in noninterest income in the third quarter and first nine months of 2006 was driven by a gain on the sale of equity interests in a card association. The increase during the first nine months of 2006 was also due to trading income from derivatives, a gain from the initial public offering of a card association realized in the second quarter of 2006 and securities losses incurred in the first nine months of 2005.

Noninterest expense increased \$38 million in the third quarter and \$33 million in the first nine months of 2006, compared with the same periods of 2005. The increases in noninterest expense were driven by higher business integration costs related to recent acquisitions and amortization of community development investments.

The provision for credit losses for this business unit represents the residual aggregate of the net credit losses allocated to the reportable business units and the Company's recorded provision determined in accordance with accounting principles generally accepted in the United States. Refer to the Corporate Risk Profile section for further information on the provision for credit losses, nonperforming assets and factors considered by the Company in assessing the credit quality of the loan portfolio and establishing the allowance for credit losses.

Income taxes are assessed to each line of business at a managerial tax rate of 36.4 percent with the residual tax expense or benefit to arrive at the consolidated effective tax rate included in Treasury and Corporate Support. The consolidated effective tax rate of the Company was 30.7 percent and 32.1 percent in the third quarter and first nine months of 2006, respectively, compared with 33.7 percent and 32.0 percent in the same periods of 2005, respectively. The effective rate for the third quarter of 2006 reflected an expected increase in income tax credits from tax-advantaged investments through the remainder of the year.

**CRITICAL ACCOUNTING POLICIES**

The accounting and reporting policies of the Company comply with accounting principles generally accepted in the United States and conform to general practices within the banking industry. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions. The financial position and results of operations can be affected by these estimates and assumptions, which are integral to understanding the Company's financial statements. Critical accounting policies are those policies that management believes are the most important to the portrayal of the Company's financial condition and results, and require management to make estimates that are difficult, subjective or complex. Most accounting policies are not considered by management to be critical accounting policies. Those policies considered to be critical accounting policies relate to the allowance for credit losses, MSRs, goodwill and other intangibles and income taxes. Management has discussed the development and the selection of critical accounting policies with the Company's Audit Committee. These accounting policies are discussed in detail in Management's Discussion and Analysis Critical Accounting Policies and the Notes to Consolidated Financial Statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2005. Refer to Note 2 of the Notes to Consolidated Financial Statements for discussion of the change in accounting for MSRs implemented in the first quarter of 2006.

**CONTROLS AND PROCEDURES**

Under the supervision and with the participation of the Company's management, including its principal executive officer and principal financial officer, the Company has evaluated the effectiveness of the design and operation of its disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the Exchange Act)).



**Table of Contents**

Based upon this evaluation, the principal executive officer and principal financial officer have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective.

During the most recently completed fiscal quarter, there was no change made in the Company's internal controls over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

U.S. Bancorp

**27**

---

**Table of Contents**U.S. Bancorp  
Consolidated Balance Sheet

(Dollars in Millions)	September 30, 2006	December 31, 2005
	(Unaudited)	
<b>Assets</b>		
Cash and due from banks	\$6,355	\$8,004
Investment securities		
Held-to-maturity (fair value \$97 and \$113, respectively)	91	109
Available-for-sale	39,429	39,659
Loans held for sale	2,649	1,686
Loans		
Commercial	46,594	42,942
Commercial real estate	28,973	28,463
Residential mortgages	21,215	20,730
Retail	47,626	45,671
Total loans	144,408	137,806
Less allowance for loan losses	(2,034)	(2,041)
Net loans	142,374	135,765
Premises and equipment	1,835	1,841
Goodwill	7,444	7,005
Other intangible assets	3,171	2,874
Other assets	13,507	12,522
Total assets	\$216,855	\$209,465
<b>Liabilities and Shareholders Equity</b>		
Deposits		
Noninterest-bearing	\$30,554	\$32,214
Interest-bearing	69,095	70,024
Time deposits greater than \$100,000	21,312	22,471
Total deposits	120,961	124,709
Short-term borrowings	24,783	20,200
Long-term debt	41,230	37,069
Other liabilities	8,955	7,401
Total liabilities	195,929	189,379
Shareholders equity		
Preferred stock, par value \$1.00 a share (liquidation preference of \$25,000 per share) authorized: 50,000,000 shares; issued and outstanding: 9/30/06 40,000 shares	1,000	
Common stock, par value \$0.01 a share authorized: 4,000,000,000 shares; issued: 9/30/06 and 12/31/05 1,972,643,007 shares	20	20
Capital surplus	5,770	5,907

Retained earnings		20,770	19,001
Less cost of common stock in treasury: 9/30/06 209,488,841 shares; 12/31/05 157,689,004 shares		(6,093)	(4,413)
Other comprehensive income		(541)	(429)
<b>Total shareholders equity</b>		<b>20,926</b>	<b>20,086</b>
<b>Total liabilities and shareholders equity</b>		<b>\$216,855</b>	<b>\$209,465</b>

*See Notes to Consolidated Financial Statements.*



**Table of Contents**U.S. Bancorp  
Consolidated Statement of Income

(Dollars and Shares in Millions, Except Per Share Data) (Unaudited)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
<b>Interest Income</b>				
Loans	\$2,569	\$2,167	\$7,350	\$6,105
Loans held for sale	40	30	99	75
Investment securities	500	492	1,490	1,454
Other interest income	40	29	119	84
Total interest income	3,149	2,718	9,058	7,718
<b>Interest Expense</b>				
Deposits	640	414	1,721	1,083
Short-term borrowings	321	205	861	460
Long-term debt	528	317	1,415	895
Total interest expense	1,489	936	3,997	2,438
Net interest income	1,660	1,782	5,061	5,280
Provision for credit losses	135	145	375	461
Net interest income after provision for credit losses	1,525	1,637	4,686	4,819
<b>Noninterest Income</b>				
Credit and debit card revenue	206	185	590	516
Corporate payment products revenue	150	135	416	362
ATM processing services	63	64	183	168
Merchant processing services	253	200	719	576
Trust and investment management fees	305	251	916	751
Deposit service charges	268	246	764	690
Treasury management fees	111	109	334	333
Commercial products revenue	100	103	311	299
Mortgage banking revenue	68	111	167	323
Investment products fees and commissions	34	37	114	115
Securities gains (losses), net		1	3	(57)
Other	190	134	600	423
Total noninterest income	1,748	1,576	5,117	4,499
<b>Noninterest Expense</b>				
Compensation	632	603	1,892	1,782
Employee benefits	123	106	379	330
Net occupancy and equipment	168	162	494	475
Professional services	54	44	130	119
Marketing and business development	58	61	156	171
Technology and communications	128	118	372	337

Edgar Filing: US BANCORP \DE\ - Form 10-Q

Postage, printing and supplies	66	64	198	190
Other intangibles	89	125	263	377
Debt prepayment			11	54
Other	220	190	673	564
Total noninterest expense	1,538	1,473	4,568	4,399
Income before income taxes	1,735	1,740	5,235	4,919
Applicable income taxes	532	586	1,678	1,573
Net income	\$1,203	\$1,154	\$3,557	\$3,346
Net income applicable to common equity	\$1,187	\$1,154	\$3,524	\$3,346
Earnings per common share	\$.67	\$.63	\$1.98	\$1.82
Diluted earnings per common share	\$.66	\$.62	\$1.95	\$1.80
Dividends declared per common share	\$.33	\$.30	\$.99	\$.90
Average common shares outstanding	1,771	1,823	1,784	1,836
Average diluted common shares outstanding	1,796	1,849	1,809	1,862

*See Notes to Consolidated Financial Statements.*

U.S. Bancorp

29

**Table of Contents**U.S. Bancorp  
Consolidated Statement of Shareholders' Equity

(Dollars and Shares in Millions) (Unaudited)	Common Shares Outstanding	Preferred Stock	Common Stock	Capital Surplus	Retained Earnings	Treasury Stock	Other Comprehensive Income	Total Shareholders' Equity
<b>Balance</b>								
<b>December 31, 2004</b>	1,858	\$ 20	\$5,902	\$16,758	\$(3,125)	\$(16)	\$19,539	
Net income				3,346			3,346	
Unrealized loss on securities available for sale							(211)	(211)
Unrealized loss on derivatives							(30)	(30)
Foreign currency translation adjustment							8	8
Realized loss on derivatives							(197)	(197)
Reclassification adjustment for losses realized in net income							120	120
Income taxes							118	118
<b>Total comprehensive income</b>								3,154
Cash dividends declared on common stock					(1,647)			(1,647)
Issuance of common and treasury stock	13		(62)			360		298
Purchase of treasury stock	(53)					(1,549)		(1,549)
Stock option and restricted stock grants				72				72
Shares reserved to meet deferred compensation obligations				1		(4)		(3)
<b>Balance</b>								
<b>September 30, 2005</b>	1,818	\$ 20	\$5,913	\$18,457	\$(4,318)	\$(208)	\$19,864	
<b>Balance</b>								
<b>December 31, 2005</b>	1,815	\$ 20	\$5,907	\$19,001	\$(4,413)	\$(429)	\$20,086	
Change in accounting principle				4				4

Net income					3,557			3,557
Unrealized loss on securities available for sale							(52)	(52)
Unrealized gain on derivatives							39	39
Foreign currency translation adjustment							5	5
Realized loss on derivatives							(199)	(199)
Reclassification adjustment for losses realized in net income							28	28
Income taxes							67	67
<b>Total comprehensive income</b>								<b>3,445</b>
Cash dividends declared:								
Preferred							(33)	(33)
Common							(1,759)	(1,759)
Issuance of common and treasury stock	28		(95)			812		717
Purchase of treasury stock	(80)					(2,488)		(2,488)
Stock option and restricted stock grants			9					9
Shares reserved to meet deferred compensation obligations			1			(4)		(3)
Issuance of preferred stock		1,000	(52)					948
<b>Balance</b>								
<b>September 30, 2006</b>	1,763	\$1,000	\$20	\$5,770	\$20,770	\$(6,093)	\$(541)	\$20,926

See Notes to Consolidated Financial Statements.

**Table of Contents**U.S. Bancorp  
Consolidated Statement of Cash Flows

	Nine Months Ended September 30,	
(Dollars in Millions) (Unaudited)	2006	2005
<b>Operating Activities</b>		
Net cash provided by operating activities	\$4,512	\$2,899
<b>Investing Activities</b>		
Proceeds from sales of available-for-sale investment securities	1,132	3,065
Proceeds from maturities of investment securities	3,174	8,072
Purchases of investment securities	(5,094)	(10,430)
Net (increase) decrease in loans outstanding	(5,455)	(8,940)
Proceeds from sales of loans	1,394	1,150
Purchases of loans	(2,171)	(2,581)
Acquisitions, net of cash acquired	(587)	(279)
Other, net	(305)	(1,216)
Net cash used in investing activities	(7,912)	(11,159)
<b>Financing Activities</b>		
Net increase (decrease) in deposits	(4,313)	54
Net increase (decrease) in short-term borrowings	4,462	9,977
Principal payments or redemption of long-term debt	(9,103)	(9,248)
Proceeds from issuance of long-term debt	13,379	11,002
Proceeds from issuance of preferred stock	948	
Proceeds from issuance of common stock	613	246
Repurchase of common stock	(2,480)	(1,605)
Cash dividends paid on preferred stock	(17)	
Cash dividends paid on common stock	(1,777)	(1,660)
Net cash provided by financing activities	1,712	8,766
Change in cash and cash equivalents	(1,688)	506
Cash and cash equivalents at beginning of period	8,202	6,537
Cash and cash equivalents at end of period	\$6,514	\$7,043

See Notes to Consolidated Financial Statements.

**Table of Contents**Notes to Consolidated Financial Statements  
(Unaudited)**Note 1** Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and, therefore, do not include all information and notes necessary for a complete presentation of financial position, results of operations and cash flow activity required in accordance with accounting principles generally accepted in the United States. In the opinion of management of U.S. Bancorp (the Company), all adjustments (consisting only of normal recurring adjustments) necessary for a fair statement of results for the interim periods have been made. For further information, refer to the consolidated financial statements and notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005. Certain amounts in prior periods have been reclassified to conform to the current presentation.

Accounting policies for the lines of business are generally the same as those used in preparation of the consolidated financial statements with respect to activities specifically attributable to each business line. However, the preparation of business line results requires management to establish methodologies to allocate funding costs and benefits, expenses and other financial elements to each line of business. Table 11 Line of Business Financial Performance provides details of segment results. This information is incorporated by reference into these Notes to Consolidated Financial Statements.

**Note 2** Accounting Changes

**Employers Accounting for Defined Benefit Pension and Other Postretirement Plans** In September 2006, the Financial Accounting Standards Board (FASB) issued Statement No. 158 (SFAS 158), Employers Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R), effective for the Company for the year ending December 31, 2006. This statement requires the recognition of the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability on the balance sheet, and recognition of changes in that funded status in the year in which the changes occur through other comprehensive income. The adoption of SFAS 158 is not expected to have a material impact on the Company's financial statements.

**Fair Value Measurements** In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157 (SFAS 157), Fair Value Measurements, effective for the Company beginning on January 1, 2008, with earlier adoption permitted. This Statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. This statement establishes a fair value hierarchy that distinguishes between valuations obtained from sources independent of the entity and those from the entity's own unobservable inputs that are not corroborated by observable market data. SFAS 157 expands disclosures about the use of fair value to measure assets and liabilities in interim and annual periods subsequent to initial recognition. The disclosures focus on the inputs used to measure fair value and for recurring fair value measurements using significant unobservable inputs, the effect of the measurements on earnings or changes in net assets for the period. This statement encourages an entity to combine the fair value information disclosed under this statement with the fair value information disclosed under other accounting pronouncements, including SFAS 107, Disclosures about Fair Value of Financial Instruments, where practicable. The Company is currently assessing the impact of this guidance on its financial statements.

**Accounting for Uncertainty in Income Taxes** In June 2006, the FASB issued Interpretation No. 48 (FIN 48),

Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109, Accounting for Income Taxes, effective for the Company beginning on January 1, 2007. FIN 48 clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. The Company is currently assessing the impact of this guidance on its financial statements.

**Table of Contents**

**Accounting for Servicing of Financial Assets** In March 2006, the FASB issued Statement of Financial Accounting Standards No. 156, Accounting for Servicing of Financial Assets ( SFAS 156 ), that amends accounting and reporting standards for servicing assets and liabilities under Statement of Financial Accounting Standards No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities . Specifically, SFAS 156 requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable. For subsequent measurement purposes, SFAS 156 permits an entity to choose to measure servicing assets and liabilities either based on fair value or lower of cost or market ( LOCOM ). The Company elected to adopt SFAS 156 effective January 1, 2006, utilizing the fair value measurement option for residential mortgage servicing rights ( MSRs ) and continuing the LOCOM method for all other servicing assets and liabilities. Adopting the fair value measurement method resulted in the Company recording a cumulative-effect accounting adjustment to increase beginning retained earnings by \$4 million (net of tax). Approximately \$3 million represented the difference between the fair value and the carrying amount of the Company s MSRs as of January 1, 2006, and the additional \$1 million represented the reclassification of unrealized gains in accumulated other comprehensive income at adoption, for certain available-for-sale securities reclassified to trading securities upon the adoption of the provisions of this statement. Additional information regarding MSRs is disclosed in Note 5 in the Notes to Consolidated Financial Statements.

**Other-Than-Temporary Impairment** In November 2005, the FASB issued FASB Staff Position FAS 115-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments ( FSP 115-1 ), effective for the Company beginning on January 1, 2006. FSP 115-1 provides clarification on when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. FSP 115-1 also requires certain disclosures for unrealized losses that have not been recognized as other-than-temporary impairments. The adoption of FSP 115-1 did not have a material impact on the Company s financial statements.

**Stock-Based Compensation** In December 2004, the FASB issued Statement of Financial Accounting Standards No. 123 (revised 2004) ( SFAS 123R ), Share-Based Payment , a revision of Statement of Financial Accounting Standards No. 123 ( SFAS 123 ), Accounting for Stock-Based Compensation. SFAS 123R requires companies to measure the cost of employee services in exchange for an award of equity instruments based on the grant-date fair value of the award. This statement eliminates the use of the alternative intrinsic value method of accounting that was allowed when SFAS 123 was originally issued. The provisions of this statement were effective for the Company beginning on January 1, 2006. The Company adopted SFAS 123R using the modified retrospective method. Because the Company retroactively adopted the fair value method in 2003, the impact of expensing stock-based awards was already recorded in the Company s financial results. In conjunction with the adoption of SFAS 123R, the Company recognized \$13 million of incremental stock-based compensation expense due to certain provisions that require immediate recognition of the value of stock awards to employees that meet retirement status, despite their continued active employment. Upon adoption, the Company also changed its method of expensing all new awards from an accelerated to a straight-line attribution method. This methodology change for expensing stock awards is expected to reduce expenses in 2006 by approximately \$33 million (\$20 million after tax).

**Table of Contents****Note 3 Investment Securities**

The detail of the amortized cost, gross unrealized holding gains and losses, and fair value of held-to-maturity and available-for-sale securities was as follows:

(Dollars in Millions)	September 30, 2006				December 31, 2005			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
<b>Held-to-maturity (a)</b>								
Mortgage-backed securities	\$7	\$	\$	\$7	\$8	\$	\$	\$8
Obligations of state and political subdivisions	71	6		77	84	5	(1)	88
Other debt securities	13			13	17			17
<b>Total held-to-maturity securities</b>	<b>\$91</b>	<b>\$6</b>	<b>\$</b>	<b>\$97</b>	<b>\$109</b>	<b>\$5</b>	<b>\$(1)</b>	<b>\$113</b>
<b>Available-for-sale (b)</b>								
U.S. Treasury and agencies	\$455	\$1	\$(7)	\$449	\$496	\$2	\$(9)	\$489
Mortgage-backed securities	34,978	84	(855)	34,207	38,161	86	(733)	37,514
Asset-backed securities	7			7	12			12
Obligations of state and political subdivisions	3,695	63		3,758	640	3	(6)	637
Other securities and investments	1,004	9	(5)	1,008	1,012	2	(7)	1,007
<b>Total available-for-sale securities</b>	<b>\$40,139</b>	<b>\$157</b>	<b>\$(867)</b>	<b>\$39,429</b>	<b>\$40,321</b>	<b>\$93</b>	<b>\$(755)</b>	<b>\$39,659</b>

(a) *Held-to-maturity securities are carried at historical cost adjusted for amortization of premiums and accretion of discounts.*

(b) *Available-for-sale securities are carried at fair value with unrealized net gains or losses reported within other comprehensive income in shareholders' equity.*

The weighted-average maturity of the available-for-sale investment securities was 6.5 years at September 30, 2006, compared with 6.1 years at December 31, 2005. The corresponding weighted-average yields were 5.25 percent and 4.89 percent, respectively. The weighted-average maturity of the held-to-maturity investment securities was 8.2 years at September 30, 2006, compared with 7.2 years at December 31, 2005. The corresponding weighted-average yields were 6.44 percent at September 30, 2006, and December 31, 2005.



Securities carried at \$37.8 billion at September 30, 2006, and \$36.9 billion at December 31, 2005, were pledged to secure public, private and trust deposits, repurchase agreements and for other purposes required by law. Securities sold under agreements to repurchase where the buyer/lender has the right to sell or pledge the securities, were collateralized by securities with an amortized cost of \$9.7 billion at September 30, 2006, and \$10.9 billion at December 31, 2005, respectively.

The following table provides information as to the amount of interest income from taxable and non-taxable investment securities:

(Dollars in Millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Taxable	\$465	\$488	\$1,416	\$1,443
Non-taxable	35	4	74	11
<b>Total interest income from investment securities</b>	<b>\$500</b>	<b>\$492</b>	<b>\$1,490</b>	<b>\$1,454</b>

The following table provides information as to the amount of gross gains and losses realized through the sales of available-for-sale investment securities:

(Dollars in Millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Realized gains	\$	\$1	\$4	\$13
Realized losses			(1)	(70)
<b>Net realized gains (losses)</b>	<b>\$</b>	<b>\$1</b>	<b>\$3</b>	<b>\$(57)</b>
Income tax (benefit) on realized gains (losses)	\$	\$	\$1	\$(22)

**Table of Contents**

For amortized cost, fair value and yield by maturity date of held-to-maturity and available-for-sale securities outstanding at September 30, 2006, refer to Table 4 included in Management's Discussion and Analysis which is incorporated by reference into these Notes to Consolidated Financial Statements.

The following table shows the gross unrealized losses and fair value of the Company's investments with unrealized losses that are not deemed to be other-than-temporarily impaired which have been in a continuous unrealized loss position at September 30, 2006:

(Dollars in Millions)	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>Held-to-maturity</b>						
Obligations of state and political subdivisions	\$10	\$	\$3	\$	\$13	\$
<b>Total</b>	<b>\$10</b>	<b>\$</b>	<b>\$3</b>	<b>\$</b>	<b>\$13</b>	<b>\$</b>
<b>Available-for-sale</b>						
U.S. Treasury and agencies	\$	\$	\$332	\$(7)	\$332	\$(7)
Mortgage-backed securities	5,726	(92)	23,806	(763)	29,532	(855)
Asset-backed securities			7		7	
Obligations of state and political subdivisions	44		35		79	
Other securities and investments	70		330	(5)	400	(5)
<b>Total</b>	<b>\$5,840</b>	<b>\$(92)</b>	<b>\$24,510</b>	<b>\$(775)</b>	<b>\$30,350</b>	<b>\$(867)</b>

The Company's rationale, by investment category, for determining if investments with unrealized losses that are not deemed to be other-than-temporarily impaired at September 30, 2006, was as follows:

**Held-to-Maturity**

**Obligations of state and political subdivisions** During the second quarter of 2006, the Company recorded an impairment of \$1 million on a municipal security with a balance of \$2 million as it was determined that the revenues supporting the security may not be sufficient to make all contractual principal and interest payments. The remaining unrealized losses were caused by increases in interest rates. The issuers of these securities do not have the contractual ability to pay off these securities at less than par. The Company has the ability and intent to hold these investments until maturity which is consistent with their designation as held to maturity. Consequently, the Company does not consider these investments to be other-than-temporarily impaired as of September 30, 2006.

**Available-for-Sale**

**U.S. Treasury and agencies** The unrealized losses on these securities were caused solely by rising interest rates since credit quality is not an issue for these types of securities. None of these securities can be paid off for less than par at maturity or any earlier call date. Because the Company has the ability and intent to hold these securities until a recovery to adjusted book value, they are not considered to be other-than-temporarily impaired as of September 30, 2006.

**Mortgage-backed securities** Substantially all of these securities were issued by GNMA, FNMA and FHLMC and the remainder were privately issued with high investment grade credit ratings. The unrealized losses for these securities

were caused by rising interest rates over the past few years. Given the high credit quality of the investments, the Company fully expects to receive all contractual cash flows. Because the Company has the ability and intent to hold these securities until a recovery to adjusted book value, they are not considered to be other-than-temporarily impaired as of September 30, 2006.

***Obligations of state and political subdivisions*** The unrealized losses were caused by rising interest rates. These municipal securities are investment grade credit quality with substantially all rated AAA. None of these securities can be paid off for less than par at maturity or any earlier call date. Because the Company has the ability and intent to hold these securities until a recovery to adjusted book value, they are not considered to be other-than-temporarily impaired as of September 30, 2006.

**Table of Contents**

**Other securities and investments** The securities in this category consist primarily of debt issued by major U.S. banks. The losses are a result of a modest widening of credit spreads since the initial purchase dates. Given the high credit quality of these issuers, the Company expects to receive all contractual cash flows. None of these securities can be paid off for less than par at maturity or any earlier call date. Because the Company has the ability and intent to hold these securities until a recovery to adjusted book value, they are not considered to be other-than-temporarily impaired as of September 30, 2006.

**Note 4 Loans**

The composition of the loan portfolio was as follows:

(Dollars in Millions)	September 30, 2006		December 31, 2005	
	Amount	Percent of Total	Amount	Percent of Total
<b>Commercial</b>				
Commercial	\$41,237	28.5%	\$37,844	27.5%
Lease financing	5,357	3.7	5,098	3.7
Total commercial	46,594	32.2	42,942	31.2
<b>Commercial real estate</b>				
Commercial mortgages	20,029	13.9	20,272	14.7
Construction and development	8,944	6.2	8,191	6.0
Total commercial real estate	28,973	20.1	28,463	20.7
<b>Residential mortgages</b>				
Residential mortgages	15,142	10.5	14,538	10.5
Home equity loans, first liens	6,073	4.2	6,192	4.5
Total residential mortgages	21,215	14.7	20,730	15.0
<b>Retail</b>				
Credit card	7,864	5.4	7,137	5.2
Retail leasing	7,068	4.9	7,338	5.3
Home equity and second mortgages	15,258	10.6	14,979	10.9
<b>Other retail</b>				
Revolving credit	2,601	1.8	2,504	1.8
Installment	4,369	3.0	3,582	2.6
Automobile	8,431	5.9	8,112	5.9
Student	2,035	1.4	2,019	1.4
Total other retail	17,436	12.1	16,217	11.7
Total retail	47,626	33.0	45,671	33.1
Total loans	\$144,408	100.0%	\$137,806	100.0%

Loans are presented net of unearned interest and deferred fees and costs, which amounted to \$1.3 billion at September 30, 2006, and December 31, 2005.

**Note 5** Mortgage Servicing Rights

The Company's portfolio of residential mortgages serviced for others was \$79.2 billion and \$69.0 billion at September 30, 2006, and December 31, 2005, respectively. Effective January 1, 2006, the Company early adopted SFAS 156 and elected the fair value measurement method for MSR's. Under this method, the Company records MSR's initially at fair value and at each subsequent reporting date. The Company records changes in fair value in noninterest income in the period in which they occur. Prior to the adoption of SFAS 156, the initial carrying value of MSR's was amortized and recorded in noninterest expense as amortization of intangible assets.

In March 2006, the Company began hedging the change in fair value of the MSR's using U.S. Treasury futures and options on U.S. Treasury futures contracts. Fair value changes related to the MSR's and the futures and options contracts, as well as servicing and other related fees, are recorded in mortgage banking revenue. The net impact of fair value changes related to MSR's and the futures and options contracts included in mortgage banking revenue was a net gain of \$7 million and net loss of \$3 million for the third quarter and first nine months of 2006, respectively.

**Table of Contents**

Servicing and other related fees revenue recorded in the third quarter and first nine months of 2006, was \$79 million and \$235 million, respectively.

Changes in fair value of capitalized MSR's are summarized as follows:

(Dollars in Millions)	Three Months	Nine Months
	Ended September 30, 2006	Ended September 30, 2006
Balance at beginning of period	\$1,323	\$1,123
Rights purchased	3	50
Rights capitalized	108	278
Changes in fair value of MSR's:		
Due to change in valuation assumptions (a)	(68)	3
Other changes in fair value (b)	(42)	(130)
Balance at end of period	\$1,324	\$1,324

(a) *Primarily reflects changes in discount rates and prepayment speed assumptions, primarily arising from interest rate changes.*

(b) *Primarily represents changes due to collection/realization of expected cash flows over time.*

The Company determines fair value by estimating the present value of the asset's future cash flows utilizing market-based prepayment rates, discount rates, and other assumptions validated through comparison to trade information, industry surveys, and independent third party appraisals. Risks inherent in the MSR's valuation include higher than expected prepayment rates and/or delayed receipt of cash flows. In March 2006, the Company implemented a program utilizing futures and options contracts to mitigate the valuation risk. The estimated sensitivity to changes in interest rates of the fair value of the MSR's portfolio and the related derivative instruments at September 30, 2006, was as follows:

(Dollars in Millions)	Down Scenario		Up Scenario	
	50 bps	25 bps	25 bps	50 bps
Net fair value	\$(31)	\$(7)	\$(16)	\$(56)

The fair value of MSR's and its sensitivity to changes in interest rates is influenced by the mix of the servicing portfolio and characteristics of each segment of the portfolio. The Company's servicing portfolio consists of the distinct portfolios of Mortgage Revenue Bond Programs (MRBP), government-insured mortgages and conventional mortgages. The MRBP division specializes in servicing loans made under state and local housing authority programs. These programs provide mortgages to low-income and moderate-income borrowers and are generally government-insured programs with a favorable rate subsidy, down payment and/or closing cost assistance. Mortgage loans originated as part of government agency and state loan programs tend to experience slower prepayment speeds and better cash flows than conventional mortgage loans. The servicing portfolios are predominantly comprised of fixed-rate agency loans (FNMA, FHLMC, GNMA, FHLB and various housing agencies) with limited adjustable-rate or jumbo mortgage loans.

A summary of the Company's MSR's and related characteristics by portfolio as of September 30, 2006, was as follows:

(Dollars in Millions)	MRBP	Government	Conventional	Total
Servicing portfolio	\$7,519	\$8,614	\$63,100	\$79,233
Fair market value	\$149	\$156	\$1,019	\$1,324
Value (bps) *	198	181	161	167
Weighted-average servicing fees (bps)	41	43	36	37
Multiple (value/servicing fees)	4.83	4.21	4.47	4.51
Weighted-average note rate	5.90%	6.11%	5.81%	5.85%
Age (in years)	3.4	3.0	2.3	2.5
Expected life (in years)	7.8	6.6	6.8	6.9
Discount rate	11.4%	11.3%	10.6%	10.8%

\* Value is calculated as fair market value divided by the servicing portfolio.

U.S. Bancorp

37

**Table of Contents****Note 6 Earnings Per Common Share**

The components of earnings per common share were:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
(Dollars and Shares in Millions, Except Per Share Data)				
Net income	\$1,203	\$1,154	\$3,557	\$3,346
Preferred dividends	16		33	
Net income applicable to common equity	\$1,187	\$1,154	\$3,524	\$3,346
Average common shares outstanding	1,771	1,823	1,784	1,836
Net effect of the assumed purchase of stock based on the treasury stock method for options and stock plans	25	26	25	26
Average diluted common shares outstanding	1,796	1,849	1,809	1,862
Earnings per common share	\$.67	\$.63	\$1.98	\$1.82
Diluted earnings per common share	\$.66	\$.62	\$1.95	\$1.80

Options to purchase 3 million and 15 million common shares for the three months ended September 30, 2006 and 2005, respectively, and 4 million and 16 million common shares for the nine months ended September 30, 2006 and 2005, respectively, were outstanding but not included in the computation of diluted earnings per common share because they were antidilutive.

**Note 7 Employee Benefits**

The components of net periodic benefit cost (income) for the Company's retirement plans were:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	Pension Plans		Post Retirement Medical Plans		Pension Plans		Post Retirement Medical Plans	
	2006	2005	2006	2005	2006	2005	2006	2005
(Dollars in Millions)								
Components of net periodic benefit cost (income)								
Service cost	\$18	\$16	\$1	\$1	\$54	\$48	\$3	\$3
Interest cost	29	28	3	4	88	84	10	12
Expected return on plan assets	(48)	(49)			(143)	(146)		(1)
Net amortization and deferral	(2)	(2)			(5)	(5)		
Recognized actuarial loss	23	15			68	44		1
Net periodic benefit cost (income)	\$20	\$8	\$4	\$5	\$62	\$25	\$13	\$15





**Table of Contents****Note 8 Stock-based Compensation**

As part of its employee and director compensation programs, the Company may grant certain stock awards under the provisions of the existing stock compensation plans, including plans assumed in acquisitions. The plans provide for grants of options to purchase shares of common stock at a fixed price equal to the fair value of the underlying stock at the date of grant. Option grants are generally exercisable up to ten years from the date of grant. In addition, the plans provide for grants of shares of common stock or stock units that are subject to restriction on transfer prior to vesting. Most stock awards vest over three to five years and are subject to forfeiture if certain vesting requirements are not met. At September 30, 2006, there were 14 million shares (subject to adjustment for forfeitures) available for grant under various plans.

The following is a summary of stock options outstanding and exercised under various stock options plans of the Company:

	2006				2005			
	Stock Options/ Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Weighted-Average Aggregate Remaining Intrinsic Value (in millions)	Stock Options/ Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Weighted-Average Aggregate Remaining Intrinsic Value (in millions)
Three Months Ended September 30,								
<b>Stock option plans</b>								
Number outstanding at beginning of period	118,714,340	\$25.30			137,980,612	\$24.14		
Granted	243,764	32.01			358,873	29.72		
Exercised	(9,697,953)	23.74			(4,433,540)	20.80		
Cancelled (a)	(474,450)	26.57			(1,555,920)	25.82		
Number outstanding at end of period (b)	108,785,701	\$25.44	5.1	\$846	132,350,025	\$24.25	5.2	\$507
Exercisable at end of period	78,958,789	\$24.39	3.9	\$697	96,067,471	\$23.86	4.3	\$405

	2006				2005			
	Stock Options/ Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Weighted-Average Aggregate Remaining Intrinsic Value (in millions)	Stock Options/ Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Weighted-Average Aggregate Remaining Intrinsic Value (in millions)
Nine Months Ended September 30,								
<b>Stock option plans</b>								
Number outstanding at beginning of period	125,983,461	\$24.38			134,727,285	\$23.41		

Granted	12,243,873	30.09			12,550,706	30.14		
Exercised	(27,499,487)	22.50			(11,830,576)	20.75		
Cancelled (a)	(1,942,146)	27.35			(3,097,390)	25.14		

Number outstanding at end of period (b)	108,785,701	\$25.44	5.1	\$846	132,350,025	\$24.25	5.2	\$507
Exercisable at end of period	78,958,789	\$24.39	3.9	\$697	96,067,471	\$23.86	4.3	\$405

(a) *Options cancelled includes both non-vested (i.e., forfeitures) and vested options.*

(b) *Outstanding options include stock-based awards that may be forfeited in future periods, however the impact of the estimated forfeitures is reflected in compensation expense.*

The weighted-average grant-date fair value of options granted was \$5.61 and \$6.14 for the three months ended September 30, 2006 and 2005, respectively, and was \$6.30 and \$6.66 for the nine months ended September 30, 2006 and 2005, respectively. The total intrinsic value of options exercised was \$83 million and \$41 million for the three months ended September 30, 2006 and 2005, respectively, and was \$245 million and \$109 million for the nine months ended September 30, 2006 and 2005, respectively. The total fair value of option shares vested was \$1 million and \$3 million for the three months ended September 30, 2006 and 2005, respectively, and was \$50 million and \$56 million for the nine months ended September 30, 2006 and 2005, respectively.

Cash received from option exercises under all share-based payment arrangements was \$215 million and \$89 million for the three months ended September 30, 2006 and 2005, respectively, and was \$603 million and \$242 million for the nine months ended September 30, 2006 and 2005, respectively. The tax benefit realized for the tax deductions from option exercises of the share-based payment arrangements totaled \$31 million and \$16 million for the three months ended September 30, 2006 and 2005, respectively, and totaled \$92 million and \$41 million for the nine months ended September 30, 2006 and 2005, respectively. To satisfy option exercises, the Company predominantly uses treasury stock.

U.S. Bancorp

39

**Table of Contents**

The fair value of each option award is estimated on the date of grant using the Black-Scholes option-pricing model, requiring the use of subjective assumptions. The following table includes the assumptions utilized by the Company for newly issued grants:

	Nine Months Ended September 30,	
	2006	2005
Risk-free interest rate	4.3%	3.6%
Dividend yield	4.0%	3.5%
Stock volatility factor	.28	.29
Expected life of options (in years)	5.4	5.4

Expected stock volatility is based on several factors including the historical volatility of the Company's stock, implied volatility determined from traded options and other factors. The Company uses historical data to estimate option exercises and employee terminations to estimate the expected life of options. The risk-free interest rate for the expected life of the options is based on the U.S. Treasury yield curve in effect on the date of grant. The expected dividend yield is based on the Company's expected dividend yield over the life of the options.

Additional information regarding stock options outstanding as of September 30, 2006, is as follows:

Range of Exercise Prices	Options Outstanding			Exercisable Options	
	Shares	Weighted- Average Remaining Contractual Life (Years)	Weighted- Average Exercise Price	Shares	Weighted- Average Exercise Price
\$5.83 - \$10.00	18,435	.5	\$ 7.96	18,435	\$ 7.96
\$10.01 - \$15.00	444,370	2.4	12.49	444,370	12.49
\$15.01 - \$20.00	14,383,656	4.4	18.81	14,228,938	18.81
\$20.01 - \$25.00	39,675,476	4.5	22.31	34,105,842	22.44
\$25.01 - \$30.00	39,543,850	5.3	29.06	23,948,583	28.76
\$30.01 - \$35.00	14,443,387	6.5	30.96	5,936,094	31.81
\$35.01 - \$36.95	276,527	.6	35.89	276,527	35.89
	108,785,701	5.1	\$25.44	78,958,789	\$24.39

A summary of the status of the Company's restricted shares of stock is presented below:

Three Months Ended September 30,		Nine Months Ended September 30,	
2006	2005	2006	2005

	Weighted-Average Grant-Date Fair Value		Weighted-Average Grant-Date Fair Value		Weighted-Average Grant-Date Fair Value		Weighted-Average Grant-Date Fair Value	
	Shares		Shares		Shares		Shares	
<b>Nonvested shares</b>								
Number outstanding at beginning of period	3,018,314	\$27.39	2,826,416	\$26.51	2,644,171	\$26.73	2,265,625	\$25.06
Granted	42,355	31.69	23,810	30.15	1,032,605	30.19	1,014,428	30.05
Cancelled/vested	(6,668)	29.76	(25,035)	22.18	(487,249)	28.90	(410,991)	26.50
Forfeited	(116,862)	30.36	(99,029)	26.65	(252,388)	29.76	(142,900)	27.38
Number outstanding at end of period	2,937,139	\$27.33	2,726,162	\$26.57	2,937,139	\$27.33	2,726,162	\$26.57

The total fair value of shares vested was \$1 million for the three months ended September 30, 2006 and 2005, respectively, and was \$15 million and \$13 million for the nine months ended September 30, 2006 and 2005, respectively.

Stock-based compensation expense was \$22 million and \$32 million for the three months ended September 30, 2006 and 2005, respectively, and was \$80 million and \$104 million for the nine months ended September 30, 2006 and 2005, respectively. At the time employee stock options expire, are exercised or cancelled, the Company determines the tax benefit associated with the stock award and under certain circumstances may be required to recognize an adjustment to tax expense. On an after-tax basis, stock-based compensation was \$14 million and \$20 million for three months ended September 30, 2006 and 2005, respectively, and was \$50 million and \$65 million for the nine months ended September 30, 2006 and 2005, respectively. As of September 30, 2006, there was \$118 million of total unrecognized compensation cost related to nonvested share-based compensation.

**Table of Contents**

arrangements granted under the plans. That cost is expected to be recognized over a weighted-average period of 3 years.

**Note 9** Income Taxes

The components of income tax expense were:

(Dollars in Millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
<b>Federal</b>				
Current	\$530	\$455	\$1,742	\$1,199
Deferred	(63)	61	(299)	189
Federal income tax	467	516	1,443	1,388
<b>State</b>				
Current	70	65	258	169
Deferred	(5)	5	(23)	16
State income tax	65	70	235	185
Total income tax provision	\$532	\$586	\$1,678	\$1,573

A reconciliation of expected income tax expense at the federal statutory rate of 35 percent to the Company's applicable income tax expense follows:

(Dollars in Millions)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Tax at statutory rate (35 percent)	\$607	\$609	\$1,832	\$1,722
State income tax, at statutory rates, net of federal tax benefit	43	45	153	120
Tax effect of				
Tax credits	(97)	(48)	(216)	(131)
Tax-exempt income	(23)	(19)	(66)	(50)
Resolution of federal and state income tax examinations				(94)
Other items	2	(1)	(25)	6
Applicable income taxes	\$532	\$586	\$1,678	\$1,573

Included in the second quarter of 2005 was a \$94 million reduction in income tax expense related to the resolution of federal income tax examinations covering substantially all of the Company's legal entities for the years 2000 through 2002. The resolution of these cycles was the result of negotiations held between the Company and representatives of

the Internal Revenue Service throughout the examinations. The resolution of these matters and the taxing authorities acceptance of submitted claims and tax return adjustments resulted in the reduction of estimated income tax liabilities.

The Company's net deferred tax liability was \$1,260 million at September 30, 2006, and \$1,615 million at December 31, 2005.

U.S. Bancorp

**41**

---

**Table of Contents****Note 10** Guarantees and Contingent Liabilities

The following table is a summary of the guarantees and contingent liabilities of the Company at September 30, 2006:

(Dollars in Millions)	Carrying Amount	Maximum Potential Future Payments
Standby letters of credit	\$79	\$10,886
Third-party borrowing arrangements	5	446
Securities lending indemnifications		15,136
Asset sales (a)	7	544
Merchant processing	52	62,664
Other guarantees	22	2,853
Other contingent liabilities	13	1,899

(a) *The maximum potential future payments does not include loans sales where the Company provides standard representations and warranties to the buyer against losses related to loan underwriting documentation. For these types of loans sales, the maximum potential future payments are not readily determinable because the Company's obligation under these agreements depends upon the occurrence of future events.*

The Company, through its subsidiaries, provides merchant processing services. Under the rules of credit card associations, a merchant processor retains a contingent liability for credit card transactions processed. This contingent liability arises in the event of a billing dispute between the merchant and a cardholder that is ultimately resolved in the cardholder's favor. In this situation, the transaction is charged-back to the merchant and the disputed amount is credited or otherwise refunded to the cardholder. If the Company is unable to collect this amount from the merchant, it bears the loss for the amount of the refund paid to the cardholder.

The Company currently processes card transactions in the United States, Canada and Europe for airlines, cruise lines and large tour operators. In the event of liquidation of these merchants, the Company could become financially liable for refunding tickets purchased through the credit card associations under the charge-back provisions. Charge-back risk related to these merchants is evaluated in a manner similar to credit risk assessments and, as such, merchant processing contracts contain various provisions to protect the Company in the event of default. At September 30, 2006, the value of airline, cruise line and large tour operator tickets purchased to be delivered at a future date was \$3.1 billion, with airline tickets representing 90 percent of that amount. The Company held collateral of \$2.1 billion in escrow deposits, letters of credit and indemnities from financial institutions, and liens on various assets.

The Company is subject to various litigation, investigations and legal and administrative cases and proceedings that arise in the ordinary course of its businesses. Due to their complex nature, it may be years before some matters are resolved. While it is impossible to ascertain the ultimate resolution or range of financial liability with respect to these contingent matters, the Company believes that the aggregate amount of such liabilities will not have a material adverse effect on the financial condition, results of operations or cash flows of the Company.

For information on the nature of the Company's guarantees and contingent liabilities, please refer to Note 23 in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.



**Table of Contents**

(This page intentionally left blank)

U.S. Bancorp

**43**

---

**Table of Contents**

U.S. Bancorp

Consolidated Daily Average Balance Sheet and Related Yields and Rates (a)

For the Three Months Ended September 30,  
2006 2005

(Dollars in Millions) (Unaudited)	Average Balances	Interest	Yields and Rates	Average Balances	Interest	Yields and Rates	% Change Average Balances
<b>Assets</b>							
Investment securities	\$39,806	\$519	5.22%	\$41,782	\$494	4.73%	(4.7)%
Loans held for sale	2,448	40	6.58	2,038	30	5.80	20.1
Loans (b)							
Commercial	46,068	769	6.63	43,251	642	5.89	6.5
Commercial real estate	28,701	538	7.44	28,193	463	6.52	1.8
Residential mortgages	21,118	313	5.90	18,741	261	5.54	12.7
Retail	47,007	956	8.07	45,098	808	7.11	4.2
Total loans	142,894	2,576	7.16	135,283	2,174	6.38	5.6
Other earning assets	2,042	40	7.73	1,349	29	8.56	51.4
Total earning assets	187,190	3,175	6.74	180,452	2,727	6.01	3.7
Allowance for loan losses	(2,056)			(2,109)			2.5
Unrealized gain (loss) on available-for-sale securities	(1,185)			(258)			*
Other assets	30,140			27,582			9.3
Total assets	\$214,089			\$205,667			4.1
<b>Liabilities and Shareholders</b>							
<b>Equity</b>							
Noninterest-bearing deposits	\$28,220			\$29,434			(4.1)
Interest-bearing deposits							
Interest checking	23,595	66	1.10	22,508	34	.61	4.8
Money market savings	26,116	151	2.30	28,740	94	1.30	(9.1)
Savings accounts	5,598	5	.40	5,777	4	.24	(3.1)
Time certificates of deposit less than \$100,000	13,867	137	3.93	13,263	101	3.01	4.6
Time deposits greater than \$100,000	22,579	281	4.93	21,262	181	3.37	6.2
Total interest-bearing deposits	91,755	640	2.77	91,550	414	1.79	.2
Short-term borrowings	23,601	334	5.60	22,248	205	3.66	6.1
Long-term debt	41,892	528	5.00	35,633	317	3.54	17.6
	157,248	1,502	3.79	149,431	936	2.49	5.2

<b>Total interest-bearing liabilities</b>			
Other liabilities	7,704	6,696	15.1
<b>Shareholders equity</b>			
Preferred equity	1,000		*
Common equity	19,917	20,106	(.9)
Total shareholders equity	20,917	20,106	4.0
<b>Total liabilities and shareholders equity</b>			
	\$214,089	\$205,667	4.1%
Net interest income	\$1,673	\$1,791	
Gross interest margin		2.95%	3.52%
Gross interest margin without taxable-equivalent increments		2.92	3.50
<b>Percent of Earning Assets</b>			
Interest income		6.74%	6.01%
Interest expense		3.18	2.06
Net interest margin		3.56%	3.95%
Net interest margin without taxable-equivalent increments		3.53%	3.93%

\* *Not meaningful*

(a) *Interest and rates are presented on a fully taxable-equivalent basis utilizing a tax rate of 35 percent.*

(b) *Interest income and rates on loans include loan fees. Nonaccrual loans are included in average loan balances.*

44

U.S. Bancorp

**Table of Contents**

U.S. Bancorp

Consolidated Daily Average Balance Sheet and Related Yields and Rates (a)

For the Nine Months Ended September 30,  
2006 2005

(Dollars in Millions) (Unaudited)	Average Balances	Interest	Yields and Rates	Average Balances	Interest	Yields and Rates	% Change Average Balances
<b>Assets</b>							
Investment securities	\$39,858	\$1,528	5.11%	\$42,308	\$1,459	4.60%	(5.8)%
Loans held for sale	2,062	99	6.42	1,723	75	5.77	19.7
Loans (b)							
Commercial	45,029	2,193	6.51	42,263	1,833	5.79	6.5
Commercial real estate	28,704	1,563	7.28	27,762	1,313	6.33	3.4
Residential mortgages	20,992	909	5.78	17,266	718	5.55	21.6
Retail	46,334	2,704	7.80	44,141	2,259	6.84	5.0
Total loans	141,059	7,369	6.98	131,432	6,123	6.23	7.3
Other earning assets	2,096	119	7.55	1,388	84	8.12	51.0
Total earning assets	185,075	9,115	6.58	176,851	7,741	5.85	4.7
Allowance for loan losses	(2,056)			(2,116)			2.8
Unrealized gain (loss) on available-for-sale securities	(1,140)			(247)			*
Other assets	30,309			27,017			12.2
Total assets	\$212,188			\$201,505			5.3
<b>Liabilities and Shareholders</b>							
<b>Equity</b>							
Noninterest-bearing deposits	\$28,666			\$29,003			(1.2)
Interest-bearing deposits							
Interest checking	23,358	161	.92	22,891	98	.58	2.0
Money market savings	26,820	405	2.02	29,517	243	1.10	(9.1)
Savings accounts	5,669	14	.34	5,876	12	.27	(3.5)
Time certificates of deposit less than \$100,000	13,688	377	3.68	13,132	281	2.86	4.2
Time deposits greater than \$100,000	22,255	764	4.59	20,133	449	2.98	10.5
Total interest-bearing deposits	91,790	1,721	2.51	91,549	1,083	1.58	.3
Short-term borrowings	23,398	884	5.05	18,313	460	3.36	27.8
Long-term debt	40,462	1,415	4.67	36,016	895	3.32	12.3
	155,650	4,020	3.45	145,878	2,438	2.23	6.7

<b>Total interest-bearing liabilities</b>			
Other liabilities	7,329	6,713	9.2
<b>Shareholders equity</b>			
Preferred equity	688		*
Common equity	19,855	19,911	(.3)
Total shareholders equity	20,543	19,911	3.2
<b>Total liabilities and shareholders equity</b>			
	\$212,188	\$201,505	5.3%
Net interest income	\$5,095	\$5,303	
Gross interest margin		3.13%	3.62%
Gross interest margin without taxable-equivalent increments		3.11	3.60
<b>Percent of Earning Assets</b>			
Interest income		6.58%	5.85%
Interest expense		2.90	1.85
Net interest margin		3.68%	4.00%
Net interest margin without taxable-equivalent increments		3.66%	3.98%

\* *Not meaningful*

(a) *Interest and rates are presented on a fully taxable-equivalent basis utilizing a tax rate of 35 percent.*

(b) *Interest income and rates on loans include loan fees. Nonaccrual loans are included in average loan balances.*

U.S. Bancorp

45

**Table of Contents**

Part II Other Information

**Item 1A. Risk Factors** There are a number of factors that may adversely affect the Company's business, financial results or stock price. Refer to Risk Factors in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for discussion of these risks. The risks described in the Company's Annual Report on Form 10-K are not the only risks facing the Company. Additional risks that the Company currently does not know about or currently views as immaterial may also impair the Company's business or adversely impact its financial results or stock price.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds** Refer to the Capital Management section within Management's Discussion and Analysis in Part I for information regarding shares repurchased by the Company during the third quarter of 2006.

**Item 6. Exhibits**

- 12 Computation of Ratio of Earnings to Fixed Charges
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934
- 32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. section 1350 as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002

**Table of Contents**

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

U.S. BANCORP  
By: /s/ Terrance R. Dolan

Terrance R. Dolan  
Executive Vice President and Controller  
(Chief Accounting Officer and Duly Authorized Officer)

DATE: November 9, 2006  
U.S. Bancorp

**47**

---

**Table of Contents****EXHIBIT 12****Computation of Ratio of Earnings to Fixed Charges**

(Dollars in Millions)	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2006
<b>Earnings</b>		
1. Net income	\$1,203	\$3,557
2. Applicable income taxes	532	1,678
3. Income before income taxes (1 + 2)	\$1,735	\$5,235
<b>4. Fixed charges:</b>		
a. Interest expense excluding interest on deposits	\$849	\$2,276
b. Portion of rents representative of interest and amortization of debt expense	18	53
c. Fixed charges excluding interest on deposits (4a + 4b)	867	2,329
d. Interest on deposits	640	1,721
e. Fixed charges including interest on deposits (4c + 4d)	\$1,507	\$4,050
5. Amortization of interest capitalized	\$	\$
6. Earnings excluding interest on deposits (3 + 4c + 5)	2,602	7,564
7. Earnings including interest on deposits (3 + 4e + 5)	3,242	9,285
8. Fixed charges excluding interest on deposits (4c)	867	2,329
9. Fixed charges including interest on deposits (4e)	1,507	4,050
<b>Ratio of Earnings to Fixed Charges</b>		
10. Excluding interest on deposits (line 6/line 8)	3.00	3.25
11. Including interest on deposits (line 7/line 9)	2.15	2.29



**Table of Contents**

**EXHIBIT 31.1**

**CERTIFICATION PURSUANT TO  
RULE 13a-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934**

I, Jerry A. Grundhofer, certify that:

- (1) I have reviewed this Quarterly Report on Form 10-Q of U.S. Bancorp;
- (2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
- (4) The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
- (5) The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Jerry A. Grundhofer

Jerry A. Grundhofer  
*Chief Executive Officer*

Dated: November 9, 2006  
U.S. Bancorp

**Table of Contents**

**EXHIBIT 31.2**

**CERTIFICATION PURSUANT TO  
RULE 13a-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934**

I, David M. Moffett, certify that:

- (1) I have reviewed this Quarterly Report on Form 10-Q of U.S. Bancorp;
- (2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
- (4) The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
- (5) The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ David M. Moffett

David M. Moffett  
*Chief Financial Officer*

Dated: November 9, 2006

**50**

U.S. Bancorp

---

**Table of Contents**

**EXHIBIT 32**

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned, Chief Executive Officer and Chief Financial Officer of U.S. Bancorp, a Delaware corporation (the Company ), do hereby certify that:

- (1) The Quarterly Report on Form 10-Q for the quarter ended September 30, 2006 (the Form 10-Q ) of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Jerry A. Grundhofer

/s/ David M. Moffett

Jerry A. Grundhofer  
*Chief Executive Officer*

David M. Moffett  
*Chief Financial Officer*

Dated: November 9, 2006  
U.S. Bancorp

**Table of Contents**

First Class  
U.S. Postage  
PAID  
Permit No. 2440  
Minneapolis, MN

Corporate Information

**Executive Offices**

U.S. Bancorp  
800 Nicollet Mall  
Minneapolis, MN 55402

**Common Stock Transfer Agent and Registrar**

Mellon Investor Services acts as our transfer agent and registrar, dividend paying agent and dividend reinvestment plan administrator, and maintains all shareholder records for the corporation. Inquiries related to shareholder records, stock transfers, changes of ownership, lost stock certificates, changes of address and dividend payment should be directed to the transfer agent at:

Mellon Investor Services  
P.O. Box 3315  
South Hackensack, NJ 07606-1915  
Phone: 888-778-1311 or 201-680-4000

Internet: [melloninvestor.com](http://melloninvestor.com)

For Registered or Certified Mail:

Mellon Investor Services  
480 Washington Boulevard  
Jersey City, NJ 07310

Telephone representatives are available weekdays from 8:00 a.m. to 6:00 p.m. Central Time, and automated support is available 24 hours a day, 7 days a week. Specific information about your account is available on Mellon's internet site by clicking on For Investors and then the Investor ServiceDirect® link.

**Independent Auditors**

Ernst & Young LLP serves as the independent auditors of U.S. Bancorp's financial statements.

**Common Stock Listing and Trading**

U.S. Bancorp common stock is listed and traded on the New York Stock Exchange under the ticker symbol USB.

**Dividends and Reinvestment Plan**

U.S. Bancorp currently pays quarterly dividends on our common stock on or about the 15th day of January, April, July and October, subject to approval by our Board of Directors. U.S. Bancorp shareholders can choose to participate in a plan that provides automatic reinvestment of dividends and/or optional cash purchase of additional shares of U.S. Bancorp common stock. For more information, please contact our transfer agent, Mellon Investor Services. See above.

**Investment Community Contacts**

Judith T. Murphy  
Senior Vice President, Investor Relations  
[judith.murphy@usbank.com](mailto:judith.murphy@usbank.com)  
Phone: 612-303-0783 or 866-775-9668

**Financial Information**

U.S. Bancorp news and financial results are available through our web site and by mail.

*Web site.* For information about U.S. Bancorp, including news, financial results, annual reports and other documents filed with the Securities and Exchange Commission, access our home page on the Internet at [usbank.com](http://usbank.com), click on About U.S. Bancorp, then Investor/Shareholder Information.

*Mail.* At your request, we will mail to you our quarterly earnings, news releases, quarterly financial data reported on Form 10-Q and additional copies of our annual reports. Please contact:

U.S. Bancorp Investor Relations  
800 Nicollet Mall  
Minneapolis, Minnesota 55402  
investorrelations@usbank.com  
Phone: 866-775-9668

**Media Requests**

Steven W. Dale  
Senior Vice President, Media Relations  
steve.dale@usbank.com  
Phone: 612-303-0784

**Privacy**

U.S. Bancorp is committed to respecting the privacy of our customers and safeguarding the financial and personal information provided to us. To learn more about the U.S. Bancorp commitment to protecting privacy, visit [usbank.com](http://usbank.com) and click on Privacy Pledge.

**Code of Ethics**

U.S. Bancorp places the highest importance on honesty and integrity. Each year, every U.S. Bancorp employee certifies compliance with the letter and spirit of our Code of Ethics and Business Conduct, the guiding ethical standards of our organization. For details about our Code of Ethics and Business Conduct, visit [usbank.com](http://usbank.com) and click on About U.S. Bancorp, then Ethics at U.S. Bank.

**Diversity**

U.S. Bancorp and our subsidiaries are committed to developing and maintaining a workplace that reflects the diversity of the communities we serve. We support a work environment where individual differences are valued and respected and where each individual who shares the fundamental values of the company has an opportunity to contribute and grow based on individual merit.

**Equal Employment Opportunity/Affirmative Action**

U.S. Bancorp and our subsidiaries are committed to providing Equal Employment Opportunity to all employees and applicants for employment. In keeping with this commitment, employment decisions are made based upon performance, skill and ability, not race, color, religion, national origin or ancestry, gender, age, disability, veteran status, sexual orientation or any other factors protected by law. The corporation complies with municipal, state and federal fair employment laws, including regulations applying to federal contractors.

U.S. Bancorp, including each of our subsidiaries, is an Equal Opportunity Employer committed to creating a diverse workforce.

U.S. Bancorp  
Member FDIC

This report has been produced on recycled paper.