NAVARRO IMELDA
Form 4
December 05, 2008

# FORM 4

Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. *See* Instruction 1(b).

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**
**Washington, D.C. 20549**

**STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES**

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

OMB APPROVAL

| | |
|---|---|
| OMB Number: | 3235-0287 |
| Expires: | January 31, 2005 |
| Estimated average burden hours per response... | 0.5 |

(Print or Type Responses)

1. Name and Address of Reporting Person *
NAVARRO IMELDA

(Last) (First) (Middle)

P.O. BOX 1359

(Street)

LAREDO, TX 78040

(City) (State) (Zip)

2. Issuer Name **and** Ticker or Trading Symbol
INTERNATIONAL BANCSHARES CORP [IBOC]

3. Date of Earliest Transaction (Month/Day/Year)
12/04/2008

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

__X__ Director _____ 10% Owner
_____ Officer (give title below) _____ Other (specify below)

6. Individual or Joint/Group Filing(Check Applicable Line)
_X_ Form filed by One Reporting Person
___ Form filed by More than One Reporting Person

**Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned**

| 1.Title of Security (Instr. 3) | 2. Transaction Date (Month/Day/Year) | 2A. Deemed Execution Date, if any (Month/Day/Year) | 3. Transaction Code (Instr. 8) | | 4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5) | | | 5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4) | 6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4) | 7. Nature of Indirect Beneficial Ownership (Instr. 4) |
|---|---|---|---|---|---|---|---|---|---|---|
| | | | Code | V | Amount | (A) or (D) | Price | | | |
| COMMON STOCK | 12/04/2008 | | S | | 6,919 | D | $ 23.3 | 243,550 | D | |

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 1474 (9-02)

**Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned**
**(*e.g.*, puts, calls, warrants, options, convertible securities)**

| 1. Title of Derivative Security (Instr. 3) | 2. Conversion or Exercise Price of Derivative Security | 3. Transaction Date (Month/Day/Year) | 3A. Deemed Execution Date, if any (Month/Day/Year) | 4. Transaction Code (Instr. 8) | | 5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5) | | 6. Date Exercisable and Expiration Date (Month/Day/Year) | | 7. Title and Amount of Underlying Securities (Instr. 3 and 4) | | 8. Price of Derivative Security (Instr. 5) | 9. Nu Deriv Secur Bene Owne Follo Repo Trans (Instr |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | Code | V | (A) | (D) | Date Exercisable | Expiration Date | Title | Amount or Number of Shares | | |

## Reporting Owners

| Reporting Owner Name / Address | Relationships | | | |
|---|---|---|---|---|
| | Director | 10% Owner | Officer | Other |
| NAVARRO IMELDA<br>P.O. BOX 1359<br>LAREDO, TX 78040 | X | | | |

## Signatures

| /S/IMELDA NAVARRO | 12/04/2008 |
|---|---|
| **Signature of Reporting Person | Date |

## Explanation of Responses:

* If the form is filed by more than one reporting person, *see* Instruction 4(b)(v).

** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, *see* Instruction 6 for procedure.
Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. reasonably practicable after such reports are electronically filed with or furnished to the SEC. The Board of Directors of the Company has also adopted and posted in the Investor Relations section of its website the Company's Corporate Governance Guidelines and charters for each of the Board's standing committees. A copy of the above filings will also be provided free of charge upon written request to the Company.

**Certifications**

*New York Stock Exchange Annual Chief Executive Officer Certification*
The Company's Chief Executive Officer submitted to the New York Stock Exchange ("NYSE") the Annual CEO Certification as the Company's compliance with the NYSE's corporate governance listing standards required by Section 303A.12 of the NYSE's listing standards.

*Sarbanes-Oxley Act Section 302 Certification*
The certifications of the Chief Executive Officer and Chief Financial Officer of the Company pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 have been filed as exhibits to this Annual Report on Form 10-K.

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Item 1A. **RISK FACTORS**

*The following are certain risk factors that could affect our business, financial condition, results of operations, and cash flows. These risk factors should be considered in connection with evaluating the forward-looking statements contained in this Annual Report on Form 10-K because these factors could cause the actual results and conditions to differ materially from those projected in forward-looking statements. Before you invest in our publicly traded securities, you should know that making such an investment involves some risks, including the risks described below. If any of the risks actually occur, our business, financial condition or results of operations could be negatively affected. In that case, the trading price of our Class A common shares could decline, and you may lose all or part of your investment.*

**Risks Relating to Our Businesses**

***Currency exchange rate, commodity price and interest rate fluctuations may adversely affect our results.***

We are exposed to a variety of market risks, including the effects of changes in non-U.S. currency exchange rates, commodity prices and interest rates. See Part II Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

More than 40% of our 2006 net revenues were derived outside the U.S., and we expect sales to non-U.S. customers to continue to represent a significant portion of our consolidated net revenues. Therefore, in the case where we manufacture our products in the U.S. and the U.S. dollar strengthens in relation to the currencies of the countries where we sell those products, such as the euro and Asian currencies, our U.S. dollar reported revenue and income will decrease. Although we enter into currency exchange contracts to reduce our risk related to currency exchange fluctuations, changes in the relative values of currencies occur from time to time and may, in some instances, have a significant effect on our results of operations. Furthermore, the reporting currency for our financial statements is the U.S. dollar. We have assets, liabilities, revenues and expenses denominated in currencies other than the U.S. dollar. To prepare our consolidated financial statements, we must translate those assets, liabilities, revenues and expenses into U.S. dollars at the applicable exchange rates. Consequently, increases and decreases in the value of the U.S. dollar versus other currencies will affect the amount of these items in our consolidated financial statements, even if their value has not changed in their original currency. Because we do not hedge against all of our currency exposure, our business will continue to be susceptible to currency fluctuations.

We are a large buyer of steel and non-ferrous metals, as well as other commodities required for the manufacture of our products. Volatility in the prices of these commodities could increase the costs of our products and services. We may not be able to pass on these costs to our customers and this could have a material adverse effect on our results of operations and cash flows. On a limited basis, we purchase commodity derivatives which reduce the volatility of the commodity prices for supplier contracts where fixed pricing is not available.

***Material adverse legal judgments, fines, penalties or settlements could adversely affect our financial health.***

We estimate that our available cash and our cash flow from operations will be adequate to fund our operations for the foreseeable future. In making this estimate, we have not assumed the need to make any material payments in connection with any pending litigation or investigations. As required by U.S. generally accepted accounting principles, we establish reserves based on our assessment of contingencies. Subsequent developments in legal proceedings, including current or future asbestos-related litigation, may affect our assessment and estimates of the loss contingency recorded as a reserve requiring us to make additional material payments, which could result in an adverse effect on our results of operations.

Such an outcome could have important consequences. For example, it could:

- increase our vulnerability to general adverse economic and industry conditions;
- limit our flexibility in planning for, or reacting to, changes in our businesses and the industries in which we operate;
- restrict our ability to exploit business opportunities; and
- make it more difficult for us to satisfy our payment obligations with respect to our outstanding indebtedness.

***Significant shortages in the raw materials we use in our businesses could increase our operating costs.***

We rely on suppliers to secure raw materials, particularly steel and non-ferrous metals, required for the manufacture of our products. A disruption in deliveries from our suppliers or decreased availability of raw materials or commodities could have an adverse effect on our ability to meet our commitments to customers or increase our operating costs. We believe that available sources of supply will generally be sufficient for our needs for the foreseeable future. Nonetheless, the unavailability of some raw materials may have an adverse effect on our results of operations or financial condition.

Due to the instability of market prices, the Company is exposed to large fluctuations for the price of petroleum-based fuel. Higher energy costs increase our operating costs and the cost of shipping our products to customers around the world. Consequently, sharp price increases, the imposition of taxes or an interruption of supply, could cause the Company to lose the ability to effectively manage the risk of rising fuel prices and our operating income could be further affected.

***Our global operations subject us to economic risks.***

Our global operations are dependent upon products manufactured, purchased and sold in the U.S. and internationally, including China, Brazil, Africa and Eastern Europe. These activities are subject to risks that are inherent in operating globally, including the following:

- countries could change regulations or impose currency restrictions and other restraints;
- in some countries, there is a risk that the government may expropriate assets;
- some countries impose burdensome tariffs and quotas;
- national and international conflict, including terrorist acts, could significantly impact our financial condition and results of operations; and
- economic downturns, political instability and war or civil disturbances may disrupt production and distribution logistics or limit sales in individual markets.

***Implementing our acquisition strategy involves risks and our failure to successfully implement this strategy could have a material adverse effect on our business.***

One of our key strategies is to grow our business by selectively pursuing bolt-on acquisitions. Since 2000, we have completed approximately 65 acquisitions, and we are continuing to actively pursue additional bolt-on acquisition opportunities. Although we have been successful with this strategy in the past, we may not be able to grow our business in the future through acquisitions for a number of reasons, including:

- encountering difficulties identifying and executing acquisitions;
- increased competition for targets, which may increase acquisition costs;
- consolidation in our industries reducing the number of acquisition targets; and
- competition laws and regulations preventing us from making certain acquisitions.

In addition, there are potential risks associated with growing our business through acquisitions, including the failure to successfully integrate and realize the expected benefits of an acquisition. For example, with any past or future acquisition, there is the possibility that:

- the business culture of the acquired business may not match well with our culture;
- technological and product synergies, economies of scale and cost reductions may not occur as expected;
- management may be distracted from overseeing existing operations by the need to integrate acquired businesses;
- we may acquire or assume unexpected liabilities;
- unforeseen difficulties may arise in integrating operations and systems;
- we may fail to retain and assimilate employees of the acquired business; and
- we may experience problems in retaining customers and integrating customer bases.

Failure to continue implementing our acquisition strategy, including successfully integrating acquired businesses, could have a material adverse effect on our business, financial condition and results of operations.

***Our reputation and our ability to do business may be impaired by improper conduct by any of our employees or agents.***

We do business in many parts of the world that have experienced governmental corruption. Our corporate policy requires strict compliance with the U.S. Foreign Corrupt Practices Act and with local laws prohibiting payments to government officials for the purpose of obtaining or keeping business or otherwise obtaining favorable treatment. Improper actions by our employees or agents could subject us to civil or criminal penalties, including substantial monetary fines, as well as disgorgement, and could damage our reputation and, therefore, our ability to do business.

**Risks Relating to Our Reorganization as a Bermuda Company**

The reorganization exposed us or our shareholders to the risks described below. In addition, we cannot be assured that the anticipated benefits of the reorganization will be realized.

***Changes in tax laws, adverse determinations by taxing authorities and changes in our status under U.S. tax laws could increase our tax burden and affect our operating results, as well as subject our shareholders to additional taxes.***

While our U.S. operations are subject to U.S. tax, we believe that our non-U.S. operations are generally not subject to U.S. tax other than withholding taxes. The realization of this or any other tax benefit of the reorganization could be impacted by changes in tax laws, tax treaties or tax regulations or the interpretation or enforcement thereof by the Internal Revenue Service or any other tax authority. We believe that our risks have been diminished by the enactment of the American Jobs Creation Act of 2004. The American Jobs Creation Act includes a provision that denies tax benefits to companies that have reincorporated after March 4, 2003. We completed our reincorporation in Bermuda on December 31, 2001, and therefore our transaction is grandfathered by the American Jobs Creation Act. In addition, we believe that neither we nor IR-New Jersey will incur significant U.S. federal income or withholding taxes as a result of the transfer of the transferred shares. However, we cannot give any assurances that anticipated tax costs with respect to the transferred shares will ultimately be borne out and that the Internal Revenue Service will not contest our determination in the course of its audit. The inability to realize any of these benefits could have a material impact on our operating results.

A non-U.S. corporation, such as the Company, will constitute a "controlled foreign corporation" or "CFC" for U.S. federal income tax purposes if certain ownership criteria are met. Although we believe that we and our non-U.S. subsidiaries currently are not CFCs, the U.S. Internal Revenue Service or a court may not concur with our conclusions. If the IRS or a court determined that we were a CFC, then each of our U.S. shareholders who own (directly, indirectly, or constructively) 10% or more of the total combined voting power of all classes of our stock on the last day of our taxable year (a "10% U.S. Voting Shareholder") would be required to include in gross income for U.S. federal income tax purposes its pro rata share of our “subpart F income" (and the subpart F income of any our subsidiaries determined to be a CFC) for the period during which we (and our non-U.S. subsidiaries) were a CFC. In addition, gain on the sale of our shares realized by such a shareholder may be treated as ordinary income to the extent of the shareholder's proportionate share of our and our CFC subsidiaries' undistributed earnings and profits accumulated during the shareholder's holding period of the shares while we are a CFC.

***Legislation regarding non-U.S. chartered companies could adversely affect us and our subsidiaries.***

The U.S. federal government and various other states and municipalities have proposed or may propose legislation intended to deny government contracts to U.S. companies that reincorporate outside of the U.S. For instance, The Homeland Security Appropriations Act, signed into law October 18, 2004, includes a provision that prohibits reincorporated companies from entering into contracts with the Department of Homeland Security for funds available under the Homeland Security Appropriations Act. In addition, the State of California adopted legislation intended to limit the eligibility of certain Bermuda and other non-U.S. chartered companies to participate in certain state contracts and the State of North Carolina enacted a bill that provides a preference for North Carolina or U.S. products and services. Generally, these types of legislation relate to direct sales and distribution, while we typically sell our products through distributors. However, we are unable to predict with any level of certainty the likelihood or final form of these types of legislation, the nature of regulations that may be promulgated thereunder, or the impact such enactments and increased regulatory scrutiny may have on our business. We cannot provide any assurance that the impact on us of any adopted or proposed legislation in this area will not be materially adverse to our operations.

Explanation of Responses:

***Bermuda law differs from the laws in effect in the United States and may afford less protection to holders of our securities.***

We are organized under the laws of Bermuda. It may not be possible to enforce court judgments in Bermuda that are obtained in the U.S. against us or our directors or officers in Bermuda based on the civil liability provisions of the U.S. federal or state securities laws. We have been advised that the U.S. and Bermuda do not currently have a treaty providing for the reciprocal recognition and enforcement of judgments in civil and commercial matters. Therefore, a final judgment for the payment of money rendered by any U.S. federal or state court based on civil liability, whether or not based solely on U.S. federal or state securities laws, would not automatically be enforceable in Bermuda.

In addition, as a result of Bermuda law, it would be difficult for a holder of our securities to effect service of process within the United States. However, we have irrevocably agreed that we may be served with process with respect to actions based on offers and sales of securities made in the United States by having Ingersoll-Rand Company, 155 Chestnut Ridge Road, Montvale, New Jersey 07645, be our U.S. agent appointed for that purpose.

Bermuda companies are governed by the Companies Act 1981 of Bermuda, which differs in some material respects from laws generally applicable to U.S. corporations and shareholders, including, among others, differences relating to interested director and officer transactions, shareholder lawsuits and indemnification. Under Bermuda law, the duties of directors and officers of a Bermuda company are generally owed to the company only. Shareholders of Bermuda companies do not generally have rights to take action against directors or officers of the company, and may only do so in limited circumstances. Under Bermuda law, a company may also agree to indemnify directors and officers for any personal liability, not involving fraud or dishonesty, incurred in relation to the company. Thus, our shareholders may have more difficulty protecting their interests than would holders of securities of a corporation incorporated in a jurisdiction of the U.S.

## Item 1B. **UNRESOLVED STAFF COMMENTS**

None.

## Item 2. **PROPERTIES**

Manufacturing and assembly operations are conducted in 39 plants in the United States; 31 plants in Europe; 16 plants in Asia; 8 plants in Latin America; and 2 plants in Canada. The Company also maintains various warehouses, offices and repair centers throughout the world.

Substantially all plant facilities are owned by the Company and the remainder are under long-term lease arrangements. The Company believes that its plants and equipment have been well maintained and are generally in good condition.

Facilities under long-term lease arrangements are included below and are not significant to each operating segment's total number of plants or square footage.

Climate Control Technologies’ manufacturing locations are as follows:

| | Number of Plants | Approximate Square Footage |
|---|---|---|
| United States | 10 | 3,874,000 |
| Non - U.S. | 15 | 2,513,000 |
| **Total** | 25 | 6,387,000 |

Compact Vehicle Technologies’ manufacturing facilities are as follows:

| | Number of Plants | Approximate Square Footage |
|---|---|---|
| United States | 3 | 1,395,000 |
| Non - U.S. | 2 | 254,000 |
| **Total** | 5 | 1,649,000 |

Construction Technologies’ manufacturing facilities are as follows:

| | Number of Plants | Approximate Square Footage |
|---|---|---|
| United States | 6 | |
| Non - U.S. | 5 | |

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**Notes to Consolidated Financial Statements (Unaudited)**

**1. Basis of Presentation**

As used in these Notes, references to Key, we, our, us and similar terms refer to the consolidated entity c
refers solely to the parent holding company, and KeyBank refers to KeyCorp s subsidiary, KeyBank National Asso
We have provided the following list of acronyms and abbreviations as a tool for the reader. The acronyms and abbre
Notes to Consolidated Financial Statements (Unaudited) as well as Management s Discussion & Analysis of Financ

**AICPA:** American Institute of Certified Public Accountants.
**ALCO:** Asset/Liability Management Committee.
**A/LM:** Asset/liability management.
**AOCI:** Accumulated other comprehensive income (loss).
**Austin:** Austin Capital Management, Ltd.
**CMO:** Collateralized mortgage obligation.
**Common Shares:** Common Shares, $1 par value.
**CPP:** Capital Purchase Program of the U.S. Treasury.
**DIF:** Deposit Insurance Fund.
**Dodd-Frank Act:** Dodd-Frank Wall Street Reform and Consumer Protection Act
**ERM:** Enterprise risk management.
**EVE:** Economic value of equity.
**FASB:** Financial Accounting Standards Board.
**FDIC:** Federal Deposit Insurance Corporation.
**Federal Reserve:** Board of Governors of the Federal Reserve System**.**
**FHLMC:** Federal Home Loan Mortgage Corporation.
**FNMA:** Federal National Mortgage Association.

**N/M:** Not meaningful.
**NOW:** Negotiable Order of With
**NYSE:** New York Stock Exchan
**OCI:** Other comprehensive incor
**OREO:** Other real estate owned.
**OTTI:** Other-than-temporary im
**QSPE:** Qualifying special purpos
**PBO:** Projected Benefit Obligatio
**S&P:** Standard and Poor s Ratin Companies, Inc.
**SCAP:** Supervisory Capital Asse Reserve.
**SEC:** U.S. Securities & Exchang
**Series A Preferred Stock:** KeyC Convertible Preferred Stock, Seri
**Series B Preferred Stock:** KeyC Preferred Stock, Series B issued t
**SILO**: Sale in, lease out transacti

**GAAP:** U.S. generally accepted accounting principles.
**GNMA:** Government National Mortgage Association.
**Heartland:** Heartland Payment Systems, Inc.
**IRS:** Internal Revenue Service.
**ISDA:** International Swaps and Derivatives Association.
**KAHC:** Key Affordable Housing Corporation.
**LIBOR:** London Interbank Offered Rate.
**LIHTC:** Low-income housing tax credit.
**LILO:** Lease in, lease out transaction.
**Moody s:** Moody s Investors Service, Inc.
**N/A:** Not applicable.
**NASDAQ:** National Association of Securities Dealers Automated Quotation System.

**SPE:** Special purpose entity.
**TAG:** Transaction Account Guar
**TARP**: Troubled Assets Relief P
**TE:** Taxable equivalent.
**TLGP:** Temporary Liquidity Gu
**U.S. Treasury:** United States De
**VAR:** Value at risk.
**VEBA:** Voluntary Employee Be
**VIE:** Variable interest entity.
**XBRL:** eXtensible Business Rep

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The consolidated financial statements include the accounts of KeyCorp and its subsidiaries. All significant intercom
eliminated in consolidation.

The consolidated financial statements include any voting rights entities in which we have a controlling financial inte
accounting guidance for consolidations, we also consolidate a VIE if we have: (i) a variable interest in the entity; (ii)
most significantly impact the entity s economic performance; and (iii) the obligation to absorb losses of the entity th
or the right to receive benefits from the entity that could potentially be significant to the VIE (i.e., we are considered
interests can include equity interests, subordinated debt, derivative contracts, leases, service agreements, guarantees,
and other contracts, agreements and financial instruments. See Note 7 ( Variable Interest Entities ) for information

We use the equity method to account for unconsolidated investments in voting rights entities or VIEs if we have sig
and financing decisions (usually defined as a voting or economic interest of 20% to 50%, but not controlling). Unco
or VIEs in which we have a voting or economic interest of less than 20% generally are carried at cost. Investments h
investment company subsidiaries (primarily principal investments) are carried at fair value.

Effective January 1, 2010, we prospectively adopted new accounting guidance which changes the way we account fo
concept of a QSPE and changing the requirements for derecognition of financial assets. In adopting this guidance, w
possible consolidation. As a result, we consolidated our education loan securitization trusts thereby adding $2.8 billi
balance sheet including $2.6 billion of loans. Prior to January 1, 2010, QSPEs, including securitization trusts, establi
guidance for transfers of financial assets were not consolidated. For additional information related to the consolidati
see the section entitled Accounting Standards Adopted in 2010 in this note and Note 16 ( Discontinued Operatio

We believe that the unaudited condensed consolidated interim financial statements reflect all adjustments of a norm
necessary for a fair presentation of the results for the interim periods presented. Some previously reported amounts h
reporting practices.

The results of operations for the interim period are not necessarily indicative of the results of operations to be expec
statements should be read in conjunction with the audited consolidated financial statements and related notes include

In preparing these financial statements, subsequent events were evaluated through the time the financial statements w
considered issued when they are widely distributed to all shareholders and other financial statement users, or filed w
accounting standards, all material subsequent events have been either recognized in the financial statements or discl

**Goodwill and Other Intangible Assets**

In accordance with relevant accounting guidance, goodwill and certain other intangible assets are subject to impairm
annually. We perform goodwill impairment testing in the fourth quarter of each year. Our reporting units for purpos
Community Banking and National Banking. Due to uncertainty regarding the strength of the economic recovery, we
indicators for goodwill and other intangible assets, and to evaluate the carrying amount of these assets as necessary.

Based on our review of impairment indicators during the first and second quarters of 2010, we determined that furth
Community Banking unit were necessary. These reviews indicated the estimated fair value of the Community Banki
amount

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at both June 30, 2010 and March 31, 2010. No further impairment testing was required. There was no goodwill asso
June 30, 2010 or March 31, 2010.

**Offsetting Derivative Positions**

In accordance with the applicable accounting guidance related to the offsetting of certain derivative contracts on the impact of bilateral collateral and master netting agreements that allow us to settle all derivative contracts held with a offset the net derivative position with the related collateral when recognizing derivative assets and liabilities. Additi offsetting is provided in Note 14 ( Derivatives and Hedging Activities ).

**Accounting Guidance Adopted in 2010**

***Transfers of financial assets.*** In June 2009, the FASB issued new accounting guidance which changes the way entit eliminating the concept of a QSPE and changing the requirements for derecognition of financial assets. This guidanc was effective at the start of an entity s first fiscal year beginning after November 15, 2009 (effective January 1, 201 have a material effect on our financial condition or results of operations.

***Consolidation of variable interest entities.*** In June 2009, the FASB issued new accounting guidance which, in addit changes how a company determines when an entity that is insufficiently capitalized or is not controlled through voti The determination of whether a company is required to consolidate an entity is based on, among other things, the en ability to direct the activities that most significantly impact the entity s economic performance. This guidance was e year beginning after November 15, 2009 (effective January 1, 2010, for us).

In conjunction with our prospective adoption of this guidance on January 1, 2010, we consolidated our education loa discontinued assets and liabilities), thereby adding $2.8 billion in assets and liabilities to our balance sheet, of which In February 2010, the FASB deferred the application of this new guidance for certain investment entities and clarifie qualifying for this deferral will continue to apply the previously existing consolidation guidance.

***Improving disclosures about fair value measurements.*** In January 2010, the FASB issued accounting guidance whi aspects of an entity s fair value disclosures and clarifies existing fair value disclosure requirements. The new disclo interim and annual reporting periods beginning after December 15, 2009 (effective January 1, 2010, for us), except f issuances and settlements in the rollforward of activity in Level 3 fair value measurements, which are effective for i December 15, 2010 (effective January 1, 2011, for us). Our policy is to recognize transfers between levels of the fai period. The required disclosures are provided in Note 15 ( Fair Value Measurements ).

**Accounting Guidance Pending Adoption at June 30, 2010**

***Credit quality disclosures.*** In July 2010, the FASB issued new accounting guidance which requires additional disclo receivables (i.e. loans) and the allowance for credit losses. Most of these additional disclosures will be required for i or after December 15, 2010 (effective December 31, 2010, for us). Specific items regarding activity that occurred be such as the allowance rollforward and modification disclosures, will be required for periods beginning after Decemb

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***Embedded credit derivatives.*** In March 2010, the FASB issued new accounting guidance that amends and clarifies h
embedded in beneficial interests in securitized financial assets. This accounting guidance eliminates the existing sco
features embedded in beneficial interests in securitized financial assets. This guidance will be effective the first day
2010 (effective July 1, 2010, for us) with early adoption permitted. We have no financial instruments that would be

**2. Earnings Per Common Share**

Our basic and diluted earnings per common share are calculated as follows:

| *dollars in millions, except per share amounts* | | **Three months ended Ju 2010** | |
|---|---|---|---|
| **EARNINGS** | | | |
| Income (loss) from continuing operations | **$** | **101** | $ |
| Less: Net income (loss) attributable to noncontrolling interests | | **4** | |
| Income (loss) from continuing operations attributable to Key | | **97** | |
| Less: Dividends on Series A Preferred Stock | | **6** | |
| Noncash deemed dividend common shares exchanged for Series A Preferred Stock | | | |
| Cash dividends on Series B Preferred Stock | | **31** | |
| Amortization of discount on Series B Preferred Stock | | **4** | |
| Income (loss) from continuing operations attributable to Key common shareholders | | **56** | |
| Income (loss) from discontinued operations, net of taxes [a] | | **(27)** | |
| Net income (loss) attributable to Key common shareholders | **$** | **29** | $ |
| **WEIGHTED-AVERAGE COMMON SHARES** | | | |
| Weighted-average common shares outstanding (000) | | **874,664** | 57 |
| Effect of dilutive convertible preferred stock, common stock options and other stock awards (000) | | | |
| Weighted-average common shares and potential common shares outstanding (000) | | **874,664** | 57 |
| **EARNINGS PER COMMON SHARE** | | | |
| Income (loss) from continuing operations attributable to Key common shareholders | **$** | **.06** | $ |
| Income (loss) from discontinued operations, net of taxes [a] | | **(.03)** | |
| Net income (loss) attributable to Key common shareholders | | **.03** | |
| Income (loss) from continuing operations attributable to Key common shareholders assuming dilution | **$** | **.06** | $ |
| Income (loss) from discontinued operations, net of taxes [a] | | **(.03)** | |
| Net income (loss) attributable to Key common shareholders assuming dilution | | **.03** | |

(a)

In September 2009, we decided to discontinue the education lending business conducted through Key Education Resources, the education payment and financing unit of KeyBank. In April 2009, we decided to wind down the operations of Austin, a subsidiary that specialized in managing hedge fund investments for institutional customers. As a result of these decisions, we have accounted for these businesses as discontinued operations. The loss from discontinued operations for the six-month period ended June 30, 2010, was primarily attributable to fair value adjustments related to the education lending securitization trusts. Included in the loss from discontinued operations for the six-month period ended June 30, 2009, is a charge for intangible assets impairment related to Austin.

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### 3. Line of Business Results

The specific lines of business that comprise each of the major business groups (operating segments) are described be re-aligned our reporting structure for our business groups. Prior to 2010, Consumer Finance consisted mainly of port portfolios and were included in our National Banking segment. For all periods presented, we are reflecting the result The automobile dealer floor-plan business, previously included in Consumer Finance, has been re-aligned with the C the Community Banking segment. Our tuition processing business was moved from Consumer Finance to Global Tr Capital and Corporate Banking Services. In addition, other previously identified exit portfolios included in the Natio Other Segments.

**Community Banking**

***Regional Banking*** provides individuals with branch-based deposit and investment products, personal finance servic home equity and various types of installment loans. This line of business also provides small businesses with deposi business advisory services.

Regional Banking also offers financial, estate and retirement planning, and asset management services to assist high portfolio management, insurance, charitable giving and related needs.

***Commercial Banking*** provides midsize businesses with products and services that include commercial lending, cash and employee benefit programs, succession planning, access to capital markets, derivatives and foreign exchange.

**National Banking**

***Real Estate Capital and Corporate Banking Services*** consists of two business units, Real Estate Capital and Corpor Real Estate Capital is a national business that provides construction and interim lending, permanent debt placements banking, and other commercial banking products and services to developers, brokers and owner-investors. This unit properties (i.e., generally properties in which at least 50% of the debt service is provided by rental income from non emphasizes providing clients with finance solutions through access to the capital markets.

Corporate Banking Services provides cash management, interest rate derivatives, and foreign exchange products and Banking and National Banking groups. Through its Public Sector and Financial Institutions businesses, Corporate B commercial banking products and services to government and not-for-profit entities and to community banks. A vari the processing of tuition payments for private schools, are provided through the Global Treasury Management unit.

***Equipment Finance*** meets the equipment leasing needs of companies worldwide and provides equipment manufactu options for their clients. Lease financing receivables and related revenues are assigned to other lines of business (pri Commercial Banking) if those businesses are principally responsible for maintaining the relationship with the client.

***Institutional and Capital Markets,*** through its KeyBanc Capital Markets unit, provides commercial lending, treasur derivatives, foreign exchange, equity and debt

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underwriting and trading, and syndicated finance products and services to large corporations and middle-market con
Institutional and Capital Markets, through its Victory Capital Management unit, also manages or offers advice regar
base, including corporations, labor unions, not-for-profit organizations, governments and individuals. These portfoli
common funds or the Victory family of mutual funds.

**Other Segments**

Other Segments consist of Corporate Treasury, our Principal Investing unit and various exit portfolios which were p
Banking segment. These exit portfolios were moved to Other Segments during the first quarter of 2010.

**Reconciling Items**

Total assets included under Reconciling Items primarily represent the unallocated portion of nonearning assets of
the funding of these assets are part of net interest income and are allocated to the business segments through noninte
intercompany eliminations and certain items that are not allocated to the business segments because they do not refle

The table on the following pages shows selected financial data for each major business group for the three- and six-
This table is accompanied by supplementary information for each of the lines of business that make up these groups
internal financial reporting system that we use to monitor and manage our financial performance. GAAP guides fina
guidance for management accounting the way we use our judgment and experience to make reporting decision
report may not be comparable with line of business results presented by other companies.

The selected financial data are based on internal accounting policies designed to compile results on a consistent basi
economics of the businesses. In accordance with our policies:

- Net interest income is determined by assigning a standard cost for funds used or a standard credit for funds provi prepayment and/or repricing characteristics. The net effect of this funds transfer pricing is charged to the lines of balances of each line.

- Indirect expenses, such as computer servicing costs and corporate overhead, are allocated based on assumptions actually uses the services.

- The consolidated provision for loan losses is allocated among the lines of business primarily based on their actua loan growth and changes in risk profile. The amount of the consolidated provision is based on the methodology t allowance for loan losses. This methodology is described in Note 1 ( Summary of Significant Accounting Polic Losses on page 82 in our 2009 Annual Report to Shareholders.

- Income taxes are allocated based on the statutory federal income tax rate of 35% (adjusted for tax-exempt interes insurance and tax credits associated with investments in low-income housing projects) and a blended state incom benefit) of 2.2%.

- Capital is assigned based on our assessment of economic risk factors (primarily credit, operating and market risk

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Developing and applying the methodologies that we use to allocate items among our lines of business is a dynamic p
revised periodically to reflect accounting enhancements, changes in the risk profile of a particular business or chang

| **Three months ended June 30,** *dollars in millions* | | **Community Banking** **2010** | | **200** |
|---|---|---|---|---|
| **SUMMARY OF OPERATIONS** | | | | |
| Net interest income (TE) | **$** | **408** | $ | 43 |
| Noninterest income | | **199** | | 19 |
| Total revenue (TE) [(a)] | | **607** | | 63 |
| Provision (credit) for loan losses | | **121** | | 19 |
| Depreciation and amortization expense | | **9** | | 1 |
| Other noninterest expense | | **446** | | 48 |
| Income (loss) from continuing operations before income taxes (TE) | | **31** | | (6 |
| Allocated income taxes and TE adjustments | | **(1)** | | (3 |
| Income (loss) from continuing operations | | **32** | | (3 |
| Income (loss) from discontinued operations, net of taxes | | | | |
| Net income (loss) | | **32** | | (3 |
| Less: Net income (loss) attributable to noncontrolling interests | | | | |
| Net income (loss) attributable to Key | **$** | **32** | $ | (3 |
| **AVERAGE BALANCES** [(b)] | | | | |
| Loans and leases | **$** | **27,218** | $ | 30,30 |
| Total assets [(a)] | | **30,292** | | 33,16 |
| Deposits | | **50,421** | | 52,78 |
| **OTHER FINANCIAL DATA** | | | | |
| Net loan charge-offs [(b)] | **$** | **148** | $ | 11 |
| Return on average allocated equity [(b)] | | **3.46 %** | | (3.3 |
| Return on average allocated equity | | **3.46** | | (3.3 |
| Average full-time equivalent employees [(e)] | | **8,246** | | 8,70 |

| **Six months ended June 30,** *dollars in millions* | | **Community Banking** **2010** | | **20** |
|---|---|---|---|---|
| **SUMMARY OF OPERATIONS** | | | | |
| Net interest income (TE) | **$** | **821** | $ | 8 |
| Noninterest income | | **386** | | 3 |
| Total revenue (TE) [(a)] | | **1,207** | | 1,2 |
| Provision (credit) for loan losses | | **263** | | 3 |
| Depreciation and amortization expense | | **18** | | |
| Other noninterest expense | | **904** | | 9 |

| | | |
|---|---|---|
| Income (loss) from continuing operations before income taxes (TE) | **22** | ( |
| Allocated income taxes and TE adjustments | **(16)** | ( |
| Income (loss) from continuing operations | **38** | ( |
| Income (loss) from discontinued operations, net of taxes | | |
| Net income (loss) | **38** | ( |
| Less: Net income (loss) attributable to noncontrolling interests | | |
| Net income (loss) attributable to Key | **$ 38** | $ ( |
| **AVERAGE BALANCES** (b) | | |
| Loans and leases | **$ 27,492** | $ 30,7 |
| Total assets (a) | **30,581** | 33,6 |
| Deposits | **50,937** | 52,2 |
| **OTHER FINANCIAL DATA** | | |
| Net loan charge-offs (b) | **$ 264** | $ 2 |
| Return on average allocated equity (b) | **2.06 %** | (1. |
| Return on average allocated equity | **2.06** | (1. |
| Average full-time equivalent employees (e) | **8,217** | 8,8 |

(a) Substantially all revenue generated by our major business groups is derived from clients that reside in the United States. Substantially all long-lived assets, including premises and equipment, capitalized software and goodwill held by our major business groups, are located in the United States.

(b) From continuing operations.

(c) Other Segments results for the second quarter of 2009 include net gains of $125 million ($78 million after tax) in connection with the repositioning of the securities portfolio and a $95 million ($59 million after tax) gain related to the exchange of Key common shares for capital securities.

(d) Reconciling Items for the second quarter of 2009 include a $32 million ($20 million after tax) gain from the sale of Key s claim associated with the Lehman Brothers bankruptcy.

(e) The number of average full-time equivalent employees has not been adjusted for discontinued operations.

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| Other Segments | | Total Segments | | Reconciling Items | | |
|---|---|---|---|---|---|---|
| 2010 | 2009 | 2010 | 2009 | 2010 | 2009 | 2010 |
| **$ 9** | $ (91) | **$ 616** | $ 580 | **$ 7** | $ (5) | **$ 623** |
| **77** | 278 [c] | **486** | 682 | **6** | 24 [d] | **492** |
| **86** | 187 | **1,102** | 1,262 | **13** | 19 | **1,115** |
| **7** | 131 | **227** | 824 | **1** | (1) | **228** |
| **10** | 18 | **44** | 60 | **41** | 40 | **85** |
| **33** | 34 | **713** | 780 | **(29)** | (25) | **684** |
| **36** | 4 | **118** | (402) | | 5 | **118** |
| **3** | (8) | **20** | (172) | **(3)** | 2 | **17** |
| **33** | 12 | **98** | (230) | **3** | 3 | **101** |
| | | | | **(27)** | 4 | **(27)** |
| **33** | 12 | **98** | (230) | **(24)** | 7 | **74** |
| **4** | 4 | **4** | 3 | | | **4** |
| **$ 29** | $ 8 | **$ 94** | $ (233) | **$ (24)** | $ 7 | **$ 70** |
| **$ 6,738** | $ 9,765 | **$ 54,904** | $ 68,656 | **$ 49** | $ 54 | **$ 54,953** |
| **30,583** | 27,920 | **85,656** | 95,880 | **2,188** | 608 | **87,844** |
| **1,574** | 1,974 | **64,469** | 67,779 | **(60)** | (416) | **64,409** |
| **$ 115** | $ 136 | **$ 436** | $ 502 | **$ (1)** | | **$ 435** |
| **N/M** | N/M | **4.60 %** | (10.50) % | **N/M** | N/M | **3.65%** |
| **N/M** | N/M | **4.60** | (10.50) | **N/M** | N/M | **2.64** |
| **40** | 87 | **10,613** | 11,341 | **5,052** | 5,596 | **15,665** |

| Other Segments | | Total Segments | | Reconciling Items | | F |
|---|---|---|---|---|---|---|
| 2010 | 2009 | 2010 | 2009 | 2010 | 2009 | 2010 |
| **$ 25** | $ (132) | **$ 1,242** | $ 1,183 | **$ 13** | $ (13) | **$ 1,255** |
| **157** | 282 [c] | **932** | 1,073 | **10** | 111 [d] | **942** |
| **182** | 150 | **2,174** | 2,256 | **23** | 98 | **2,197** |
| **128** | 324 | **651** | 1,669 | **(10)** | 1 | **641** |
| **21** | 36 | **90** | 121 | **83** | 80 | **173** |
| **63** | 73 | **1,446** | 1,671 | **(65)** | (90) | **1,381** |

| | | | | | | |
|---|---|---|---|---|---|---|
| **(30)** | (283) | **(13)** | (1,205) | **15** | 107 | **2** |
| **(31)** | (126) | **(52)** | (421) | **(6)** | 19 | **(58)** |
| **1** | (157) | **39** | (784) | **21** | 88 | **60** |
| | | | | **(25)** | (25) | **(25)** |
| **1** | (157) | **39** | (784) | **(4)** | 63 | **35** |
| **20** | (4) | **20** | (7) | | | **20** |
| **$ (19)** | $ (153) | **$ 19** | $ (777) | **$ (4)** | $ 63 | **$ 15** |
| **$ 7,047** | $ 10,180 | **$ 56,229** | $ 70,108 | **$ 53** | $ 45 | **$ 56,282** |
| **29,962** | 27,651 | **86,064** | 97,314 | **2,219** | 584 | **88,283** |
| **1,609** | 1,884 | **64,991** | 66,603 | **(109)** | (293) | **64,882** |
| **$ 269** | $ 267 | **$ 957** | $ 962 | | | **$ 957** |
| **N/M** | N/M | **.46%** | (17.62) % | **N/M** | N/M | **.75%** |
| **N/M** | N/M | **.46** | (17.62) | **N/M** | N/M | **.28** |
| **41** | 97 | **10,606** | 11,503 | **5,112** | 5,698 | **15,718** |

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Supplementary information (Community Banking lines of business)

| **Three months ended June 30,** *dollars in millions* | **Regional Banking** **2010** | **200** |
|---|---|---|
| Total revenue (TE) | **$ 494** | $ 52 |
| Provision for loan losses | **57** | 16 |
| Noninterest expense | **409** | 43 |
| Net income (loss) attributable to Key | **30** | (3 |
| Average loans and leases | **18,405** | 19,74 |
| Average loans held for sale | **69** | 16 |
| Average deposits | **45,234** | 48,71 |
| Net loan charge-offs | **82** | 7 |
| Net loan charge-offs to average loans | **1.79 %** | 1.4 |
| Nonperforming assets at period end | **$ 339** | $ 24 |
| Return on average allocated equity | **4.90 %** | (6.6 |
| Average full-time equivalent employees | **7,891** | 8,33 |

| **Six months ended June 30,** *dollars in millions* | **Regional Banking** **2010** | **200** |
|---|---|---|
| Total revenue (TE) | **$ 985** | $ 1,03 |
| Provision for loan losses | **172** | 23 |
| Noninterest expense | **830** | 84 |
| Net income (loss) attributable to Key | **14** | (1 |
| Average loans and leases | **18,578** | 19,87 |
| Average loans held for sale | **75** | 14 |
| Average deposits | **45,713** | 48,25 |
| Net loan charge-offs | **179** | 12 |
| Net loan charge-offs to average loans | **1.94 %** | 1.2 |
| Nonperforming assets at period end | **$ 339** | $ 24 |
| Return on average allocated equity | **1.15 %** | (.8 |
| Average full-time equivalent employees | **7,864** | 8,45 |

Supplementary information (National Banking lines of business)

| **Three months ended June 30,** *dollars in millions* | **Real Estate Capital and Corporate Banking Services** **2010** | **2009** | **Equipment Financ** **2010** | **2** |
|---|---|---|---|---|
| Total revenue (TE) | **$ 176** | $ 191 | **$ 61** | $ |
| Provision for loan losses | **77** | 414 | **10** | |
| Noninterest expense | **106** | 113 | **49** | |
| Net income (loss) attributable to Key | **(4)** | (209) | **1** | |
| Average loans and leases | **11,465** | 15,145 | **4,478** | 5, |
| Average loans held for sale | **194** | 182 | **16** | |
| Average deposits | **9,811** | 10,678 | **5** | |
| Net loan charge-offs | **142** | 212 | **18** | |

| | | | | |
|---|---|---|---|---|
| Net loan charge-offs to average loans | **4.97 %** | 5.61 % | **1.61 %** | 2 |
| Nonperforming assets at period end | **$ 867** | $ 1,023 | **$ 106** | $ |
| Return on average allocated equity | **(.78) %** | (34.43) % | **1.14 %** | (25 |
| Average full-time equivalent employees | **1,052** | 1,125 | **549** | |

| **Six months ended June 30,** | **Real Estate Capital and Corporate Banking Services** | | **Equipment Financ** | |
|---|---|---|---|---|
| *dollars in millions* | **2010** | **2009** | **2010** | **20** |
| Total revenue (TE) | **$ 320** | $ 374 | **$ 122** | $ 1 |
| Provision for loan losses | **222** | 852 | **14** | |
| Noninterest expense | **221** | 304 | **96** | 1 |
| Net income (loss) attributable to Key | **(76)** | (530) | **7** | ( |
| Average loans and leases | **11,900** | 15,432 | **4,525** | 5,0 |
| Average loans held for sale | **154** | 194 | **9** | |
| Average deposits | **9,823** | 10,433 | **5** | |
| Net loan charge-offs | **349** | 385 | **36** | |
| Net loan charge-offs to average loans | **5.91 %** | 5.03 % | **1.60 %** | 2 |
| Nonperforming assets at period end | **$ 867** | $ 1,023 | **$ 106** | $ 1 |
| Return on average allocated equity | **(7.42) %** | (45.00) % | **3.92 %** | (20 |
| Average full-time equivalent employees | **1,065** | 1,146 | **556** | 6 |

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## 4. Securities

***Securities available for sale.*** These are securities that we intend to hold for an indefinite period of time but that may
rates, prepayment risk, liquidity needs or other factors. Securities available for sale are reported at fair value. Unreal
deemed temporary are recorded in equity as a component of AOCI on the balance sheet. Unrealized losses on equity
other-than-temporary, and realized gains and losses resulting from sales of securities using the specific identificat
(losses) on the income statement. Unrealized losses on debt securities deemed to be other-than-temporary are in
income statement or AOCI in accordance with the applicable accounting guidance related to the recognition of OTT

Other securities held in the available-for-sale portfolio are primarily marketable equity securities that are traded o
NASDAQ.

***Held-to-maturity securities.*** These are debt securities that we have the intent and ability to hold until maturity. Debt
amortization of premiums and accretion of discounts using the interest method. This method produces a constant rat

Other securities held in the held-to-maturity portfolio consist of foreign bonds, capital securities and preferred eq

The amortized cost, unrealized gains and losses, and approximate fair value of our securities available for sale and h
following tables. Gross unrealized gains and losses represent the difference between the amortized cost and the fair v
the dates indicated. Accordingly, the amount of these gains and losses may change in the future as market conditions

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| *in millions* | **Amortized Cost** | **G Unreal G** |
|---|---|---|
| **SECURITIES AVAILABLE FOR SALE** | | |
| U.S. Treasury, agencies and corporations | **$ 8** | |
| States and political subdivisions | **75** | **$** |
| Collateralized mortgage obligations | **17,817** | |
| Other mortgage-backed securities | **1,187** | |
| Other securities | **106** | |
| Total securities available for sale | **$ 19,193** | **$** |
| **HELD-TO-MATURITY SECURITIES** | | |
| States and political subdivisions | **$ 3** | |
| Other securities | **16** | |
| Total held-to-maturity securities | **$ 19** | |

| *in millions* | **Amortized Cost** | **I G Unreal G** |
|---|---|---|
| **SECURITIES AVAILABLE FOR SALE** | | |
| U.S. Treasury, agencies and corporations | $ 8 | |
| States and political subdivisions | 81 | $ |
| Collateralized mortgage obligations | 14,894 | |
| Other mortgage-backed securities | 1,351 | |
| Other securities | 100 | |
| Total securities available for sale | $ 16,434 | $ |
| **HELD-TO-MATURITY SECURITIES** | | |
| States and political subdivisions | $ 3 | |
| Other securities | 21 | |
| Total held-to-maturity securities | $ 24 | |

| *in millions* | Amortized Cost | G Unreal G |
|---|---|---|
| **SECURITIES AVAILABLE FOR SALE** | | |
| U.S. Treasury, agencies and corporations | $ 1,710 | |
| States and political subdivisions | 85 | $ |
| Collateralized mortgage obligations | 8,462 | |
| Other mortgage-backed securities | 1,525 | |
| Other securities | 66 | |
| Total securities available for sale | $ 11,848 | $ |
| **HELD-TO-MATURITY SECURITIES** | | |
| States and political subdivisions | $ 4 | |
| Other securities | 21 | |
| Total held-to-maturity securities | $ 25 | |

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The following table summarizes our securities available for sale that were in an unrealized loss position as of June 3
2009.

| | Duration of Unrealized Loss Position | | | |
|---|---|---|---|---|
| | Less than 12 Months | | 12 Months or Longe | |
| *in millions* | Fair Value | Gross Unrealized Losses | Fair Value | Unrea L |
| **JUNE 30, 2010** | | | | |
| Securities available for sale: | | | | |
| Other securities | **$ 18** | **$ 2** | **$ 3** | **$** |
| Total temporarily impaired securities | **$ 18** | **$ 2** | **$ 3** | **$** |
| **DECEMBER 31, 2009** | | | | |
| Securities available for sale: | | | | |
| Collateralized mortgage obligations | $ 4,988 | $ 75 | | |
| Other securities | 2 | | $ 4 | $ |
| Total temporarily impaired securities | $ 4,990 | $ 75 | $ 4 | $ |
| **JUNE 30, 2009** | | | | |
| Securities available for sale: | | | | |
| Collateralized mortgage obligations | $ 1,660 | $ 38 | | |
| Other securities | 10 | 1 | $ 2 | $ |
| Total temporarily impaired securities | $ 1,670 | $ 39 | $ 2 | $ |

The unrealized losses within each investment category are considered temporary since we expect to collect all contra
Accordingly, these investments have been reduced to their fair value through OCI, not earnings.
We regularly assess our securities portfolio for OTTI. The assessments are based on the nature of the securities, und
the issuer, the extent and duration of the loss, our intent related to the individual securities, and the likelihood that w
expected recovery.
Debt securities identified to have OTTI are written down to their current fair value. For those debt securities that we
required to sell, prior to the expected recovery of the amortized cost, the entire impairment (i.e., the difference betwe
recognized in earnings. For those debt securities that we do not intend to sell, or more-likely-than-not will not be req
credit portion of OTTI is recognized in earnings, while the remaining OTTI is recognized in equity as a component o
the following table, there was $4 million in impairment losses recognized in earnings for the three months ended Jun

| **Three months ended June 30, 2010** | |
|---|---|
| *in millions* | |
| **Balance at March 31, 2010** | |
| Impairment recognized in earnings | $ 4 |

| | |
|---|---|
| **Balance at June 30, 2010** | $ 4 |

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As a result of adopting new consolidation guidance on January 1, 2010, we have consolidated our education loan sec
interests in these trusts. Prior to our consolidation of these trusts, we accounted for the residual interests associated w
which we regularly assessed for impairment. These residual interests will no longer be assessed for impairment. The
these trusts are included in discontinued assets and discontinued liabilities on the balance sheet as a result of o
For more information about this discontinued operation, see Note 16 ( Discontinued Operations ).
Realized gains and losses related to securities available for sale were as follows:

| **Six months ended June 30, 2010**<br>*in millions* | |
|---|---|
| Realized gains | $ 5 |
| Realized losses | 4 |
| Net securities gains (losses) | $ 1 |

At June 30, 2010, securities available for sale and held-to-maturity securities totaling $12.1 billion were pledged to s
agreements, public and trust deposits, to facilitate access to secured funding, and for other purposes required or perm
The following table shows securities by remaining maturity. Collateralized mortgage obligations and other mortgage
included in the securities available-for-sale portfolio are presented based on their expected average lives. The rem
held-to-maturity portfolio, are presented based on their remaining contractual maturity. Actual maturities may differ
borrowers have the right to prepay obligations with or without prepayment penalties.

| | Securities Available for Sal | |
|---|---|---|
| **June 30, 2010**<br>*in millions* | **Amortized Cost** | **V** |
| Due in one year or less | $ 679 | $ |
| Due after one through five years | 18,371 | 1 |
| Due after five through ten years | 126 | |
| Due after ten years | 17 | |
| Total | $ 19,193 | $ 1 |

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## 5. Loans and Loans Held for Sale

Our loans by category are summarized as follows:

| *in millions* | | June 30, 2010 |
|---|---|---|
| Commercial, financial and agricultural | $ | **17,113** |
| Commercial real estate: | | |
| Commercial mortgage | | **9,971** |
| Construction | | **3,430** |
| Total commercial real estate loans | | **13,401** |
| Commercial lease financing | | **6,620** |
| Total commercial loans | | **37,134** |
| Real estate residential mortgage | | **1,846** |
| Home equity: | | |
| Community Banking | | **9,775** |
| Other | | **753** |
| Total home equity loans | | **10,528** |
| Consumer other Community Banking | | **1,147** |
| Consumer other: | | |
| Marine | | **2,491** |
| Other | | **188** |
| Total consumer other | | **2,679** |
| Total consumer loans | | **16,200** |
| Total loans [(a)] | $ | **53,334** |

(a) Excludes loans in the amount of $6.6 billion, $3.5 billion and $3.6 billion at June 30, 2010, December 31, 2009 and June 30, 2009, respectively, related to the discontinued operations of the education lending business.

We use interest rate swaps, which modify the repricing characteristics of certain loans, to manage interest rate risk. F
Note 20 ( Derivatives and Hedging Activities ), which begins on page 122 of our 2009 Annual Report to Sharehold
Our loans held for sale by category are summarized as follows:

| *in millions* | | **June 30, 2010** |
|---|---|---|
| Commercial, financial and agricultural | **$** | **255** |
| Real estate commercial mortgage | | **235** |
| Real estate construction | | **112** |
| Commercial lease financing | | **16** |
| Real estate residential mortgage | | **81** |
| Automobile | | |
| Total loans held for sale [(a)] | **$** | **699** [(b)] |

(a) Excludes loans in the amount of $92 million, $434 million and $148 million at June 30, 2010, December 31, 2009, and June 30, 2009, respectively, related to the discontinued operations of the education lending business.

(b) The beginning balance at December 31, 2009 of $443 million increased by new originations in the amount of $1.321 billion and net transfers from held to maturity in the amount of $174 million, and decreased by loan sales of $1.200 billion, transfers to

OREO/valuation adjustments of $17 million and loan payments of $22 million, for an ending balance of $699 million at June 30, 2010.

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Changes in the allowance for loan losses are summarized as follows:

| *in millions* | Three months ended Ju 2010 | |
|---|---|---|
| Balance at beginning of period | **$ 2,425** | $ |
| Charge-offs | **(492)** | |
| Recoveries | **57** | |
| Net loans charged off | **(435)** | |
| Provision for loan losses from continuing operations | **228** | |
| Foreign currency translation adjustment | **1** | |
| Balance at end of period | **$ 2,219** | $ |

Changes in the liability for credit losses on lending-related commitments are summarized as follows:

| *in millions* | Three months ended Ju 2010 | |
|---|---|---|
| Balance at beginning of period | **$ 119** | $ |
| Provision (credit) for losses on lending-related commitments | **(10)** | |
| Balance at end of period [(a)] | **$ 109** | $ |

(a) Included in accrued expense and other liabilities on the balance sheet.

## 6. Mortgage Servicing Assets

We originate and periodically sell commercial mortgage loans but continue to service those loans for the buyers. We commercial mortgage loans for other lenders. A servicing asset is recorded if we purchase or retain the right to servi exceed the going market rate. Changes in the carrying amount of mortgage servicing assets are summarized as follov

| *in millions* | Six months ended June 30, 2010 | 2009 |
|---|---|---|
| Balance at beginning of period | **$ 221** | $ 242 |
| Servicing retained from loan sales | **3** | 4 |
| Purchases | **7** | 15 |
| Amortization | **(22)** | (27) |
| Balance at end of period | **$ 209** | $ 234 |

| | | |
|---|---|---|
| Fair value at end of period | **$ 307** | $ 403 |

The fair value of mortgage servicing assets is determined by calculating the present value of future cash flows assoc
calculation uses a number of assumptions that are based on current market conditions. Primary economic assumptior
mortgage servicing assets at June 30, 2010 and 2009, are:

- w prepayment speed generally at an annual rate of 0.00% to 25.00%;
- w expected credit losses at a static rate of 2.00% to 3.00%; and
- w residual cash flows discount rate of 7.00% to 15.00%.

Changes in these assumptions could cause the fair value of mortgage servicing assets to change in the future. The vo
losses are critical to the valuation of servicing assets. At June 30, 2010, a 1.00% increase in the assumed default rate
$9 million decrease in the fair value of our mortgage servicing assets.

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Contractual fee income from servicing commercial mortgage loans totaled $37 million and $34 million for the six-m
respectively. We have elected to remeasure servicing assets using the amortization method. The amortization of serv
and over the period of, the estimated net servicing income. The amortization of servicing assets for each period, as sl
reduction to fee income. Both the contractual fee income and the amortization are recorded in other income on th
Additional information pertaining to the accounting for mortgage and other servicing assets is included in Note 1 (
under the heading Servicing Assets on page 82 of our 2009 Annual Report to Shareholders and Note 16 ( Discor
lending.

## 7. Variable Interest Entities

A VIE is a partnership, limited liability company, trust or other legal entity that meets any one of the following crite

- The entity does not have sufficient equity to conduct its activities without additional subordinated financial supp
- The entity s investors lack the power to direct the activities that most significantly impact the entity s economic
- The entity s equity at risk holders do not have the obligation to absorb losses and the right to receive residual re
- The voting rights of some investors are not proportional to their economic interest in the entity, and substantially conducted on behalf of investors with disproportionately few voting rights.

Our VIEs, including those consolidated and those in which we hold a significant interest, are summarized below. W
subordinated interest that exposes us to a significant portion, but not the majority, of the VIE s expected losses or re
power to direct the activities that most significantly impact the entity s economic performance.

| | Consolidated VIEs | | |
|---|---|---|---|
| *in millions* | **Total Assets** | **Total Liabilities** | **Total Assets** |
| June 30, 2010 | | | |
| LIHTC funds | $ 134 | N/A | $ 175 |
| Education loan securitization trusts | 3,285 | $ 3,135 | N/A |
| LIHTC investments | N/A | N/A | 963 |

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Our involvement with VIEs is described below.

Consolidated VIEs

***LIHTC guaranteed funds.*** KAHC formed limited partnerships, known as funds, which invested in LIHTC operating
offered in syndication to qualified investors who paid a fee to KAHC for a guaranteed return. We also earned syndic
asset management fees. The funds assets primarily are investments in LIHTC operating partnerships, which totaled
investments are recorded in accrued income and other assets on the balance sheet and serve as collateral for the fu
We have not formed new funds or added LIHTC partnerships since October 2003. However, we continue to act as a
for existing funds under a guarantee obligation. As a result of this guarantee obligation, we have determined that we
We recorded additional expenses of approximately $2 million related to this guarantee obligation during the first six
return guarantee agreements with LIHTC investors is presented in Note 13 ( Commitments, Contingent Liabilities a

In accordance with the applicable accounting guidance for distinguishing liabilities from equity, third-party interests
are considered mandatorily redeemable instruments and are recorded in accrued expense and other liabilities on th
indefinitely deferred the measurement and recognition provisions of this accounting guidance for mandatorily redeem
finite-lived subsidiaries, such as our LIHTC guaranteed funds. We adjust our financial statements each period for th
profits and losses. At June 30, 2010, we estimated the settlement value of these third-party interests to be between $
value, including reserves, totaled $143 million. The partnership agreement for each of our guaranteed funds requires

***Education loan securitization trusts.*** In September 2009, we decided to exit the government-guaranteed education l
accounted for this business as a discontinued operation. As part of our education lending business model, we would
as the transferor, retained a portion of the risk in the form of a residual interest and also retained the right to service t
fees.

As a result of adopting the new consolidation accounting guidance issued by the FASB in June 2009, we have conso
securitization trusts as of January 1, 2010. We were required to consolidate these trusts because we hold the residual
the power to direct the activities that most significantly impact the economic performance of these trusts. We electe
assets held by these trusts can only be used to settle the obligations or securities issued by the trusts. We cannot sell
consolidated trusts. The security holders or beneficial interest holders do not have recourse to us. We do not have an
other than the securities issued by the trusts. We have not securitized any education loans since 2006. Additional inf
Note 16 ( Discontinued Operations ) under the heading Education lending.

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Unconsolidated VIEs

***LIHTC nonguaranteed funds.*** Although we hold significant interests in certain nonguaranteed funds that we formed
not the primary beneficiary of those funds because we do not absorb the majority of the funds expected losses and
most significantly impact the economic performance of these entities. At June 30, 2010, assets of these unconsolidat
Our maximum exposure to loss in connection with these funds is minimal, and we do not have any liability recorded
nonguaranteed funds since October 2003.

***LIHTC investments***. Through the Community Banking business group, we have made investments directly in LIHT
parties. As a limited partner in these operating partnerships, we are allocated tax credits and deductions associated w
determined that we are not the primary beneficiary of these investments because the general partners have the power
most significantly impact their economic performance and have the obligation to absorb expected losses and the righ
June 30, 2010, assets of these unconsolidated LIHTC operating partnerships totaled approximately $963 million. At
in connection with these partnerships is the unamortized investment balance of $373 million plus $78 million of tax
do not have any liability recorded related to these investments because we believe the likelihood of any loss in conne
During the first six months of 2010, we did not obtain significant direct investments (either individually or in the agg
We have additional investments in unconsolidated LIHTC operating partnerships that are held by the consolidated L
operating partnerships were approximately $1.3 billion at June 30, 2010. The tax credits and deductions associated w
investors based on their ownership percentages. We have determined that we are not the primary beneficiary of these
have the power to direct the activities that most significantly impact their economic performance and the obligation t
residual returns from the entity. Information regarding our exposure to loss in connection with these guaranteed fund
Return guarantee agreement with LIHTC investors.

***Commercial and residential real estate investments and principal investments.*** Our Principal Investing unit and the
Services line of business make equity and mezzanine investments, some of which are in VIEs. These investments are
subject to the provisions of the AICPA Audit and Accounting Guide, Audits of Investment Companies. We are no
disclosure provisions in the applicable accounting guidance for consolidations to these investments, which remain un
deferred the effective date of this guidance for such nonregistered investment companies.

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**8. Nonperforming Assets and Past Due Loans from Continuing Operat**

Impaired loans totaled $1.4 billion at June 30, 2010, compared to $1.9 billion at December 31, 2009, and $1.9 billion average balance of $1.6 billion for the second quarter of 2010 and $1.7 billion for the second quarter of 2009. At Jun included in impaired loans) totaled $213 million while at December 31, 2009, restructured loans totaled $364 million were added during the first six months of 2010, the decrease in restructured loans was primarily attributable to the tr restructurings to performing status, and $83 million in payments and charge-offs. Restructured loans were nominal a

Our nonperforming assets and past due loans were as follows:

| *in millions* | June 3 201 |
|---|---|
| Impaired loans | $ 1,43 |
| Other nonperforming loans | 26 |
| Total nonperforming loans | 1,70 |
| Nonperforming loans held for sale | 22 |
| Other real estate owned ( OREO ) | 20 |
| Allowance for OREO losses | (6 |
| OREO, net of allowance | 13 |
| Other nonperforming assets | 2 |
| Total nonperforming assets | $ 2,08 |
| Impaired loans with a specifically allocated allowance | $ 1,09 |
| Specifically allocated allowance for impaired loans | 15 |
| Restructured loans included in nonaccrual loans [(a)] | $ 16 |
| Restructured loans with a specifically allocated allowance [(b)] | 6 |
| Specifically allocated allowance for restructured loans [(c)] | 1 |
| Accruing loans past due 90 days or more | $ 24 |
| Accruing loans past due 30 through 89 days | 61 |

(a) Restructured loans (i.e. troubled debt restructurings) are those for which we, for reasons related to a borrower s financial difficulties, have granted a concession to the borrower that we would not otherwise have considered. These concessions are made to improve the collectability of the loan and generally take the form of a reduction of the interest rate, extension of the maturity date or reduction in the principal balance.

(b) Included in impaired loans with a specifically allocated allowance.

(c) Included in specifically allocated allowance for impaired loans.

At June 30, 2010, we did not have any significant commitments to lend additional funds to borrowers with loans on

We evaluate the collectability of our loans as described in Note 1 ( Summary of Significant Accounting Policies ) t

page 82 of our 2009 Annual Report to Shareholders.

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### 9. Capital Securities Issued by Unconsolidated Subsidiaries

We own the outstanding common stock of business trusts formed by us that issued corporation-obligated mandatoril
trusts used the proceeds from the issuance of their capital securities and common stock to buy debentures issued by 
assets; the interest payments from the debentures finance the distributions paid on the capital securities.

We unconditionally guarantee the following payments or distributions on behalf of the trusts:

- w required distributions on the capital securities;

- w the redemption price when a capital security is redeemed; and

- w the amounts due if a trust is liquidated or terminated.

Our capital securities have historically provided an attractive source of funds: they currently constitute Tier 1 capital
the same federal tax advantages as debt.

In 2005, the Federal Reserve adopted a rule that allows bank holding companies to continue to treat capital securitie
quantitative limits that were to take effect March 31, 2009. On March 17, 2009, in light of continued stress in the fin
the effective date of these new limits until March 31, 2011. We believe this new rule will not have any material effe

The enactment of the Dodd-Frank Act changes the regulatory capital standards that apply to bank holding companie
securities and cumulative preferred securities (excluding TARP CPP preferred stock issued to the United States or it
October 4, 2010) as Tier 1 eligible capital. This three year phase-out period, which commences January 1, 2013, and
securities being treated only as Tier 2 capital. These changes in effect apply the same leverage and risk-based capita
institutions to bank holding companies, savings and loan companies, and non-bank financial companies identified as
has 180 days from the enactment of the Dodd-Frank Act to issue its regulations in this area. We anticipate that the F
should provide additional clarity to the regulatory capital guidelines applicable to bank holding companies such as K

As of June 30, 2010, the capital securities issued by the KeyCorp and Union State Bank capital trusts represent $1.8

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The capital securities, common stock and related debentures are summarized as follows:

| *dollars in millions* | | Capital Securities, Net of Discount [a] | | Common Stock | | Principal Amount of Debentures, Net of Discount |
|---|---|---|---|---|---|---|
| June 30, 2010 | | | | | | |
| KeyCorp Capital I | **$** | **156** | **$** | **6** | **$** | **158** |
| KeyCorp Capital II | | **81** | | **4** | | **106** |
| KeyCorp Capital III | | **102** | | **4** | | **136** |
| KeyCorp Capital V | | **115** | | **4** | | **128** |
| KeyCorp Capital VI | | **55** | | **2** | | **60** |
| KeyCorp Capital VII | | **164** | | **5** | | **177** |
| KeyCorp Capital VIII | | **171** | | | | **210** |
| KeyCorp Capital IX | | **331** | | | | **359** |
| KeyCorp Capital X | | **570** | | | | **616** |
| Union State Capital I | | **20** | | **1** | | **21** |
| Union State Statutory II | | **20** | | | | **20** |
| Union State Statutory IV | | **10** | | | | **10** |
| Total<br>Total | **$** | **1,795** | **$** | **26** | **$** | **2,001** |
| December 31, 2009<br>Total | $ | 1,872 | $ | 26 | $ | 1,906 |
| June 30, 2009<br>Total | $ | 2,449 | $ | 29 | $ | 2,485 |

(a) The capital securities must be redeemed when the related debentures mature, or earlier if provided in the governing indenture. Each issue of capital securities carries an interest rate identical to that of the related debenture. Certain capital securities include basis adjustments related to fair value hedges totaling $4 million at June 30, 2010, $81 million at December 31, 2009, and $158 million at June 30, 2009. See Note 14 ( Derivatives and Hedging Activities ) for an explanation of fair value hedges.

(b) We have the right to redeem our debentures: (i) in whole or in part, on or after July 1, 2008 (for debentures owned by KeyCorp Capital I); March 18, 1999 (for debentures owned by KeyCorp Capital II); July 16, 1999 (for debentures owned by KeyCorp Capital III); July 21, 2008 (for debentures owned by KeyCorp Capital V); December 15, 2008 (for debentures owned by KeyCorp Capital VI); June 15, 2010 (for debentures owned by KeyCorp Capital VII); June 15, 2011 (for debentures owned by KeyCorp Capital VIII); December 15, 2011 (for debentures owned by KeyCorp Capital IX); March 15, 2013 (for debentures owned by KeyCorp Capital X); February 1, 2007 (for debentures owned by Union State Capital I); July 31, 2006 (for debentures owned by Union State Statutory II); and April 7, 2009 (for debentures owned by Union State Statutory IV); and (ii) in whole at any time within 90 days after and during the continuation of a tax event, a capital treatment event , with respect to KeyCorp Capital V, VI, VII, VIII, IX and X only an investment company event with respect to KeyCorp Capital X only a rating agency event (as each is defined in the applicable indenture). If the debentures purchased by KeyCorp Capital I, KeyCorp Capital V, KeyCorp Capital

VI, KeyCorp Capital VII, KeyCorp Capital VIII, KeyCorp Capital IX, Union State Capital I or Union State Statutory IV are redeemed before they mature, the redemption price will be the principal amount, plus any accrued but unpaid interest. If the debentures purchased by KeyCorp Capital II or KeyCorp Capital III are redeemed before they mature, the redemption price will be the greater of: (a) the principal amount, plus any accrued but unpaid interest or (b) the sum of the present values of principal and interest payments discounted at the Treasury Rate (as defined in the applicable indenture), plus 20 basis points (25 basis points or 50 basis points in the case of redemption upon either a tax event or a capital treatment event for KeyCorp Capital III), plus any accrued but unpaid interest. If the debentures purchased by Union State Statutory II are redeemed before July 31, 2011, the redemption price will be 101.50% of the principal amount, plus any accrued but unpaid interest. When debentures are; redeemed in response to tax or capital treatment events, the redemption price for KeyCorp Capital II and KeyCorp Capital III generally is slightly more favorable to us. The principal amount of debentures includes adjustments related to hedging with financial instruments totaling $184 million at June 30, 2010, $89 million at December 31, 2009, and $165 million at June 30, 2009.

(c) The interest rates for KeyCorp Capital II, KeyCorp Capital III, KeyCorp Capital V, KeyCorp Capital VI, KeyCorp Capital VII, KeyCorp Capital VIII, KeyCorp

Capital IX, KeyCorp Capital X and Union State Capital I are fixed. KeyCorp Capital I has a floating interest rate equal to three-month LIBOR plus 74 basis points that reprices quarterly. Union State Statutory II has a floating interest rate equal to three-month LIBOR plus 358 basis points that reprices quarterly. Union State Statutory IV has a floating interest rate equal to three-month LIBOR plus 280 basis points that reprices quarterly. The total interest rates are weighted-average rates.

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## 10. Shareholders Equity

**Cumulative effect adjustment (after-tax)**

Effective January 1, 2010, we adopted new consolidation accounting guidance. As a result of adopting this new guid securitization trusts (classified as discontinued assets and liabilities), thereby adding $2.8 billion in assets and liabili cumulative effect adjustment (after-tax) of $45 million to beginning retained earnings on January 1, 2010. Additiona consolidation guidance and the consolidation of these education loan securitization trusts is provided in Note 1 ( Ba Operations ).

We did not undertake any new capital generating activities during the first six months of 2010. Note 15 ( Sharehold Report to Shareholders provides information regarding our capital generating activities in 2009.

## 11. Employee Benefits

**Pension Plans**

Effective December 31, 2009, we amended our pension plans to freeze all benefit accruals. We will continue to cred until they receive their plan benefits. The plans were closed to new employees as of December 31, 2009.

The components of net pension cost for all funded and unfunded plans are as follows:

| *in millions* | Three months ended J 2010 | |
|---|---|---|
| Service cost of benefits earned | | $ |
| Interest cost on PBO | **$ 15** | |
| Expected return on plan assets | **(18)** | |
| Amortization of losses | **9** | |
| Net pension cost | **$ 6** | $ |

**Other Postretirement Benefit Plans**

We sponsor a contributory postretirement healthcare plan that covers substantially all active and retired employees h criteria. Retirees contributions are adjusted annually to reflect certain cost-sharing provisions and benefit limitation covering certain grandfathered employees; the plan is noncontributory. Separate VEBA trusts are used to fund the h

The components of net postretirement benefit cost for all funded and unfunded plans are as follows:

| *in millions* | Three months ended J 2010 | |
|---|---|---|
| Interest cost on APBO | **$ 1** | $ |
| Expected return on plan assets | **(1)** | |
| Amortization of unrecognized prior service benefit | **(1)** | |
| Net postretirement (benefit) cost | **$ (1)** | |

The Patient Protection and Affordable Care Act and Education Reconciliation Act of 2010, which were signed respectively, changed the tax treatment of

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federal subsidies paid to sponsors of retiree health benefit plans that provide a benefit that is at least actuarially equ
As a result of these laws, these subsidy payments become taxable in tax years beginning after December 31, 2012. T
taxes requires the impact of a change in tax law to be immediately recognized in the period that includes the enactme
of the Patient Protection and Affordable Care Act and Education Reconciliation Act of 2010 did not impact us
a result of Medicare Part D subsidies received.

## 12. Income Taxes

**Income Tax Provision**

In accordance with current accounting guidance, the principal method established for computing the provision for in
make our best estimate of the effective tax rate expected to be applicable for the full year. This estimated effective ta
pre-tax operating income to determine the interim provision for income taxes. This method has been used to determi
for income taxes for the quarters ended March 31, 2010 and June 30, 2009.

However, the accounting guidance allows for an alternative method to computing the effective tax rate and, thus the
taxpayer is unable to calculate a reliable estimate of the effective tax rate for the entire year. Due to the current econ
the alternative method is more reliable in determining the provision for income taxes for the second quarter of 2010.
calculated by applying the statutory federal income tax rate to the quarter s consolidated operating income before ta
recognized in the quarter which include income from corporate-owned life insurance and tax credits related to invest
then adding state taxes.

**Deferred Tax Asset**

As of June 30, 2010, we had a net deferred tax asset from continuing operations of $594 million compared to a net d
of $577 million as of December 31, 2009 included in accrued income and other assets on the balance sheet; prior
deferred tax liability position. To determine the amount of deferred tax assets that are more likely than not to be real
quarterly assessment of all available evidence. This evidence includes, but is not limited to, taxable income in prior p
projected future reversals of deferred tax items. Based on these criteria, and in particular our projections for future ta
more likely than not that we will realize the net deferred tax asset in future periods.

**Unrecognized Tax Benefits**

As permitted under the applicable accounting guidance for income taxes, it is our policy to recognize interest and pe
income tax expense.

## 13. Commitments, Contingent Liabilities and Guarantees

**Legal Proceedings**

***Shareholder derivative matter.*** On July 6, 2010, certain current and former directors and executive officers of KeyC
*King, Jr. v. Henry L. Meyer III, et al.*, a shareholder derivative lawsuit filed in the Cuyahoga County Court of Comm
KeyCorp defendants violated their fiduciary duties, including their duties of candor, good faith and loyalty, and are l
enrichment in connection with 2009 executive compensation decisions.

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The complaint seeks unspecified compensatory damages from the KeyCorp defendants, various forms of equitable a
other professional fees and costs. KeyCorp was also named as a nominal defendant in the lawsuit, but no damages ar
KeyCorp s Board of Directors has appointed a special committee of non-management directors to assess its executi
the allegations made in the complaint. This committee has retained an independent law firm to assist in its investigat

***Taylor litigation.*** On August 11, 2008, a purported class action case was filed against KeyCorp, its directors and cer
*et al.,* in the United States District Court for the Northern District of Ohio. On September 16, 2008, a second and rel
captioned *Wildes v. KeyCorp et al*. The plaintiffs in these cases seek to represent a class of all participants in our 401
defendants in the lawsuit breached fiduciary duties owed to them under ERISA. On January 7, 2009, the Court conso
single action. Plaintiffs have since filed their consolidated complaint, which continues to name certain employees as
directors. We strongly disagree with the allegations asserted against us in these actions, and intend to vigorously def

***Madoff-related claims.*** In December 2008, Austin, a subsidiary that specialized in managing hedge fund investment
its funds had suffered investment losses of up to approximately $186 million resulting from the crimes perpetrated b
controlled. The investment losses borne by Austin s clients stem from investments that Austin made in certain Mad
including putative class actions and direct actions, and one arbitration proceeding were filed against Austin seeking
Madoff s crimes. The lawsuits and arbitration proceeding allege various claims, including negligence, fraud, breach
securities laws and ERISA. In the event we were to incur any liability for this matter, we believe it would be covered
insurance policy, subject to a $25 million self-insurance deductible and usual policy exceptions.

In April 2009, we decided to wind down Austin s operations and have determined that the related exit costs will not
discontinued operations is included in Note 16 ( Discontinued Operations ).

***Data Treasury matter.*** In February 2006, an action styled *DataTreasury Corporation v. Wells Fargo & Company, e*
numerous other financial institutions, as owners and users of Small Value Payments Company, LLC software, in the
District of Texas. The plaintiff alleges patent infringement and is seeking an unspecified amount of damages and tre
entered an order establishing three trial dates due to the number of defendants involved in the action, including an O
trial phase codefendants. We strongly disagree with the allegations asserted against us, and have been vigorously de
has established appropriate reserves for the matter consistent with applicable accounting guidance.

***Other litigation***. In the ordinary course of business, we are subject to other legal actions that involve claims for subs
presently known to us, we do not believe there is any legal action to which we are a party, or involving any of our pr
would reasonably be expected to have a material adverse effect on our financial condition.

**Guarantees**

We are a guarantor in various agreements with third parties. The following table shows the types of guarantees that
Information pertaining to the basis for determining the liabilities recorded in connection with these guarantees is inc

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Significant Accounting Policies ) under the heading Guarantees on page 84 of our 2009 Annual Report to Sharel

**June 30, 2010**
*in millions*

Financial guarantees:
Standby letters of credit
Recourse agreement with FNMA
Return guarantee agreement with LIHTC investors
Written put options [(a)]
Default guarantees

Total

(a) The maximum potential undiscounted future payments represent notional amounts of derivatives qualifying as guarantees.

We determine the payment/performance risk associated with each type of guarantee described below based on the pr the maximum potential undiscounted future payments shown in the preceding table. We use a scale of low (0-30% p probability of payment) or high (71-100% probability of payment) to assess the payment/performance risk, and have risk associated with each type of guarantee outstanding at June 30, 2010, is low.

***Standby letters of credit.*** KeyBank issues standby letters of credit to address clients financing needs. These instrun when a client fails to repay an outstanding loan or debt instrument, or fails to perform some contractual nonfinancial standby letters of credit are treated as loans to the client; they bear interest (generally at variable rates) and pose the 2010, our standby letters of credit had a remaining weighted-average life of 1.6 years, with remaining actual lives ra ten years.

***Recourse agreement with FNMA.*** We participate as a lender in the FNMA Delegated Underwriting and Servicing p originating, underwriting and servicing mortgages, and we assume a limited portion of the risk of loss during the ren loan that we sell to FNMA. We maintain a reserve for such potential losses in an amount that we believe approximat 2010, the outstanding commercial mortgage loans in this program had a weighted-average remaining term of 5.9 yea outstanding of loans sold by us as a participant in this program was $2.2 billion. As shown in the preceding table, th future payments that we could be required to make under this program is equal to approximately one-third of the pri June 30, 2010. If we are required to make a payment, we would have an interest in the collateral underlying the relat loss incurred could be offset by the amount of any recovery from the collateral.

***Return guarantee agreement with LIHTC investors.*** KAHC, a subsidiary of KeyBank, offered limited partnership i formed by KAHC invested in low-income residential rental properties that qualify for federal low income housing ta Revenue Code. In certain partnerships, investors paid a fee to KAHC for a guaranteed return that is based on the fina property s confirmed LIHTC status throughout a fifteen-year compliance period. Typically, KAHC provides these g and deductions associated with the specific properties. If KAHC defaults on its obligation to provide the guaranteed

necessary payments to investors. No recourse or collateral is available to offset our guarantee obligation other than t
properties and the residual value of the operating partnership interests.

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As shown in the previous table, KAHC maintained a reserve in the amount of $62 million at June 30, 2010, which w
future obligations under the guarantees. The maximum exposure to loss reflected in the table represents undiscounte
return on and of their investments.

These guarantees have expiration dates that extend through 2019, but there have been no new partnerships formed u
Additional information regarding these partnerships is included in Note 7 ( Variable Interest Entities ).

***Written put options.*** In the ordinary course of business, we write interest rate caps and floors for commercial loan
respectively, with us and wish to mitigate their exposure to changes in interest rates. At June 30, 2010, our written p
These instruments are considered to be guarantees as we are required to make payments to the counterparty (the com
underlying variable that is related to an asset, a liability or an equity security held by the guaranteed party. We are ob
benchmark interest rate is above or below a specified level (known as the strike rate ). These written put options a
which are further discussed in Note 14 ( Derivatives and Hedging Activities ). We typically mitigate our potential
positions with third parties.

Written put options where the counterparty is a broker-dealer or bank are accounted for as derivatives at fair value, b
counterparties do not typically hold the underlying instruments. In addition, we are a purchaser and seller of credit d
Note 14.

***Default guarantees.*** Some lines of business participate in guarantees that obligate us to perform if the debtor (typica
obligations to third parties. We generally undertake these guarantees for one of two possible reasons: either the risk
investment return, or we are supporting our underlying investment. The terms of these default guarantees range from
some default guarantees do not have a contractual end date. Although no collateral is held, we would receive a pro ra
or all of the amounts due from the debtor.

**Other Off-Balance Sheet Risk**

Other off-balance sheet risk stems from financial instruments that do not meet the definition of a guarantee as specif
guarantees, and from other relationships.

***Liquidity facilities that support asset-backed commercial paper conduits.*** We provide liquidity facilities to several
conduits. These facilities obligate us to provide funding in the event that a credit market disruption or other factors p
paper. At June 30, 2010, we had one liquidity facility remaining, which will expire by May, 2011, obligating us to p
The aggregate amount available to be drawn is based on the amount of current commitments to borrowers and totale
periodically evaluate our commitments to provide liquidity.

***Indemnifications provided in the ordinary course of business.*** We provide certain indemnifications, primarily throu
contracts that we execute in the ordinary course of business in connection with loan sales and other ongoing activitie
sales of businesses. We maintain reserves, when appropriate, with respect to liability that reasonably could arise in c

***Intercompany guarantees.*** KeyCorp and certain of our affiliates are parties to various guarantees that facilitate the o
These business activities encompass debt issuance, certain lease and insurance obligations, the purchase or issuance
leasing transactions involving clients.

***Heartland Payment Systems matter.*** Under an agreement between KeyBank and Heartland Payment Systems, Inc. ( membership in the Visa and MasterCard networks to provide merchant payment processing services for Visa and M Heartland publicly announced its discovery of an alleged criminal breach of its credit card payment processing syste reportedly occurred during 2008 and allegedly involved the malicious collection of in-transit, unencrypted payment Heartland s 2008 Form 10-K filed with the SEC on March 10, 2009, ( Heartland s 2008 Form 10-K ) reported tha MasterCard, asserted claims seeking to impose fines, penalties, and/or other assessments against Heartland and/or ce as a result of the alleged potential breach of the respective card brand rules and regulations, and the alleged criminal systems environment.

KeyBank has received letters from both Visa and MasterCard imposing fines, penalties or assessments related to the Heartland, KeyBank has certain rights of indemnification from Heartland for costs assessed against it by Visa and M KeyBank has notified Heartland of its indemnification rights. In the event that Heartland is unable to fulfill its inden charges (net of any indemnification) could be significant, although it is not possible to quantify them at this time. Ac we have not established any reserve.

In Heartland s Form 10-K filed with the SEC on March 10, 2010 ( Heartland s 2009 Form 10-K ), Heartland disc reported settlement among Heartland, Visa U.S.A. Inc., Visa International Service Association, and Visa Inc., and th Heartland Bank.

In Heartland s Form 8-K filed with the SEC on May 19, 2010, Heartland disclosed that it had entered into a settlem Incorporated to resolve potential claims and other disputes among Heartland, the Acquiring Banks, including KeyBa MasterCard and certain MasterCard Issuers, on the other hand, with respect to potential rights of MasterCard issuers MasterCard and MasterCard Issuers related to the Intrusion. The maximum potential aggregate amounts payable to t Settlement Agreement will not exceed $41.4 million, including MasterCard s credit of $6.6 million of the non-comp amounts. The Settlement Agreement contains mutual releases between Heartland and the Acquiring Bank, on the on Issuers who accept the recovery offers, on the other hand, of claims relating to the Intrusion. Consummation of the s termination period. At March 31, 2010, Heartland carried a $42.8 million reserve for the Intrusion (before adjustmen For further information on Heartland and the Intrusion, see Heartland s 2009 Form 10-K, Heartland s 2008 Form 1 on May 11, 2009, August 7, 2009, and May 7, 2010, Heartland s Form 8-K filed with the SEC on August 4, 2009, N 2010, February 18, 2010, February 24, 2010, and May 19, 2010.

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## 14. Derivatives and Hedging Activities

We are a party to various derivative instruments, mainly through our subsidiary, KeyBank. Derivative instruments a
have a notional amount and an underlying variable, require no net investment and allow for the net settlement of pos
as the basis for the payment provision of the contract, and takes the form of units, such as shares or dollars. A deriva
interest rate, security price, commodity price, foreign exchange rate, index or other variable. The interaction betwee
variable determines the number of units to be exchanged between the parties and influences the fair value of the deri
The primary derivatives that we use are interest rate swaps, caps, floors and futures; foreign exchange contracts; ene
derivatives. Generally, these instruments help us manage exposure to interest rate risk, mitigate the credit risk inhere
changes in foreign currency exchange rates, and meet client financing and hedging needs. Interest rate risk represent
equity or net interest income will be adversely affected by fluctuations in interest rates. Credit risk is the risk of loss
meet contractual payment or performance terms. Foreign exchange risk is the risk that an exchange rate will adverse
instrument.

Derivative assets and liabilities are recorded at fair value on the balance sheet, after taking into account the effects o
agreements. These bilateral collateral and master netting agreements allow us to settle all derivative contracts held w
offset net derivative positions with related collateral, where applicable. As a result, we could have derivative contrac
derivative assets on the balance sheet and contracts with positive fair values included in derivative liabilities.

At June 30, 2010, after taking into account the effects of bilateral collateral and master netting agreements, we had $
$244 million of derivative liabilities that relate to contracts entered into for hedging purposes. As of the same date, a
collateral and master netting agreements, and a reserve for potential future losses, we had derivative assets of $872 n
that were not designated as hedging instruments.

The recently enacted Dodd-Frank Act may limit the types of derivatives activities conducted by KeyBank and other
is possible that our continued use of one or more of the types of derivatives noted above could be affected.

Additional information regarding our accounting policies for derivatives is provided in Note 1 (  Basis of Presentatio
of our 2009 Annual Report to Shareholders.

### Derivatives Designated in Hedge Relationships

Changes in interest rates and differences in the repricing and maturity characteristics of interest-earning assets and i
fluctuations in net interest income and the economic value of equity. To minimize the volatility of net interest incom
interest rate risk in accordance with policy limits established by the Enterprise Risk Management Committee. We ut
part of a hedge relationship in accordance with the applicable accounting guidance for derivatives and hedging to mi
derivative instruments used to manage interest rate risk are interest rate swaps, which modify the interest rate charac
instruments are used to convert the contractual interest rate index of agreed-upon amounts of assets and liabilities (i.
index.

We designate certain  receive fixed/pay variable  interest rate swaps as fair value hedges. These swaps are used pri
risk. These contracts convert certain fixed-rate long-

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term debt into variable-rate obligations. As a result, we receive fixed-rate interest payments in exchange for making
contracts without exchanging the notional amounts.

Similarly, we designate certain receive fixed/pay variable interest rate swaps as cash flow hedges. These contract
into fixed-rate loans to reduce the potential adverse effect of interest rate decreases on future interest income. These
interest payments in exchange for making variable-rate payments over the lives of the contracts without exchanging
certain pay fixed/receive variable interest rate swaps as cash flow hedges. These swaps are used to convert certai

We also use interest rate swaps to hedge the floating-rate debt that funds fixed-rate leases entered into by our Equip
are designated as cash flow hedges to mitigate the interest rate mismatch between the fixed-rate lease cash flows and

The derivatives used for managing foreign currency exchange risk are cross currency swaps. We have several outsta
are denominated in foreign currencies. The notes are subject to translation risk, which represents the possibility that
foreign-denominated debt will occur based on movement of the underlying foreign currency spot rate. It is our pract
changes caused by changes in foreign currency exchange rates and interest rates. The hedge converts the notes to a v
which is designated as a fair value hedge of foreign currency exchange risk.

**Derivatives Not Designated in Hedge Relationships**

On occasion, we enter into interest rate swap contracts to manage economic risks but do not designate the instrumen
significant amount in interest rate swap contracts entered into to manage economic risks at June 30, 2010.

Like other financial services institutions, we originate loans and extend credit, both of which expose us to credit risk
portfolio and the associated credit risk in a manner consistent with asset quality objectives. This process entails the u
default swaps ¾ to mitigate our credit risk. Credit default swaps enable us to transfer to a third party a portion of the
extension of credit, and to manage portfolio concentration and correlation risks. Occasionally, we also provide credi
of credit default swaps. In most instances, this objective is accomplished through the use of an investment-grade div
swaps. These transactions may generate fee income, and diversify and reduce overall portfolio credit risk volatility.
management purposes, they are not treated as hedging instruments as defined by the applicable accounting guidance

We also enter into derivative contracts to meet customer needs and for proprietary purposes that consist of the follov

w interest rate swap, cap, floor and futures contracts entered into generally to accommodate the needs of commerci

w energy swap and options contracts entered into to accommodate the needs of clients;

w interest rate swaps and foreign exchange contracts used for proprietary trading purposes;

w positions with third parties that are intended to offset or mitigate the interest rate or market risk related to client p

w foreign exchange forward contracts entered into to accommodate the needs of clients.

These contracts are not designated as part of hedge relationships.

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**Fair Values, Volume of Activity and Gain/Loss Information Related to Derivative Instruments**

The following table summarizes the fair values of our derivative instruments on a gross basis as of June 30, 2010, D volume of our derivative transaction activity during the first half of 2010 is represented by the change in the notiona from December 31, 2009 to June 30, 2010. The notional amounts are not affected by bilateral collateral and master n are included in derivative assets or derivative liabilities on the balance sheet, as indicated in the following tabl

| | June 30, 2010 | | | December 31, 2009 | | |
|---|---|---|---|---|---|---|
| | | Fair Value | | | Fair Value | |
| *in millions* | **Notional Amount** | **Derivative Assets** | **Derivative Liabilities** | **Notional Amount** | **Derivative Assets** | **Derivative Liabilities** |
| Derivatives designated as hedging instruments: | | | | | | |
| Interest rate | **$ 14,168** | **$ 601** | **$ 4** | $ 18,259 | $ 489 | $ 9 |
| Foreign exchange | **1,383** | **14** | **334** | 1,888 | 78 | 189 |
| Total | **15,551** | **615** | **338** | 20,147 | 567 | 198 |
| Derivatives not designated as hedging instruments: | | | | | | |
| Interest rate | **65,173** | **1,624** | **1,611** | 70,017 | 1,434 | 1,345 |
| Foreign exchange | **7,617** | **183** | **163** | 6,293 | 206 | 184 |
| Energy and commodity | **2,031** | **344** | **364** | 1,955 | 403 | 427 |
| Credit | **3,640** | **47** | **37** | 4,538 | 55 | 49 |
| Equity | **18** | **1** | **1** | 3 | 1 | 1 |
| Total | **78,479** | **2,199** | **2,176** | 82,806 | 2,099 | 2,006 |
| Netting adjustments [a] | **N/A** | **(1,661)** | **(1,193)** | N/A | (1,572) | (1,192) |
| Total derivatives Total | **$ 94,030** | **$ 1,153** | **$ 1,321** | $ 102,953 | $ 1,094 | $ 1,012 |

(a) Netting adjustments represent the amounts recorded to convert our derivative assets and liabilities from a gross basis to a net basis in accordance with the applicable accounting guidance related to the offsetting of certain derivative contracts on the balance sheet. The net basis takes into account the impact of bilateral collateral and master netting agreements that allow us to settle all derivative contracts with a single counterparty on a net basis and to offset the net derivative position with the related collateral.

***Fair value hedges.*** Instruments designated as fair value hedges are recorded at fair value and included in derivativ
sheet. The effective portion of a change in the fair value of a hedging instrument designated as a fair value hedge is r
change in fair value of the hedged item, resulting in no effect on net income. The ineffective portion of a change in t
recorded in other income on the income statement with no corresponding offset. During the six-month period end
portion of these hedging instruments from the assessment of hedge effectiveness. While some ineffectiveness is pres
fair value hedges remained highly effective as of June 30, 2010.

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The following table summarizes the pre-tax net gains (losses) on our fair value hedges for the six-month periods end
are recorded on the income statement.

| | | | Six months ended Jun | |
|---|---|---|---|---|
| *in millions* | **Income Statement Location of Net Gains (Losses) on Derivative** | **Net Gains (Losses) on Derivative** | **Hedged Item** | **Incom** |
| Interest rate | Other income | **$ 184** | Long-term debt | |
| Interest rate | Interest expense Long-term debt | **109** | | |
| Foreign exchange | Other income | **(264)** | Long-term debt | |
| Foreign exchange | Interest expense Long-term debt | **3** | Long-term debt | Inte |
| Total | | **$ 32** | | |

| | | | Six months ended Jun | |
|---|---|---|---|---|
| *in millions* | **Income Statement Location of Net Gains (Losses) on Derivative** | **Net Gains (Losses) on Derivative** | **Hedged Item** | **Incon** |
| Interest rate | Other income | $ (437) | Long-term debt | |
| Interest rate | Interest expense Long-term | 112 | | |

| | | | | |
|---|---|---|---|---|
| | debt | | | |
| Foreign exchange | Other income | 66 | Long-term debt | |
| | Interest expense | | | |
| Foreign exchange | Long-term debt | 12 | Long-term debt | Inte |
| Total | | $ (247) | | |

(a) Net gains (losses) on hedged items represent the change in fair value caused by fluctuations in interest rates.

(b) Net losses on hedged items represent the change in fair value caused by fluctuations in foreign currency exchange rates.

***Cash flow hedges.*** Instruments designated as cash flow hedges are recorded at fair value and included in derivative sheet. The effective portion of a gain or loss on a cash flow hedge is initially recorded as a component of AOCI on th into income when the hedged transaction impacts earnings (e.g. when we pay variable-rate interest on debt, receive v sell commercial real estate loans). The ineffective portion of cash flow hedging transactions is included in other inc six-month period ended June 30, 2010, we did not exclude any portion of these hedging instruments from the assess ineffectiveness is present in our hedging relationships, all of our cash flow hedges remained highly effective as of The following table summarizes the pre-tax net gains (losses) on our cash flow hedges for the six-month periods end are recorded on the income statement. The table includes the effective portion of net gains (losses) recognized in OC net gains (losses) reclassified from OCI into income during the current period and the portion of net gains (losses) re amount of hedge ineffectiveness.

| | | | Six months ended June 30, |
|---|---|---|---|
| *in millions* | **Net Gains (Losses) Recognized in OCI (Effective Portion)** | **Income Statement Location of Net Gains (Losses) Reclassified From OCI Into Income (Effective Portion)** | **Net Gai (Losse Reclassifie From OCI In Incon (Effectiv Portio** |

| | | | |
|---|---|---|---|
| Interest rate | **$ 42** | Interest income Loans | **$ 13** |
| Interest rate | **(22)** | Interest expense Long-term debt | **(1** |
| Interest rate | | Net gains (losses) from loan securitizations and sales | |
| Total | **$ 20** | | **$ 12** |
| Total | | | |

**Six months ended June 30,**

| *in millions* | **Net Gains (Losses) Recognized in OCI (Effective Portion)** | **Income Statement Location of Net Gains (Losses) Reclassified From OCI Into Income (Effective Portion)** | **Net Gain (Losses Reclassifie From OCI Int Incom (Effectiv Portion** |
|---|---|---|---|
| Interest rate | $ 102 | Interest income Loans | $ 23 |
| Interest rate | 25 | Interest expense Long-term debt | ( |
| Interest rate | 4 | Net gains (losses) from loan securitizations and sales | |
| Total | $ 131 | | $ 22 |
| Total | | | |

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The after-tax change in AOCI resulting from cash flow hedges is as follows:

| in millions | | December 31, 2009 | | 2 Hedg Acti |
|---|---|---|---|---|
| Accumulated other comprehensive income resulting from cash flow hedges | $ | 114 | $ | |

Considering the interest rates, yield curves and notional amounts as of June 30, 2010, we would expect to reclassify
derivative instruments from AOCI to income during the next twelve months. In addition, we expect to reclassify app
terminated cash flow hedges from AOCI to income during the next 12 months. The maximum length of time over w
18 years.

***Nonhedging instruments.*** Our derivatives that are not designated as hedging instruments are recorded at fair value i
the balance sheet. Adjustments to the fair values of these instruments, as well as any premium paid or received, are i
markets income (loss) on the income statement.

The following table summarizes the pre-tax net gains (losses) on our derivatives that are not designated as hedging i
June 30, 2010 and 2009, and where they are recorded on the income statement.

| in millions | Six months ended June 30, 2010 | | | 2009 |
|---|---|---|---|---|
| **NET GAINS (LOSSES)** [(a)] | | | | |
| Interest rate | **$** | **7** | $ | 15 |
| Foreign exchange | | **20** | | 31 |
| Energy and commodity | | **4** | | 4 |
| Credit | | **(9)** | | (23) |
| Total net gains (losses) | **$** | **22** | $ | 27 |

(a) Recorded in investment banking and capital markets income (loss) on the income statement.

**Counterparty Credit Risk**

Like other financial instruments, derivatives contain an element of credit risk. This risk is measured as the expected
We use several means to mitigate and manage exposure to credit risk on derivative contracts. We generally enter int
agreements using standard forms published by ISDA. These agreements provide for the net settlement of all contrac
default. Additionally, we monitor counterparty credit risk exposure on each contract to determine appropriate limits
types. We review our collateral positions on a daily basis and exchange collateral with our counterparties in accorda
We generally hold collateral in the form of cash and highly rated securities issued by the U.S. Treasury, government

collateral netted against derivative assets on the balance sheet totaled $469 million at June 30, 2010, $381 million at June 30, 2009. The collateral netted against derivative liabilities totaled $2 million at June 30, 2010, less than $1 mil at June 30, 2009.

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The following table summarizes our largest exposure to an individual counterparty at the dates indicated.

| *in millions* | **June 3** **201** |
|---|---|
| Largest gross exposure to an individual counterparty | **$ 21** |
| Collateral posted by this counterparty | **3** |
| Derivative liability with this counterparty | **32** |
| Collateral pledged to this counterparty | **15** |
| Net exposure after netting adjustments and collateral | **2** |

The following table summarizes the fair value of our derivative assets by type. These assets represent our gross expo
the effects of bilateral collateral and master netting agreements and other means used to mitigate risk.

| *in millions* | **June 3** **201** |
|---|---|
| Interest rate | **$ 1,43** |
| Foreign exchange | **9** |
| Energy and commodity | **7** |
| Credit | **1** |
| Equity | |
| Derivative assets before collateral | **1,62** |
| Less: Related collateral | **46** |
| Total derivative assets | **$ 1,15** |

We enter into derivative transactions with two primary groups: broker-dealers and banks, and clients. Since these gr
we have different methods for managing counterparty credit exposure and credit risk.

We enter into transactions with broker-dealers and banks for various risk management purposes and proprietary trad
generally are high dollar volume. We generally enter into bilateral collateral and master netting agreements with the
taking into account the effects of bilateral collateral and master netting agreements, we had gross exposure of $1.1 b
exposure of $314 million after the application of master netting agreements and collateral; our net exposure to broke
reduced to $84 million with the $230 million of additional collateral held in the form of securities.

We enter into transactions with clients to accommodate their business needs. These types of transactions generally a
master netting agreements with these counterparties. In addition, we mitigate our overall portfolio exposure and mar
with broker-dealers and other banks. Due to the smaller size and magnitude of the individual contracts with clients, c
connection with these derivative transactions. To address the risk of default associated with the uncollateralized con
(included in derivative assets ) in the amount of $80 million at June 30, 2010, which we estimate to be the potentia
counterparties in the event of default. At June 30, 2009 and December 31, 2009 the default reserve was $52 million a
2010, after taking into account the effects of master netting agreements, we had gross exposure of $958 million to cl
$841 million on our derivatives with clients after the application of master netting agreements, collateral and the rela

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**Credit Derivatives**

We are both a buyer and seller of credit protection through the credit derivative market. We purchase credit derivativ
specific commercial lending and swap obligations. We also sell credit derivatives, mainly index credit default swaps
loan portfolio.

The following table summarizes the fair value of our credit derivatives purchased and sold by type. The fair value of
take into account the effects of bilateral collateral or master netting agreements.

| | June 30, 2010 | | | December 31, 2009 | | |
|---|---|---|---|---|---|---|
| *in millions* | **Purchased** | **Sold** | **Net** | **Purchased** | **Sold** | **Ne** |
| Single name credit default swaps | **$ 12** | **$ (4)** | **$ 8** | $ 5 | $ (3) | $ 2 |
| Traded credit default swap indices | **1** | **(2)** | **(1)** | 2 | | 2 |
| Total credit derivatives Other | **5** | **(2)** | **3** | (1) | 4 | 3 |
| Total credit derivatives | **$ 18** | **$ (8)** | **$ 10** | $ 6 | $ 1 | $ 7 |

Single name credit default swaps are bilateral contracts whereby the seller agrees, for a premium, to provide protecti
in connection with a specific debt obligation. The protected credit risk is related to adverse credit events, such as ban
acceleration or restructuring of obligations, specified in the credit derivative contract using standard documentation t
single name credit derivative, we would be required to pay the purchaser the difference between the par value and th
settlement) or receive the specified referenced asset in exchange for payment of the par value (physical settlement) i
predefined credit event. For a single name credit derivative, the notional amount represents the maximum amount th
event that physical settlement occurs and we receive our portion of the related debt obligation, we will join other cre
result in the recovery of a portion of the amount paid under the credit default swap contract. We also may purchase c
reference entity from third parties that will permit us to recover the amount we pay should a credit event occur.

A traded credit default swap index represents a position on a basket or portfolio of reference entities. As a seller of p
would be required to pay the purchaser if one or more of the entities in the index had a credit event. For a credit defa
represents the maximum amount that a seller could be required to pay. Upon a credit event, the amount payable is ba
allocated to the specific defaulting entity.

The majority of transactions represented by the other category shown in the above table are risk participation agre
participant has a swap agreement with a customer. The lead participant (purchaser of protection) then enters into a ri
counterparty (seller of protection), under which the counterparty receives a fee to accept a portion of the lead partici
the swap contract, the counterparty to the risk participation agreement must reimburse the lead participant for the co
value of the customer swap as of the default date. If the customer swap has a negative fair value, the counterparty ha
notional amount represents the maximum amount that the seller could be required to pay. In the case of customer de
of the lead participant s claims against the customer under the terms of the initial swap agreement between the lead

The following table provides information on the types of credit derivatives sold by us and held on the balance sheet
June 30, 2009. The payment/performance risk assessment is based on the default probabilities for the underlying refe
credit ratings matrix provided by Moody s, specifically Moody s Idealized Cumulative Default Rates, except as
table represents a weighted-average of

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the default probabilities for all reference entities in the respective portfolios. These default probabilities are directly
to make a payment under the credit derivative contracts.

| | June 30, 2010 | | | December 31, 2009 | | |
|---|---|---|---|---|---|---|
| *dollars in millions* | **Notional Amount** | **Average Term (Years)** | **Payment / Performance Risk** | **Notional Amount** | **Average Term (Years)** | **Payment / Performance Risk** |
| Single name credit default swaps | **$ 1,102** | **2.45** | **4.10 %** | $ 1,140 | 2.57 | 4.88 % |
| Traded credit default swap indices | **344** | **4.00** | **8.08** | 733 | 2.71 | 13.29 |
| Other | **46** | **3.09** | **7.70** | 44 | 1.94 | 5.41 |
| Total credit derivatives sold | **$ 1,492** | | | $ 1,917 | | |

(a) The other credit derivatives were not referenced to an entity s debt obligation. We determined the payment/performance risk based on the probability that we could be required to pay the maximum amount under the credit derivatives. We have determined that the payment/performance risk associated with the other credit derivatives was low (i.e., less than or equal to 30% probability of payment).

**Credit Risk Contingent Features**

We have entered into certain derivative contracts that require us to post collateral to the counterparties when these c
amount of collateral to be posted is based on the amount of the net liability and thresholds generally related to our lo
Moody s and S&P. Collateral requirements are also based on minimum transfer amounts, which are specific to each
ISDA Master Agreement) that we have signed with the counterparties. In a limited number of instances, counterpart
Master Agreements with us if our ratings fall below a certain level, usually investment-grade level (i.e., Baa3 for
KeyBank s ratings with Moody s and S&P were A2 and A-, respectively, and KeyCorp s ratings with Mood
were a downgrade of our ratings, we could be required to post additional collateral under those ISDA Master Agreen
As of June 30, 2010, the aggregate fair value of all derivative contracts with credit risk contingent features (i.e., thos

provisions based on our ratings) held by KeyBank that were in a net liability position totaled $1.1 billion, which incl
$1.9 billion in derivative liabilities. We had $1.1 billion in cash and securities collateral posted to cover those positio
The following table summarizes the additional cash and securities collateral that KeyBank would have been required
features been triggered for the derivative contracts in a net liability position as of June 30, 2010, December 31, 2009
amounts were calculated based on scenarios under which KeyBank s ratings are downgraded one, two or three ratin
all collateral already posted. At June 30, 2010, KeyCorp did not have any derivatives in a net liability position that c

| | June 30, 2010 | | December 31, 200 | |
|---|---|---|---|---|
| *in millions* | **Moody s** | **S&P** | **Moody s** | |
| KeyBank s long-term senior unsecured credit ratings | **A2** | **A-** | A2 | |
| One rating downgrade | **$ 28** | **$ 22** | $ 34 | $ |
| Two rating downgrades | **51** | **25** | 56 | |
| Three rating downgrades | **59** | **30** | 65 | |

If KeyBank s ratings had been downgraded below investment grade as of June 30, 2010, payments of up to $81 mil
terminate the contracts or post additional collateral for those contracts in a net liability position, taking into account
downgraded below investment grade, KeyBank s long-term senior unsecured credit rating would need to be downg
by S&P.

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## 15. Fair Value Measurements

### Fair Value Determination

As defined in the applicable accounting guidance for fair value measurements and disclosures, fair value is the price
orderly transaction between market participants in our principal market. We have established and documented our pr
assets and liabilities, where applicable. Fair value is based on quoted market prices, when available, for identical or s
quoted market prices, we determine the fair value of our assets and liabilities using valuation models or third-party p
on market-based parameters when available, such as interest rate yield curves, option volatilities and credit spreads,
may be based on our judgment, assumptions and estimates related to credit quality, liquidity, interest rates and other
Valuation adjustments, such as those pertaining to counterparty and our own credit quality and liquidity, may be nec
recorded at fair value. Credit valuation adjustments are made when market pricing is not indicative of the counterpar
When we are unable to observe recent market transactions for identical or similar instruments, we make liquidity val
the uncertainty in the pricing and trading of the instrument. Liquidity valuation adjustments are based on the followi

- the amount of time since the last relevant valuation;
- whether there is an actual trade or relevant external quote available at the measurement date; and
- volatility associated with the primary pricing components.

We ensure that our fair value measurements are accurate and appropriate by relying upon various controls, including

- an independent review and approval of valuation models;
- a detailed review of profit and loss conducted on a regular basis; and
- a validation of valuation model components against benchmark data and similar products, where possible.

We review any changes to valuation methodologies to ensure they are appropriate and justified, and refine valuation
becomes available.

Additional information regarding our accounting policies for the determination of fair value is provided in Note 1 (
under the heading Fair Value Measurements on page 84 of our 2009 Annual Report to Shareholders.

### Qualitative Disclosures of Valuation Techniques

***Loans***. Loans recorded as trading account assets are valued using an internal cash flow model because the market in
active. The most significant inputs to our internal model are actual and projected financial results for the individual b
classified as Level 3 assets. As of June 30, 2010, there was one loan that was actively traded. This loan was valued b
and, therefore, classified as Level 2 since the fair value recorded is based on observable market data.

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***Securities (trading and available for sale)***. Securities are classified as Level 1 when quoted market prices are availa
securities. Level 1 instruments include exchange-traded equity securities. If quoted prices for identical securities are
pricing models or quoted prices of similar securities. These instruments, classified as Level 2 assets, include municip
government, corporate bonds, certain mortgage-backed securities, securities issued by the U.S. Treasury and certain
obligations. Inputs to the pricing models include actual trade data (i.e., spreads, credit ratings and interest rates) for c
high-grade scales, option-adjusted spreads and standard inputs, such as yields, broker/dealer quotes, bids and offers.
for a particular instrument, we use internal models based on certain assumptions to determine fair value. Such instru
certain commercial mortgage-backed securities and certain commercial paper. Inputs for the Level 3 internal models
underlying loans, which take into account expected default and recovery percentages, market research and discount r
conditions.
***Private equity and mezzanine investments***. Private equity and mezzanine investments consist of investments in debt
Capital line of business. They include direct investments made in a property, as well as indirect investments made in
purpose of investing in properties. There is not an active market in which to value these investments. The direct inve
transaction price. The carrying amount is then adjusted based upon the estimated future cash flows associated with th
future cash flows include the cost of build-out, future selling prices, current market outlook and operating performan
investments are valued using a methodology that is consistent with accounting guidance that allows us to use statem
net asset value per share. A primary input used in estimating fair value is the most recent value of the capital accoun
investee funds. Private equity and mezzanine investments are classified as Level 3 assets since our judgment impacts
Within private equity and mezzanine investments, we have investments in real estate private equity funds. The main
portfolio of real estate investments that provides attractive risk-adjusted returns and current income for investors. Ce
determinable fair values and represent our ownership interest in an entity that follows measurement principles under
following table presents the fair value of the funds and related unfunded commitments at June 30, 2010:

**June 30, 2010**
*in millions*

| | |
|---|---|
| **INVESTMENT TYPE** | |
| Passive funds [(a)] | |
| Co-managed funds [(b)] | |
| Total | |

(a) We invest in passive funds, which are multi-investor private equity funds. These investments can never be redeemed. Instead, distributions are received through the liquidation of the underlying investments in the funds. Some funds have no restrictions on sale, while others require investors to remain in the fund until maturity. The funds will be liquidated over a period of one to six years.

(b) We are a manager or co-manager of these funds. These investments can never be redeemed. Instead, distributions are received through the liquidation of the underlying investments in the funds. In addition, we receive management fees. A sale or transfer of our interest in the funds can only occur through written consent of a majority of the fund s investors. In one instance, the other co-manager of the fund must consent to the sale or transfer of our interest in the fund. The funds will

mature over a
period of four to
seven years.

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***Principal investments***. Principal investments consist of investments in equity and debt instruments made by our prin investments (investments made in a particular company), as well as indirect investments (investments made through predominantly privately held companies and funds. When quoted prices are available in an active market for the ide in the valuation process, and the related investments are classified as Level 1 assets. However, in most cases, quoted identical investment, and we must rely upon other sources and inputs, such as market multiples; historical and foreca depreciation and amortization; net debt levels; and investment risk ratings to perform the valuations of the direct inv primary and secondary investments in private equity funds engaged mainly in venture- and growth-oriented investin values. The indirect investments are valued using a methodology that is consistent with accounting guidance that all value per share (or its equivalent, such as member units or an ownership interest in partners capital to which a prop primary input used in estimating fair value is the most recent value of the capital accounts as reported by the general investments are classified as Level 3 assets since our assumptions impact the overall determination of fair value. The indirect funds and related unfunded commitments at June 30, 2010:

**June 30, 2010**
*in millions*

| |
|---|
| **INVESTMENT TYPE** |
| Private equity funds [(a)] |
| Hedge funds [(b)] |
| Total |

(a) Consists of buyout, venture capital and fund of funds. These investments can never be redeemed with the investee funds. Instead, distributions are received through the liquidation of the underlying investments of the fund. These investments cannot be sold without the approval of the general partners of the investee funds. We estimate that the underlying investments of the funds will be liquidated over a period of one to ten years.

(b) Consists of investee funds invested in long and short positions of stressed and distressed fixed income-oriented securities with the goal of producing attractive risk-adjusted returns. The investments can be redeemed quarterly with 45 days notice. However, the general partners may impose quarterly redemption limits that may delay receipt of requested redemptions.

***Derivatives***. Exchange-traded derivatives are valued using quoted prices and, therefore, are classified as Level 1 inst derivatives are exchange-traded, so the majority of our derivative positions are valued using internally developed mo observable market inputs, such as interest rate curves, yield curves, the LIBOR discount rates and curves, index pric volatility surfaces. These derivative contracts, which are classified as Level 2 instruments, include interest rate swap credit default swaps. In addition, we have a few customized derivative instruments and risk participations that are cla derivative positions are valued using internally developed models. Inputs to the models consist of available market d well as our assumptions, such as loss probabilities and proxy prices.

Market convention implies a credit rating of AA equivalent in the pricing of derivative contracts, which assumes creditworthiness. To reflect the actual exposure on our derivative contracts related to both counterparty and our own adjustment in the form of a default reserve. The credit component is valued on a counterparty-by-counterparty basis considers master netting and collateral agreements. The default reserve is considered to be a Level 3 input.

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***Other assets and liabilities.*** The value of our repurchase and reverse repurchase agreements, trade date receivables a the valuation of the underlying securities. The underlying securities may include equity securities, which are valued market for identical securities, resulting in a Level 1 classification. If quoted prices for identical securities are not av pricing models or quoted prices of similar securities, resulting in a Level 2 classification. Inputs include spreads, cre rate-driven products. Inputs include actual trade data for comparable assets, and bids and offers for the credit-driven corporate bonds and mortgage-backed securities, while interest rate-driven securities include government bonds, U.S by the U.S. government.

**Assets and Liabilities Measured at Fair Value on a Recurring Basis**

Certain assets and liabilities are measured at fair value on a recurring basis in accordance with GAAP. These assets a regular basis. The following tables present our assets and liabilities measured at fair value on a recurring basis at Jun

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| **June 30, 2010** *in millions* | **Level 1** | **Level 2** | **Level** |
|---|---|---|---|
| **ASSETS MEASURED ON A RECURRING BASIS** | | | |
| Short term investments: | | | |
| Securities purchased under resale agreements | | $ 416 | |
| Trading account assets: | | | |
| U.S. Treasury, agencies and corporations | | 7 | |
| Other mortgage-backed securities | | | $ |
| Other securities | $ 59 | 910 | 2 |
| Total trading account securities | 59 | 917 | 2 |
| Commercial loans | | 2 | |
| Total trading account assets | 59 | 919 | 3 |
| Securities available for sale: | | | |
| U.S. Treasury, agencies and corporations | | 8 | |
| States and political subdivisions | | 78 | |
| Collateralized mortgage obligations | | 18,290 | |
| Other mortgage-backed securities | | 1,283 | |

**Guarantees**

As part of its reorganization in 2001, the Company has fully and unconditionally guaranteed payment of all of the i
No other subsidiary of the Company guarantees these securities.

IR-New Jersey has unconditionally guaranteed payment of the principal, premium, if any, and interest on the C
aggregate principal amount of $300 million. The guarantee is unsecured and provided on an unsubordinated b
payment with all of the existing and future unsecured and unsubordinated debt of IR-New Jersey.

**Critical Accounting Policies**

The notes to the financial statements include a summary of significant accounting policies and methods used in
statements and the following summarizes what the Company believes are the critical accounting policies and metho

- Allowance for doubtful accounts - The Company has provided an allowance for doubtful accounts receivable us
knowledge of its end markets, customer base and products.

In the first quarter of 2006, the Company changed its estimate of the allowance for doubtful accounts in light of va
a significant change in its business portfolio and historical and expected write-off experience. In addition, the C
limits its bad debt exposure. As a result, the Company reduced its allowance by $20.5 million, or $17.1 million
diluted earnings per share by $0.05.

- Goodwill and other intangible assets - The Company has significant goodwill and other intangible assets on
valuation and classification of these assets and the assignment of amortization lives involves significant judgmen
intangibles under established accounting guidelines for impairment also requires significant use of judgment a
determination of fair market value. The Company’s goodwill and other intangible assets are tested and review
significant change in circumstances. The Company believes that its use of estimates and assumptions are rea

accounting principles. Changes in business conditions could potentially require future adjustments to these valuati

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· Long-lived assets - Long-lived assets are reviewed for impairment whenever events or changes in circumstances
may not be recoverable. Assets are grouped with other assets and liabilities at the lowest level for which ic
impairment in the carrying value of an asset would be recognized whenever anticipated future undiscounted cash
value. The impairment is measured as the amount by which the carrying value exceeds the fair value of the asse
cash flows.

· Loss contingencies - Liabilities are recorded for various contingencies arising in the normal course of busi
proceedings, environmental and asbestos matters and product liability, product warranty, worker's compensation
reserves in the financial statements related to these matters, which are developed using input derived from actu
experience data depending on the nature of the reserve, and in certain instances with consultation of legal co
engineers. Subject to the uncertainties inherent in estimating future costs for these types of liabilities, the C
reasonable and does not believe the final determination of the liabilities with respect to these matters would hav
results of operations, liquidity or cash flows of the Company for any year.

· Revenue Recognition - Revenue is generally recognized and earned when all of the following criteria are
arrangement exists; (b) price is fixed or determinable; (c) collectibility is reasonably assured; and (d) deliver
Delivery generally occurs when the title and the risks and rewards of ownership have substantially transferred
contracts or extended warranties is recognized on a straight-line basis over the life of the contract, unless anoth
incurred. The Company enters into agreements that contain multiple elements, such as equipment, installatio
arrangements, the Company recognizes revenue for delivered elements when the delivered item has stand
undelivered elements are known, customer acceptance has occurred, and there are only customary refund or return

· Income taxes - Deferred tax assets and liabilities are determined based on temporary differences between fin
liabilities, applying enacted tax rates expected to be in effect for the year in which the differences are expected to
benefits, such as net operating losses and non-U.S. tax credits, to the extent that realizing these benefits is conside
The Company regularly reviews the recoverability of its deferred tax assets considering its historic profitability,
reversals of existing temporary differences and the feasibility of its tax planning strategies. Where appropriate, the
respect to a future tax benefit.

The provision for income taxes involves a significant amount of management judgment regarding interpretation of
which the Company operates. Future changes in applicable laws, projected levels of taxable income, and tax planni
balances recorded by the Company. In addition, U.S. and non-U.S. tax authorities periodically review income ta
issues regarding its filing positions, timing and amount of income or deductions, and the allocation of income an
operates. A significant period of time may elapse between the filing of an income tax return and the ultimate resolu
with respect to that return. The Company believes that it has adequately provided for any reasonably foreseeable r
adjust its estimate if significant events so dictate. To the extent that the ultimate results differ from the original or
will be recorded in the provision for income taxes in the period that the matter is finally resolved.

· Employee benefit plans - The Company provides a range of benefits to eligible employees and retired emplo postemployment health-care benefits. Determining the cost associated with such benefits is dependent on vari rates, expected return on plan assets, compensation increases, employee mortality and turnover rates, and healt perform the required calculations to determine expense in accordance with U.S. generally accepted accounting actuarial assumptions and are generally accumulated and amortized into earnings over future periods. Effective D recognized in shareholders' equity on an annual basis, due to the adoption of SFAS 158. The Company reviews date and makes modifications to the assumptions based on current rates and trends, if appropriate. The discount r expected long-term rates of return on plan assets are determined as of the measurement date. The discount rate ref effectively settled. It is established and based primarily on the yields of high-quality fixed-income investments av life of the plans, a study based on the Citigroup Pension Liability index, and a review of the current yields reporte of compensation increase is dependent on expected future compensation levels. The expected long-term rates of be earned over the period until the benefits are paid, which should reflect the rates of return on present investme expected long-term rate of return on plan assets is based on what is achievable given the plan's investment polic return trends for the larger plans are reviewed over fifteen, ten and five-year periods. The actual rates of return fo periods have exceeded the expected rates of return used. The Company believes that the assumptions utilized i reasonable based on input from its actuaries, outside investment advisors, and information as to assumptions used

Changes in any of the assumptions can have an impact on the net periodic pension cost or postretirement cost. Esti cost of a 0.25% rate decrease in the three basic assumptions are as follows: the discount rate would increase expe compensation increase would decrease expense by approximately $4.7 million, and the estimated return on as approximately $6.9 million. A 0.25% rate decrease in the discount rate for postretirement benefits would increase n million and a 1.0% increase in the health care cost trend rate would increase the cost by approximately $6.3 million.

In 2006, the Company adopted SFAS 158, which requires the Company to record the funded status of its pension sheet effective December 31, 2006. Refer to Notes 8 and 9 in the Company's financial statements and the Liqui details of the impact of SFAS 158.

The preparation of all financial statements includes the use of estimates and assumptions that affect a number of statements. If actual amounts are ultimately different from previous estimates, the revisions are included in the actual amounts become known. Historically, the aggregate differences, if any, between the Company's estimates significant impact on the consolidated financial statements.

**New Accounting Standards**

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin No. Misstatements when Quantifying Misstatements in Current Year Financial Statements" (SAB 108). SAB 108 provi the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstate should quantify errors using both a balance sheet and an income statement approach and evaluate whether either a that, when all relevant quantitative and qualitative factors are considered, is material. SAB 108 is effective for the 31, 2006. SAB 108 did not have a material impact on the Company's financial statements.

In June 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an in which prescribes a recognition threshold and measurement process for recording in the financial statements uncert in a tax return. Additionally, FIN 48 provides guidance on the derecognition, classification, accounting in inte uncertain tax positions. The provisions of FIN 48 are effective for the Company for the fiscal year beginning on Ja the impact of FIN 48 on its consolidated financial statements.

In September 2006, the FASB issued Statement of Financial Accounting Standard No. 157, "Fair Value Measu framework for measuring fair value that is based on the assumptions market participants would use when pricing a hierarchy that prioritizes the information to develop those assumptions. Additionally, the standard expands the include disclosing the fair value measurements of assets or liabilities within each level of the fair value hierarchy. S on January 1, 2008. The Company is currently evaluating the impact on its financial statements of adopting SFAS 1

In February 2007, the FASB issued Statement of Financial Accounting Standard No. 159, "The Fair Value Optio (SFAS 159). SFAS 159 permits companies the option, at specified election dates, to measure financial assets and corresponding changes in fair value from period to period recognized in the income statement. Additionally, SFA requirements designed to facilitate comparisons between companies that choose different measurement attributes effective for the Company starting on January 1, 2008. The Company is currently evaluating the impact on its financ

Item 7A. **QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK**

The Company is exposed to fluctuations in the price of major raw materials used in the manufacturing process, cu From time to time, the Company enters into agreements to reduce its raw material, currency and interest rate non-performance, those agreements are made only through major financial institutions with significant experience i

The Company experiences currency exposures in the normal course of business. To mitigate the risk from currency
generally enter into forward currency exchange contracts for the purchase or sale of a currency to hedge this exposu

The Company evaluates its exposure to changes in currency exchange rates using a sensitivity analysis. The sensiti
loss in fair value based on a percentage increase or decrease in exchange rates against the U.S. dollar. Based
instruments in place at December 31, 2006, a hypothetical change in fair value of those financial instruments assu
the U.S. dollar would result in an unrealized loss of approximately $32.5 million, as compared with $16.0 million at
offset by changes in the fair value of underlying currency transactions.

The Company entered into two total return swaps (the Swaps) which are derivative instruments used to hedg
share-based compensation expense. The Swaps are benchmarked to the Company's Class A common share price an
market price of our Class A common shares. Assuming a 10% decrease in our share price at December 31, 2006
approximately $3.3 million. This amount would be offset by changes in the fair value of underlying share-based co

From time to time the Company participates in the debt markets through the issuance of commercial paper, which,
In managing its portfolio the Company issues and reissues commercial paper, thus exposing it to interest rate risk in

## Item 8. **FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

(a) The following consolidated financial statements and the report thereon of PricewaterhouseCoopers LLP dated M
of this Annual Report on Form 10-K.

Consolidated Financial Statements:
Report of independent registered public accounting firm
Consolidated balance sheets at December 31, 2006 and 2005
For the years ended December 31, 2006, 2005 and 2004:
Consolidated statements of income
Consolidated statements of shareholders' equity
Consolidated statements of cash flows
Notes to consolidated financial statements

Financial Statement Schedule:
Consolidated schedule for the years ended December 31, 2006, 2005 and 2004:
Schedule II — Valuation and Qualifying Accounts

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(b) The unaudited quarterly financial data for the two years ended December 31, is a

*In millions, except per share amounts*

| 2006 | Net revenues | Cost of goods sold | Operating income | Net earning |
|---|---|---|---|---|
| First quarter | $ 2,711.0 | $ 1,998.0 | $ 341.1 | $ |
| Second quarter | 3,041.9 | 2,215.4 | 416.5 | |
| Third quarter | 2,765.9 | 2,043.8 | 357.7 | |
| Fourth quarter | 2,890.5 | 2,167.0 | 325.5 | |
| Year 2006 | $ 11,409.3 | $ 8,424.2 | $ 1,440.8 | $ 1 |
| | | | | |
| 2005 | | | | |
| First quarter | $ 2,458.8 | $ 1,810.6 | $ 297.0 | $ |
| Second quarter | 2,759.5 | 2,019.1 | 379.1 | |
| Third quarter | 2,615.3 | 1,920.7 | 340.0 | |
| Fourth quarter | 2,713.3 | 1,993.7 | 345.7 | |
| Year 2005 | $ 10,546.9 | $ 7,744.1 | $ 1,361.8 | $ 1 |

*The amounts have been restated to reflect a two-for-one stock split that occurred in August 2005.

## Item 9. CHANGES IN AND DISAGREEMENTS WITH INDEPENDENT ACCOUNTANTS ON ACCOUNT

None.

## Item 9A CONTROLS AND PROCEDURES

***Disclosure Controls and Procedures***

The Company's management, including its Chief Executive Officer and Chief Financial Officer, have conducted a controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange A as of the end of the period covered by this Annual Report on Form 10-K. Based on that evaluation, the Chief E concluded as of December 31, 2006, that the disclosure controls and procedures are effective in ensuring that all m Annual Report on Form 10-K has been recorded, processed, summarized and reported when required and the infor appropriate, to allow timely decisions regarding required disclosure.

***Management's Report on Internal Control Over Financial Reporting***

The Company's management is responsible for establishing and maintaining adequate internal control over fina Exchange Act Rules 13a-15(f) and 15d-15(f). Internal control over financial reporting is a process designed to reliability of financial reporting and the preparation of financial statements for external purposes in accordance with

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in con the policies and procedures may deteriorate.

Management has assessed the effectiveness of internal control over financial reporting as of December 31, 2006
utilized the criteria set forth by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission
Management concluded that based on its assessment, the Company's internal control over financial reporti
Management's assessment of the effectiveness of internal control over financial reporting as of December 31, 2006
LLP, an independent registered public accounting firm, as stated in their report.

***Changes in Internal Control Over Financial Reporting***

There has been no change in the Company's internal controls over financial reporting during the quarter ended Dece
is reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. **OTHER INFORMATION**

None.

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## PART III

The information called for by Part III (Items 10, 11, 12, and 13) of Form 10-K will be included in the Company's Pr
General Meeting of Shareholders, which the Company intends to file within 120 days after the close of its fiscal
incorporated by reference to such Proxy Statement, except that the information as to the Company's executive offic
on Form 10-K, is incorporated by reference into Items 10 and 12, respectively, of this Report.

Item 14. **PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The information required by this item is incorporated herein by reference to the information contained under the c
Proxy Statement.

In early 2005, our registered public accounting firm, PricewaterhouseCoopers LLP (PwC), informed the Securities
Company Accounting Oversight Board and our Audit Committee that certain non-audit work that PwC previous
questions regarding PwC's independence with respect to its performance of audit services for us.

During the fiscal years 2004, 2003, 2002 and 2001, certain PwC affiliates, in connection with the preparation of
authorities with respect to individual employee tax liabilities. As a result, PwC's non-U.S. affiliates had tempora
funds. The fees we paid to PwC's non-U.S. affiliates in China and Taiwan for the preparation of these tax returns,
$433, $14,765, $24,849 and $18,767 for the years 2004, 2003, 2002 and 2001, respectively. These services were dis

Our Audit Committee has reviewed the facts surrounding these services provided by PwC. PwC has informed the
the performance of the tax services described above has impaired PwC's independence. In light of the de minimis
actions performed and the fact that the services have been discontinued, neither our Audit Committee nor PwC belie
the performance of these services.

**PART IV**

Item 15. **EXHIBITS AND FINANCIAL STATEMENTS SCHEDULE**

(a) 1. and 2. Financial statements and financial statement schedule

See Item 8.

3. Exhibits

The exhibits listed on the accompanying index to exhibits are filed as part of this Annual Rep

**INGERSOLL-RAND COMPANY LIMITED**
**INDEX TO EXHIBITS**
**(Item 15(a))**

**Description**

2 Agreement and Plan of Merger, dated as of October 31, 2001, among Ingersoll-Rand Company Limited, Ingersol
Incorporated by reference to Amendment No. 1 to Form S-4. Registration Statement No, 333-71642, filed October

2.1 Stock and Asset Purchase Agreement, dated as of October 16, 2002, between Ingersoll-Rand Company L
subsidiaries and The Timken Company, on behalf of itself and certain of its subsidiaries. Incorporated by referen

2.2 Amendment to the Stock and Asset Purchase Agreement, dated as of February 18, 2003, amending the Stock
2002, between Ingersoll-Rand Company Limited, on behalf of itself and certain of its subsidiaries and The Timk
its subsidiaries. Incorporated by reference to Form Schedule 13D, filed March 5, 2003 by Ingersoll-Rand Compa

2.3 Equity Purchase Agreement between FRC Acquisition LLC, on behalf of itself and the other buyers named ther
behalf of itself and the other sellers named therein, dated August 25, 2004, in connection with the divestiture o
Form 8-K dated August 25, 2004.

2.4 Pricing Agreement, dated as of May 24, 2005 among Ingersoll-Rand Company Limited, Banc of America Secur
Ingersoll-Rand Company. Incorporated by reference to Form 8-K for Ingersoll-Rand Company Limited, dated M

2.5 Asset and Stock Purchase Agreement, dated as of February 27, 2007, among Ingersoll-Rand Company limited, o
therein, and AB Volvo (publ), on behalf of itself and the other buyers named therein. Incorporated by reference t
Limited dated February 27, 2007, filed February 28, 2007.

3.1 Memorandum of Association of Ingersoll-Rand Company Limited. Incorporated by reference to Amendment No
333-71642, filed October 30, 2001.

3.2 Amended and Restated Bye-Laws of Ingersoll-Rand Company Limited, dated June 1, 2005. Incorporated by
June 30, 2005, of Ingersoll-Rand Company Limited, filed August 5, 2005.

4.1 Certificate of Designation, Preferences and Rights of Series A Preference Shares of Ingersoll-Rand Com
Amendment No. 1 to Form S-4 Registration Statement No. 333-71642, filed October 30, 2001.

4.2 Rights Agreement between Ingersoll-Rand Company Limited and The Bank of New York, as Rights Agent. Inco
Form S-4 Registration Statement No. 333-71642, filed October 30, 2001.

4.3 Voting Agreement between Ingersoll-Rand Company Limited and Ingersoll-Rand Company. Incorporated by
Registration Statement No. 333-71642, filed October 30, 2001.

4.4 Indenture dated as of August 1, 1986, between Ingersoll-Rand Company and The Bank of New York, as Truste
supplemental indentures. Incorporated by reference to Ingersoll-Rand Company's Form S-3 Registration Stateme
to Form S-3 Registration Statement No. 333-50902 as filed November 29, 2000.

4.5 Fourth Supplemental Indenture, dated as of December 31, 2001, among Ingersoll-Rand Company Limited, Ing
York, as trustee. Incorporated by reference to Form 10-K of Ingersoll-Rand Company Limited for the year ended

4.6 Credit Agreement dated as of August 12, 2005, among Ingersoll-Rand Company and Ingersoll-Rand Company
USA, Inc., as Syndication Agent, and Bank of America, N.A., Deutsche Bank Securities Inc., The Bank of To
UBS Securities LLC, as Documentation Agents, and JPMorgan Chase Bank, N.A., as Administrative Agent, a
Global Markets Inc., as Lead Arrangers and Bookrunners. Incorporated by reference to Form 10-K of Ingerso
December 31, 2006, filed March 1, 2006.

4.7 Credit Agreement, dated as of June 25, 2004, among Ingersoll-Rand Company and Ingersoll-Rand Company Li
Chase Bank, as Administrative Agent, Citibank N.A., and Deutsche Bank Securities Inc., as Co-Syndication Ag
as Documentation Agent, and J.P. Morgan Securities Inc., as Lead Arranger and Bookrunner. Incorporated b
Company Limited for the year ended December 31, 2004, filed March 16, 2005.

4.8 Ingersoll-Rand Company Limited and its subsidiaries are parties to several long-term debt instruments under whi
authorized does not exceed 10% of the total assets of Ingersoll-Rand Company Limited and its subsidiaries on a c
4(iii) of Item 601(b) of Regulation S-K, Ingersoll-Rand Company Limited agrees to furnish a copy of such instru
Commission upon request.

4.9 Indenture dated as of May 24, 2005 among Ingersoll-Rand Company Limited, Ingersoll-Rand Company and We
by reference to Form 8-K for Ingersoll-Rand Company Limited, dated May 24, 2005, filed May 27, 2005.

10.1 Management Incentive Unit Plan of Ingersoll-Rand Company. Amendment to the Management Incentive Unit
to the Management Incentive Unit Plan, effective January 1, 1987. Amendment to the Management Incentive U
by reference to Form 10-K of Ingersoll-Rand Company for the year ended December 31, 1993, filed March 30,

10.2 Reorganization Amendment to Management Incentive Unit Plan, dated December 31, 2001. Incorporated b
Company Limited for the year ended December 31, 2001, filed March 13, 2002.

10.3 Amended and Restated Director Deferred Compensation and Stock Award Plan. Incorporated by reference to F
year ended December 31, 2000, filed March 20, 2001.

10.4 First Amendment to Director Deferred Compensation and Stock Award Plan. Incorporated by reference to Fo
for the year ended December 31, 2001, filed March 13, 2002.

10.5 Second Amendment to Director Deferred Compensation and Stock Award Plan. Incorporated by referenc
Limited for the year ended December 31, 2003, filed February 27, 2004.

10.6 Third Amendment to Director Deferred Compensation and Stock Award Plan, dated December 31, 2004
Ingersoll-Rand Company Limited, dated December 31, 2004, filed January 6, 2005.

10.7 Fourth Amendment to Director Deferred Compensation and Stock Award Plan, dated March 10, 2005.
Ingersoll-Rand Company Limited for the year ended December 31, 2004, filed March 16, 2005.

10.8 Director Deferred Compensation and Stock Award Plan II, dated December 31, 2004. Incorporated by refere
Limited, dated December 31, 2004, filed January 6, 2005.

10.9 First Amendment to Director Deferred Compensation and Stock Award Plan II, dated March 10, 2005.
Ingersoll-Rand Company Limited for the year ended December 31, 2004, filed March 16, 2005.

10.10 Description of Annual Incentive Arrangements for Chairman, President, Sector Presidents and other Staff C
Incorporated by reference to Form 10-K of Ingersoll-Rand Company Limited for the year ended December 31

10.11 Description of Performance Share Program for Chairman, President and Chief Executive Officer and the o
Limited. Incorporated by reference to Form 10-K of Ingersoll-Rand Company Limited for the year ended Dece

10.12 Form of Change in Control Agreement with Tier 1 Officers of Ingersoll-Rand Company Limited, dated as of D
to Exhibit 99.1 in Form 8-K of Ingersoll-Rand Company Limited, dated November 30, 2006, filed December 4

10.13 Form of Change in Control Agreement with Tier 2 Officers of Ingersoll-Rand Company Limited, dated as of
to Exhibit 99.2 in Form 8-K of Ingersoll-Rand Company Limited, dated November 30, 2006, filed December 4

10.14 Executive Supplementary Retirement Agreement for selected executive officers of Ingersoll- Rand Compan
Ingersoll-Rand Company for the year ended December 31, 1993, filed March 30, 1994.

10.15 Executive Supplementary Retirement Agreement for selected executive officers of Ingersoll-Rand Company
the year ended December 31, 1996, filed March 26, 1997.

10.16 Forms of insurance and related letter agreements with certain executive officers of Ingersoll-Rand Compan
Ingersoll-Rand Company for the year ended December 31, 1993, filed March 30, 1994.

10.17 Amended and Restated Supplemental Pension Plan, dated January 1, 2003. Incorporated by reference to Form
the year ended December 31, 2002, filed March 5, 2003.

10.18 First Amendment to the Amended and Restated Supplemental Pension Plan, dated January 1, 2003. I
Ingersoll-Rand Company Limited for the year ended December 31, 2003, filed February 27, 2004.

10.19 Amended and Restated Supplemental Employee Savings Plan, dated January 1, 2003. Incorporated by referer
Limited for the year ended December 31, 2002, filed March 5, 2003.

10.20 First Amendment to the Amended and Restated Supplemental Employee Savings Plan, dated January 1, 2003.
Ingersoll-Rand Company Limited for the year ended December 31, 2003, filed February 27, 2004.

10.21 Incentive Stock Plan of 1995. Incorporated by reference to the Notice of 1995 Annual Meeting of Shareholder
See Appendix A of the Proxy Statement dated March 15, 1995.

10.22 Reorganization Amendment to Incentive Stock Plan of 1995, dated December 21, 2001. Incorporated by
Company Limited for the year ended December 31, 2001, filed March 13, 2002.

10.23 Senior Executive Performance Plan. Incorporated by reference to the Notice of 2000 Annual Meetin
Ingersoll-Rand Company, dated March 7, 2000. See Appendix A of the Proxy Statement, dated March 7, 2000

10.24 Amended and Restated Elected Officers Supplemental Plan, dated December 31, 2004. Incorporated by referen
Limited for the year ended December 31, 2004, filed March 16, 2005.

10.25 Amendment, dated February 1, 2006, to Amended and Restated Elected Officers Supplemental Plan, dated De
Form 10-K of Ingersoll-Rand Company Limited for the year ended December 31, 2006, filed March 1, 2006.

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10.26 Elected Officers Supplemental Plan II, dated February 1, 2006. Incorporated by reference to Form 10-K of Ing
ended December 31, 2006, filed March 1, 2006.

10.27 Amended and Restated Executive Deferred Compensation Plan. Incorporated by reference to Form 10-K of
December 31, 2000, filed March 20, 2001.

10.28 First Amendment to Executive Deferred Compensation Plan, dated December 31, 2001. Incorporated by
Company Limited for the year ended December 31, 2001, filed March 13, 2002.

10.29 Second Amendment to Executive Deferred Compensation Plan, dated February 24, 2004. Incorporated b
Company Limited for the year ended December 31, 2003, filed February 27, 2004.

10.30 Third Amendment to Executive Deferred Compensation Plan, dated December 31, 2004. Incorporated l
Company Limited dated December 31, 2004, filed January 6, 2005.

10.31 Fourth Amendment to Executive Deferred Compensation Plan, dated March 10, 2005. Incorporated by referer
Limited for the year ended December 31, 2004, filed March 16, 2005.

10.32 Executive Deferred Compensation Plan II, dated December 31, 2004. Incorporated by reference to Form 8-
December 31, 2004, filed January 6, 2005.

10.33 First Amendment to Executive Deferred Compensation Plan II, dated March 10, 2005. Incorporated by referer
Limited for the year ended December 31, 2004, filed March 16, 2005.

10.34 Amended and Restated Incentive Stock Plan of 1998. Incorporated by reference to Ingersoll-Rand Compan
filed December 1, 2005.

10.35 Amendment to the Ingersoll-Rand Company Limited Amended and Restated Incentive Stock Plan of 199
reference to Form 8-K of Ingersoll-Rand Company Limited, dated December 7, 2005, filed December 9, 2005

10.36 Composite Employment Agreement with Chief Executive Officer. Incorporated by reference to Form 10-K o
December 31, 1999, filed March 30, 2000.

10.37 Employment Agreement with Timothy McLevish, Senior Vice President and Chief Financial Officer.
Ingersoll-Rand Company Limited for the year ended December 31, 2002, filed March 5, 2003.

10.38 Employment Agreement with Michael Lamach, Senior Vice President. Incorporated by reference to Form 10-I
year ended December 31, 2003, filed February 27, 2004.

10.39 Addendum, dated June 3, 2005, to Employment Agreement with Timothy R. McLevish. Incorporated by refer
Limited, dated June 1, 2005, filed June 6, 2005.

10.40 Employment Agreement with James R. Bolch, Senior Vice President. Incorporated by reference to Form 10-
year ended December 31, 2006, filed March 1, 2006.

10.41 Addendum, dated December 8, 2005, to Employment Agreement with James R. Bolch. Incorporated by refere
Limited for the year ended December 31, 2006, filed March 1, 2006.

10.42 Amended and Restated Estate Enhancement Program, dated June 1, 1998, and the related form agreements
Ingersoll-Rand Company Limited for the quarter ended March 31, 2006, filed May 5, 2006.

10.43 First Amendment to the Amended and Restated Estate Enhancement Program, dated December 31, 2001
Ingersoll-Rand Company Limited for the quarter ended March 31, 2006, filed May 5, 2006.

10.44 Employment Agreement with William Gauld, Senior Vice President, dated September 7,

10.45 Employment Agreement with Marcia J. Avedon, Senior Vice President, dated January 8,

12 Computations of Ratios of Earnings to Fixed Charges. Filed herewith.

14 Ingersoll-Rand Company Limited Code of Ethics. Incorporated by reference to Form 10-K of Ingersoll-Rand C
31, 2006, filed March 1, 2006.

21 List of Subsidiaries of Ingersoll-Rand Company Limited. Filed herewit

23 Consent of Independent Registered Public Accounting Firm. Filed herew

31.1 Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) or Rule 15d-14(a), as adopted pursuant
2002. Filed herewith.

31.2 Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) or Rule 15d-14(a), as adopted pursuant to S
Filed herewith.

32 Certifications of Chief Executive Officer and Chief Financial Officer Pursuant to Rule 13a-14(b) or Rule 15d-1
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. Filed herewith.

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## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly c
the undersigned, thereunto duly authorized.

**INGERSOLL RAND COMPANY LIMITED**
(Registrant)

By: /S/ Herbert L. Henkel

(Herbert L. Henkel)
Chief Executive Officer
Date: March 1, 2007

Pursuant to the requirement of the Securities Exchange Act of 1934, this report has been signed by the following per
capacities and on the dates indicated.

| Signature | Title |
|---|---|
| /S/ Herbert L. Henkel<br>(Herbert L. Henkel) | Chairman, President, Chief Executive Officer and Director (Principal Executive Officer) |
| /S/ Timothy R. McLevish<br>(Timothy R. McLevish) | Senior Vice President and Chief Financial Officer (Principal Financial Officer) |
| /S/ Richard W. Randall<br>(Richard W. Randall) | Vice President and Controller (Principal Accounting Officer) |
| /S/ Ann C. Berzin<br>(Ann C. Berzin) | Director |
| /S/ Peter C. Godsoe<br>(Peter C. Godsoe) | Director |
| /S/ Constance Horner<br>(Constance Horner) | Director |
| /S/ H. William Lichtenberger<br>(H. William Lichtenberger) | Director |

| | |
|---|---|
| /S/ Theodore E. Martin<br>(Theodore E. Martin) | Director |
| /S/ Patricia Nachtigal<br>(Patricia Nachtigal) | Director |
| /S/ Orin R. Smith<br>(Orin R. Smith) | Director |
| /S/ Richard J. Swift<br>(Richard J. Swift) | Director |
| /S/ Tony L. White<br>(Tony L. White) | Director |

**INGERSOLL-RAND COMPANY LIMITED**
**Index to Consolidated Financial Statements**



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**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders of Ingersoll-Rand Company Limited:

We have completed integrated audits of Ingersoll-Rand Company Limited's (successor company to Ingersoll-Ran and of its internal control over financial reporting as of December 31, 2006, in accordance with the standards of the (United States). Our opinions, based on our audits, are presented below.

Consolidated financial statements and financial statement schedule

In our opinion, the consolidated financial statements listed in the index appearing under Item 15(a)(1) present fairly of Ingersoll-Rand Company Limited and its subsidiaries at December 31, 2006 and 2005, and the results of their c three years in the period ended December 31, 2006 in conformity with accounting principles generally accepted in our opinion, the financial statement schedule listed in the index appearing under Item 15(a)(2), presents fairly, in a therein when read in conjunction with the related consolidated financial statements. These financial statemen responsibility of the Company's management. Our responsibility is to express an opinion on these financial statem our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Those standards require that we plan and perform the audit to obtain reasonable assurance about whether t misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amoun assessing the accounting principles used and significant estimates made by management, and evaluating the overal that our audits provide a reasonable basis for our opinion.

As discussed in Note 1 to the consolidated financial statements, the Company adopted Statement of Financial Ac *Payment*, as of January 1, 2006, using the modified prospective method.

As discussed in Note 1 to the consolidated financial statements, the Company adopted Statement of Financia *Accounting for Defined Benefit Pension and Other Postretirement Plans - an Amendment to FASB Statements No.* 2006.

Internal control over financial reporting

Also, in our opinion, management's assessment, included in Management's Report on Internal Control Over Financi Company maintained effective internal control over financial reporting as of December 31, 2006 based on criteri *Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), is fairly criteria. Furthermore, in our opinion, the Company maintained, in all material respects, effective internal control 2006, based on criteria established in *Internal Control - Integrated Framework* issued by the COSO. The Company effective internal control over financial reporting and for its assessment of the effectiveness of internal control ov express opinions on management's assessment and on the effectiveness of the Company's internal control ov conducted our audit of internal control over financial reporting in accordance with the standards of the Public Co States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether eff was maintained in all material respects. An audit of internal control over financial reporting includes obtaining an u reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness o procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for

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A company's internal control over financial reporting is a process designed to provide reasonable assurance regardi
preparation of financial statements for external purposes in accordance with generally accepted accounting principl
reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reason
transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are r
financial statements in accordance with generally accepted accounting principles, and that receipts and expendi
accordance with authorizations of management and directors of the company; and (iii) provide reasonable assuranc
unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financia

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstater
effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in co
the policies or procedures may deteriorate.

PricewaterhouseCoopers LLP
Florham Park, New Jersey
March 1, 2007

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**Ingersoll-Rand Company Limited**
**Consolidated Statements of Income**
*In millions, except per share amounts*

| For the years ended December 31, | | 2006 | |
|---|---|---|---|
| Net revenues | $ | 11,409.3 | $ |
| Cost of goods sold | | 8,424.2 | |
| Selling and administrative expenses | | 1,544.3 | |
| Operating income | | 1,440.8 | |
| Interest expense | | (131.8) | |
| Other income, net | | 5.9 | |
| Minority interests | | (14.9) | |
| Earnings before income taxes | | 1,300.0 | |
| Provision for income taxes | | 231.7 | |
| Earnings from continuing operations | | 1,068.3 | |
| Discontinued operations, net of tax | | (35.8) | |
| Net earnings | $ | 1,032.5 | $ |
| Basic earnings per common share: | | | |
| Earnings from continuing operations | $ | 3.34 | $ |
| Discontinued operations, net of tax | | (0.11) | |
| Net earnings | $ | 3.23 | $ |
| Diluted earnings per common share: | | | |
| Earnings from continuing operations | $ | 3.31 | $ |
| Discontinued operations, net of tax | | (0.11) | |
| Net earnings | $ | 3.20 | $ |

*See accompanying Notes to Consolidated Financial Statements.*

**Ingersoll-Rand Company Limited**
**Consolidated Balance Sheets**
*In millions*

| | |
|---|---|
| December 31, | |
| **ASSETS** | |
| **Current assets:** | |
| Cash and cash equivalents | $ |
| Marketable securities | |
| Accounts and notes receivable, less allowance of $17.8 in 2006 and $47.6 in 2005 | |
| Inventories | |
| Prepaid expenses and deferred income taxes | |
| Total current assets | |
| | |
| Property, plant and equipment, net | |
| Goodwill | |
| Intangible assets, net | |
| Other assets | |
| Total assets | $ |
| | |
| **LIABILITIES AND EQUITY** | |
| **Current liabilities:** | |
| Accounts payable | $ |
| Accrued compensation and benefits | |
| Accrued expenses and other current liabilities | |
| Loans payable and current maturities of long-term debt | |
| Total current liabilities | |
| | |
| Long-term debt | |
| Postemployment and other benefit liabilities | |
| Other noncurrent liabilities | |
| Total liabilities | |
| Commitments and contingencies (Note 15) | |
| | |
| **Shareholders' equity:** | |
| Class A common shares, $1 par value (364,462,276 and 360,740,316 shares issued at December 31, 2006 and 2005, respectively, and net of 57,699,279 and 30,032,378 shares owned by subsidiary at December 31, 2006 and 2005, respectively) | |
| Retained earnings | |
| Accumulated other comprehensive income (loss) | |
| Total shareholders' equity | |
| Total liabilities and shareholders' equity | $ |

*See accompanying Notes to Consolidated Financial Statements.*

**Ingersoll-Rand Company Limited**
**Consolidated Statements of Shareholders' Equity**
*In millions, except per share amounts*

| | Total shareholders' equity | Common stock Amount | Common stock Shares | Capital in excess of par value |
|---|---|---|---|---|
| Balance at December 31, 2003 | $ 4,493.3 | $ 174.5 | 174.5 | $ 610.6 |
| Net earnings | 1,218.7 | | | |
| Currency translation | 168.7 | | | |
| Change in fair value of derivatives qualifying as cash flow hedges, net of tax of $0.4 | 3.1 | | | |
| Minimum pension liability adjustment, net of tax of $103.7 | 161.5 | | | |
| Total comprehensive income | | | | |
| Shares issued under incentive stock plans | 213.5 | 3.9 | 3.9 | 209.6 |
| Repurchase of common shares by subsidiary | (355.9) | (5.3) | (5.3) | (350.6) |
| Change in fiscal year end of subsidiary, net of tax of $7.3 | (16.5) | | | |
| Cash dividends, declared and paid ($0.44 per share) | (152.6) | | | |
| Balance at December 31, 2004 | 5,733.8 | 173.1 | 173.1 | 469.6 |
| Net earnings | 1,054.2 | | | |
| Currency translation | (267.7) | | | |
| Change in fair value of marketable securities and derivatives qualifying as cash flow hedges, net of tax of $0.3 | 5.7 | | | |
| Minimum pension liability adjustment, net of tax of $60.5 | 71.6 | | | |
| Total comprehensive income | | | | |
| Shares issued under incentive stock plans | 120.0 | 2.3 | 2.3 | 117.7 |
| Repurchase of common shares by subsidiary | (763.6) | (19.4) | (19.4) | (587.3) |
| Stock split | - | 174.7 | 174.7 | |
| Cash dividends, declared and paid ($0.57 per share) | (192.0) | | | |
| Balance at December 31, 2005 | 5,762.0 | 330.7 | 330.7 | - |
| Net earnings | 1,032.5 | | | |
| Currency translation | 258.8 | | | |
| Change in fair value of marketable securities and derivatives qualifying as cash flow hedges, net of tax of $0.8 | (7.3) | | | |
| Minimum pension liability adjustment, net of tax of $3.2 | (9.2) | | | |
| Total comprehensive income | | | | |
| Adoption of FASB Statement No. 158, net of tax of $268.2 | (472.8) | | | |
| Shares issued under incentive stock plans | 111.1 | 3.8 | 3.8 | 107.3 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Repurchase of common shares by subsidiary | | (1,096.3) | | (27.7) | (27.7) | | (150.9) |
| Share-based compensation | | 43.6 | | | | | 43.6 |
| Cash dividends, declared and paid ($0.68 per share) | | (217.6) | | | | | |
| Balance at December 31, 2006 | $ | 5,404.8 | $ | 306.8 | 306.8 | $ | - $ |

*See accompanying Notes to Consolidated Financial Statements.*

**Ingersoll-Rand Company Limited**
**Consolidated Statements of Cash Flows**
*In millions*

| For the years ended December 31, | 2006 | 2005 | 2004 |
|---|---|---|---|
| **Cash flows from operating activities:** | | | |
| Net earnings | $ 1,032.5 | $ 1,054.2 | $ 1,218.7 |
| Loss (income) from discontinued operations, net of tax | 35.8 | (1.1) | (388.9) |
| Adjustments to arrive at net cash provided by operating activities: | | | |
| Depreciation and amortization | 190.7 | 195.7 | 174.4 |
| Gain on sale of businesses | - | (1.5) | - |
| Gain on sale of property, plant and equipment | (5.7) | (2.4) | (8.9) |
| Minority interests, net of dividends | 9.2 | (1.3) | 6.3 |
| Equity earnings, net of dividends | 0.1 | 0.4 | (8.6) |
| Stock settled share based compensation | 23.4 | - | - |
| Deferred income taxes | (59.3) | 64.0 | (59.2) |
| Other items | (31.1) | (42.0) | (16.6) |
| Changes in other assets and liabilities | | | |
| (Increase) decrease in: | | | |
| Accounts and notes receivable | (204.7) | (128.5) | (70.1) |
| Inventories | (116.1) | 0.6 | (174.8) |
| Other current and noncurrent assets | (91.7) | (189.1) | (139.2) |
| Increase (decrease) in: | | | |
| Accounts and notes payable | 169.2 | 87.8 | 91.5 |
| Other current and noncurrent liabilities | 56.5 | (163.6) | 145.6 |
| Net cash (used in) provided by continuing operating activities | 1,008.8 | 873.2 | 770.2 |
| Net cash (used in) provided by discontinued operating activities | (36.6) | (34.1) | 27.3 |
| **Cash flows from investing activities:** | | | |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Capital expenditures | (212.3) | (141.8) | (125.6) | | | | | | | |
| Proceeds from sale of property, plant and equipment | 16.4 | 19.0 | 50.4 | | | | | | | |
| Acquisitions, net of cash acquired | (121.5) | (514.7) | (33.7) | | | | | | | |
| Proceeds from business dispositions | - | 11.4 | 1,413.2 | | | | | | | |
| Proceeds from sales and maturities of marketable securities | 155.8 | - | 0.3 | | | | | | | |
| Purchase of marketable securities | - | (153.2) | - | | | | | | | |
| Cash provided by equity companies, net | 0.4 | 7.6 | 7.6 | | | | | | | |
| Net cash (used in) provided by continuing investing activities | (161.2) | (771.7) | 1,312.2 | | | | | | | |
| Net cash (used in) provided by discontinued investing activities | - | - | (7.4) | | | | | | | |
| **Cash flows from financing activities:** | | | | | | | | | | |
| Increase (decrease) in short-term borrowings | 369.2 | (40.2) | (16.3) | | | | | | | |
| Proceeds from long-term debt | 4.0 | 301.7 | - | | | | | | | |
| Payments of long-term debt | (513.7) | (198.8) | (453.1) | | | | | | | |
| Net change in debt | (140.5) | 62.7 | (469.4) | | | | | | | |
| Redemption of preferred stock of subsidiaries | - | (73.6) | - | | | | | | | |
| Proceeds from exercise of stock options | 95.7 | 90.9 | 170.7 | | | | | | | |
| Dividends paid | (217.6) | (192.1) | (152.6) | | | | | | | |
| Repurchase of common shares by subsidiary | (1,096.3) | (763.6) | (355.9418 | | 3 | | 3.03 | | 1,034 | |
| | 8,092 | 53 | | 2.91 | | 9,183 | | 66 | | 3.07 |
| | 63,017 | 303 | | 1.94 | | 66,287 | | 348 | | 2.10 |
| | 14,655 | | | | | 13,604 | | | | |
| | 3,097 | | | | | 2,055 | | | | |
| | 4,141 | | | | | 4,091 | | | | |
| | 84,910 | | | | | 86,037 | | | | |
| | 10,843 | | | | | 10,961 | | | | |
| | 222 | | | | | 223 | | | | |

| | | | | | | |
|---|---|---|---|---|---|---|
| 11,065 | | | | 11,184 | | |
| $ 95,975 | | | | $ 97,221 | | |
| | | | 2.53 % | | | 2.30 % |
| | | 637 | 3.04 % | | 599 | 2.80 % |
| | | 7 | | | 7 | |
| | | $ 630 | | | $ 592 | |

(e) Yield is calculated on the basis of amortized cost.

(f) Rate calculation excludes basis adjustments related to fair value hedges.

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Figure 10 shows how the changes in yields or rates and average balances from the prior year affected net interest inc
contains additional discussion about changes in earning assets and funding sources.

**Figure 10. Components of Net Interest Income Changes from Continuing O**

| | From three months ended June 30, 2009 to three months ended June 30, 2010 | | | |
|---|---|---|---|---|
| *in millions* | **Average Volume** | **Yield/ Rate** | **Net Change** | **Av Vo** |
| **INTEREST INCOME** | | | | |
| Loans | **$ (170)** | **$ 28** | **$ (142)** | **$** |
| Loans held for sale | **(1)** | **(2)** | **(3)** | |
| Securities available for sale | **82** | **(17)** | **65** | |
| Trading account assets | **(2)** | **(1)** | **(3)** | |
| Short-term investments | **(1)** | | **(1)** | |
| Other investments | | | | |
| Total interest income (TE) | **(92)** | **8** | **(84)** | |
| **INTEREST EXPENSE** | | | | |
| NOW and money market deposit accounts | **2** | **(10)** | **(8)** | |
| Certificates of deposit ($100,000 or more) | **(34)** | **(13)** | **(47)** | |
| Other time deposits | **(30)** | **(24)** | **(54)** | |
| Deposits in foreign office | | **1** | **1** | |
| Total interest-bearing deposits | **(62)** | **(46)** | **(108)** | |
| Federal funds purchased and securities sold under repurchase agreements | | **1** | **1** | |
| Bank notes and other short-term borrowings | **(4)** | **4** | | |
| Long-term debt | **(22)** | **(3)** | **(25)** | |
| Total interest expense | **(88)** | **(44)** | **(132)** | |
| Net interest income (TE) | **$ (4)** | **$ 52** | **$ 48** | **$** |

The change in interest not due solely to volume or rate has been allocated in proportion to the absolute dollar amoun

**Noninterest income**

Our noninterest income was $492 million for the second quarter of 2010, compared to $706 million for the year-ago
noninterest income was $942 million, representing a decrease of $242 million, or 20%, from the first half of 2009.

As shown in Figure 11, the second quarter of 2009 included a $125 million net gain from the sale of collateralized m
related to the exchange of common shares for capital securities, and a $32 million gain from the sale of Key s claim
bankruptcy. Additionally, net gains on leased equipment during the second quarter of 2010 declined by $34 million
this decline in noninterest income were net gains of $25 million from loan sales, and net gains of $17 million from p
attributable to noncontrolling interests) in the second quarter of 2010, compared to net losses of $3 million and $6 m
an increase in investment banking and capital markets income of $17 million during the second quarter of 2010.

For the year-to-date period, the decrease in noninterest income was largely attributable to a reduction of net gains fro
repositioning of the portfolio in the second quarter of 2009, a reduction of net gains from leased equipment and lowe
contributing to the decline was a $9 million decrease in service charges on deposit accounts, and a $3 million decrea
The decreases were offset in part by a $132 million increase in net gains from principal investing, a $25 million incr

increase in income from investment banking and capital markets activities, and increases in income from electronic

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banking fees and insurance income. Additionally, Key recorded a $105 million gain from the sale of Visa Inc. shares
to the decrease in noninterest income from the first six months of 2009.

**Figure 11. Noninterest Income**

| | Three months ended June 30, | | Change | | Six months e 30 |
|---|---|---|---|---|---|
| *dollars in millions* | **2010** | **2009** | **Amount** | **Percent** | **2010** |
| Trust and investment services income | **$ 112** | $ 119 | $ (7) | (5.9) % | **$ 226** |
| Service charges on deposit accounts | **80** | 83 | (3) | (3.6) | **156** |
| Operating lease income | **43** | 59 | (16) | (27.1) | **90** |
| Letter of credit and loan fees | **42** | 44 | (2) | (4.5) | **82** |
| Corporate-owned life insurance income | **28** | 25 | 3 | 12.0 | **56** |
| Net securities gains (losses) | **(2)** | 125 | (127) | N/M | **1** |
| Electronic banking fees | **29** | 27 | 2 | 7.4 | **56** |
| Gains on leased equipment | **2** | 36 | (34) | (94.4) | **10** |
| Insurance income | **19** | 16 | 3 | 18.8 | **37** |
| Net gains (losses) from loan sales | **25** | (3) | 28 | N/M | **29** |
| Net gains (losses) from principal investing | **17** | (6) | 23 | N/M | **54** |
| Investment banking and capital markets income (loss) | **31** | 14 | 17 | 121.4 | **40** |
| Gain from sale/redemption of Visa Inc. shares | | | | | |
| Gain (loss) related to exchange of common shares for capital securities | | 95 | (95) | (100.0) | |
| Other income: | | | | | |
| Gain from sale of Key s claim associated with the Lehman Brothers bankruptcy | | 32 | (32) | (100.0) | |
| Credit card fees | **3** | 3 | | | **6** |
| Miscellaneous income | **63** | 37 | 26 | 70.3 | **99** |
| Total other income | **66** | 72 | (6) | (8.3) | **105** |
| Total noninterest income | **$ 492** | $ 706 | $ (214) | (30.3) % | **$ 942** |

The following discussion explains the composition of certain elements of our noninterest income and the factors that
***Trust and investment services income.*** Trust and investment services are our largest source of noninterest income. T
by these services are shown in Figure 12. The second quarter of 2010 decrease of $7 million, or 6%, is attributable to
and fees.

**Figure 12. Trust and Investment Services Income**

**Change**

| Three months ended June 30, | Six months 3 |
| --- | --- |