FIFTH THIRD BANCORP
Form 8-K
January 19, 2011

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 8-K

CURRENT REPORT

PURSUANT TO SECTION 13 OR 15(D) OF THE

SECURITIES EXCHANGE ACT OF 1934

Date of report (Date of earliest event reported): January 19, 2011

FIFTH THIRD BANCORP

(Exact Name of Registrant as Specified in Its Charter)

OHIO

(State or Other Jurisdiction of Incorporation)

001-33653	**31-0854434**
(Commission File Number)	**(IRS Employer Identification No.)**

Fifth Third Center

38 Fountain Square Plaza, Cincinnati, Ohio	**45263**
(Address of Principal Executive Offices)	**(Zip Code)**

(800) 972-3030

(Registrant s Telephone Number, Including Area Code)

Not Applicable

(Former Name or Former Address, if Changed Since Last Report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (*see* General Instruction A.2. below):

¨ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

¨ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

¨ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

¨ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 7.01 Regulation FD Disclosure

On January 19, 2011, Fifth Third Bancorp issued a press release regarding its common stock offering. A copy of this press release is furnished as Exhibit 99.1 to this Current Report on Form 8-K. The information in this press release shall not be deemed filed for purposes of Section 18 of the Securities Act of 1934, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933, except as shall be expressly set forth by specific reference.

Item 8.01 Other Events

Fifth Third Bancorp is filing the information contained in Item 8.01 in this Current Report on Form 8-K to incorporate into its securities filings certain financial information from its January 19, 2011 earnings release for the quarter and year ended December 31, 2010.

2011 Fourth Quarter Financial Information

On January 19, 2011 Fifth Third Bancorp reported full year 2010 net income of $753 million compared with net income of $737 million in 2009. 2010 net income available to common shareholders was $503 million or $0.63 per diluted share compared with 2009 net income of $511 million or $0.67 per diluted share. 2009 earnings benefited from a $1.1 billion after-tax gain on the processing business sale.

Fourth quarter 2010 net income was $333 million, compared with net income of $238 million in the third quarter and a net loss of $98 million in the fourth quarter of 2009. After preferred dividends, fourth quarter 2010 net income available to common shareholders was $270 million or $0.33 per diluted share, compared with third quarter net income of $175 million or $0.22 per diluted share, and a net loss of $160 million or $0.20 per diluted share in the fourth quarter of 2009.

Fourth quarter 2010 results included a $17 million charge related to the early extinguishment of $1.0 billion in FHLB borrowings and $21 million of investment portfolio securities gains. Third quarter 2010 net income included a pre-tax benefit, net of expenses, of $127 million from the settlement of litigation related to a bank-owned life insurance (BOLI) policy. Third quarter 2010 results also included the effect of actions taken to reduce credit risk. During the third quarter, $228 million of residential mortgage loans, largely nonperforming, were sold for $105 million, generating $123 million of additional net charge-offs. Additionally, $961 million of commercial loans were transferred to held-for-sale, a majority of which were nonperforming, generating $387 million of additional net charge-offs to mark the loans to estimated sales price. These actions resulted in total net charge-offs of $510 million and a reduction in Fifth Third s allowance for loan and lease losses of approximately $337 million. Fourth quarter 2009 results included the benefit of a $20 million pre-tax mark-to-market adjustment on warrants related to the processing business sale, recorded in other noninterest income, and a $22 million pre-tax litigation reserve accrual recorded in other noninterest expense for litigation associated with bank card association membership.

Earnings Highlights

	For the Three Months Ended					% Change	
	December 2010	September 2010	June 2010	March 2010	December 2009	Seq	Yr/Yr
Earnings ($ in millions)							
Net income (loss) attributable to Bancorp	$ 333	$ 238	$ 192	($ 10)	($ 98)	40%	NM
Net income (loss) available to common shareholders	$ 270	$ 175	$ 130	($ 72)	($ 160)	54%	NM
Common Share Data							
Earnings per share, basic	0.34	0.22	0.16	(0.09)	(0.20)	55%	NM
Earnings per share, diluted	0.33	0.22	0.16	(0.09)	(0.20)	50%	NM
Cash dividends per common share	0.01	0.01	0.01	0.01	0.01		
Financial Ratios							
Return on average assets	1.18%	0.84%	0.68%	(.04%)	(.35%)	40%	NM
Return on average common equity	10.4	6.8	5.2	(3.0)	(6.3)	53%	NM
Tier I capital	13.94	13.85	13.65	13.39	13.30	1%	5%
Tier I common equity	7.50	7.34	7.17	6.96	6.99	2%	7%
Net interest margin (a)	3.75	3.70	3.57	3.63	3.55	1%	6%
Efficiency (a)	62.6	56.2	62.1	62.5	63.1	11%	(1%)
Common shares outstanding (in thousands)	796,273	796,283	796,320	794,816	795,068		
Average common shares outstanding (in thousands):							
Basic	791,072	791,017	790,839	790,473	790,442		
Diluted	836,225	797,492	802,255	790,473	790,442	5%	6%

(a) Presented on a fully taxable equivalent basis
NM: Not Meaningful

Income Statement Highlights

	For the Three Months Ended					% Change	
	December 2010	September 2010	June 2010	March 2010	December 2009	Seq	Yr/Yr
Condensed Statements of Income ($ in millions)							
Net interest income (taxable equivalent)	$ 919	$ 916	$ 887	$ 901	$ 883		4%
Provision for loan and lease losses	166	457	325	590	776	(64%)	(79%)
Total noninterest income	656	827	620	627	651	(21%)	1%
Total noninterest expense	987	979	935	956	967	1%	2%
Income (loss) before income taxes (taxable equivalent)	422	307	247	(18)	(209)	38%	NM
Taxable equivalent adjustment	5	4	5	4	5	25%	
Applicable income taxes	83	65	50	(12)	(116)	28%	NM
Net Income (loss)	334	238	192	(10)	(98)	40%	NM
Less: Net Income (loss) attributable to noncontrolling interest	1						
Net income (loss) attributable to Bancorp	333	238	192	(10)	(98)	40%	NM
Dividends on preferred stock	63	63	62	62	62		
Net income (loss) available to common shareholders	270	175	130	(72)	(160)	54%	NM
Earnings per share, diluted	$ 0.33	$ 0.22	$ 0.16	($ 0.09)	($ 0.20)	50%	NM

NM: Not Meaningful

Net Interest Income

	For the Three Months Ended					% Change	
	December 2010	September 2010	June 2010	March 2010	December 2009	Seq	Yr/Yr
Interest Income ($ in millions)							
Total interest income (taxable equivalent)	$ 1,109	$ 1,130	$ 1,121	$ 1,147	$ 1,148	(2%)	(3%)
Total interest expense	190	214	234	246	265	(11%)	(28%)
Net interest income (taxable equivalent)	$ 919	$ 916	$ 887	$ 901	$ 883		4%
Average Yield							
Yield on interest-earning assets	4.52%	4.57%	4.51%	4.62%	4.61%	(1%)	(2%)
Yield on interest-bearing liabilities	1.04%	1.13%	1.23%	1.29%	1.39%	(8%)	(25%)
Net interest rate spread (taxable equivalent)	3.48%	3.44%	3.28%	3.33%	3.22%	1%	8%
Net interest margin (taxable equivalent)	3.75%	3.70%	3.57%	3.63%	3.55%	1%	6%
Average Balances ($ in millions)							
Loans and leases, including held for sale	$ 79,148	$ 78,854	$ 78,807	$ 80,136	$ 79,920		(1%)
Total securities and other short-term investments	18,066	19,309	20,891	20,559	18,869	(6%)	(4%)
Total interest-bearing liabilities	72,657	75,076	76,415	77,655	75,815	(3%)	(4%)
Bancorp shareholders equity	14,007	13,852	13,563	13,518	13,724	1%	2%

Net interest income of $919 million on a taxable equivalent basis increased $3 million from the third quarter of 2010. The net interest margin was 3.75 percent, an increase of 5 bps from 3.70 percent in the previous quarter. The increase in net interest income and net interest margin reflected ongoing CD repricing and deposit mix shift out of CDs, as well as higher average loan balances and continued deposit pricing discipline, particularly in savings rates. These positive effects were partially offset by the reduced interest income due to the refinancing of the FTPS, LLC loan, strong commercial loan originations to high quality credits with lower yields, and higher securities premium amortization expense due to increased prepayments as a result of the rate environment.

Compared with the fourth quarter of 2009, net interest income increased $36 million and the net interest margin increased 20 bps, largely the result of the mix shift from higher cost term deposits to lower cost deposit products throughout the year, which more than offset the effect of a $10 million, or 4 bps, reduction in purchase accounting accretion on acquired loans and lower loan balances.

Securities

Average securities and other short-term investments were $18.1 billion in the fourth quarter of 2010, compared with $19.3 billion in the previous quarter and $18.9 billion in the fourth quarter of 2009. The primary driver of the sequential decline was a $1.0 billion decrease in average short-term investments due to lower cash balances held at the Fed. During the quarter, we prepaid $1.0 billion in FHLB debt. Additionally, a portion of portfolio cash flows was reinvested in retail branch originated mortgages, generally with maturities of 20 years or less.

Loans

	For the Three Months Ended					% Change	
	December 2010	September 2010	June 2010	March 2010	December 2009	Seq	Yr/Yr
Average Portfolio Loans and Leases ($ in millions)							
Commercial:							
Commercial and industrial loans	$ 26,338	$ 26,344	$ 26,176	$ 26,294	$ 25,816		2%
Commercial mortgage	10,985	11,375	11,659	11,708	11,981	(3%)	(8%)
Commercial construction	2,171	2,885	3,160	3,700	4,024	(25%)	(46%)
Commercial leases	3,314	3,257	3,336	3,467	3,574	2%	(7%)
Subtotal - commercial loans and leases	42,808	43,861	44,331	45,169	45,395	(2%)	(6%)
Consumer:							
Residential mortgage loans	8,382	7,837	7,805	7,976	8,129	7%	3%
Home equity	11,655	11,897	12,102	12,338	12,291	(2%)	(5%)
Automobile loans	10,825	10,517	10,170	10,185	8,973	3%	21%
Credit card	1,844	1,838	1,859	1,940	1,982		(7%)
Other consumer loans and leases	722	667	706	773	831	8%	(13%)
Subtotal - consumer loans and leases	33,428	32,756	32,642	33,212	32,206	2%	4%
Total average loans and leases (excluding held for sale)	$ 76,236	$ 76,617	$ 76,973	$ 78,381	$ 77,601		(2%)
Average loans held for sale	2,912	2,237	1,834	1,756	2,319	30%	26%

Average portfolio loan and lease balances were flat sequentially and declined 2 percent from the fourth quarter of 2009. During the fourth quarter of 2010, FTPS, LLC refinanced its $1.25 billion loan related to the processing joint venture into a larger syndicated loan structure in connection with an acquisition. The impact of this refinancing reduced quarterly average portfolio loan and lease balances by $552 million. Period end loan and lease balances increased $1.5 billion, despite the effect of an $842 million reduction in the balances of our loans with FTPS, LLC.

Average commercial portfolio loan and lease balances declined 2 percent sequentially and 6 percent from the fourth quarter of 2009. Commercial and industrial (C&I) average loans were flat sequentially, with strong originations during the quarter offset by the impact of the FTPS, LLC loan refinancing and the transfer of loans to held-for-sale at the end of the third quarter 2010. Compared with the fourth quarter of 2009, C&I average loans increased 2 percent. Year-over-year comparisons were affected by the addition of $724 million in C&I balances that were consolidated on January 1, 2010 due to an accounting change in U.S. GAAP. Average commercial mortgage and commercial construction loan balances declined by a combined 8 percent sequentially and 18 percent from the same period the previous year, reflecting low customer demand and tighter underwriting standards as well as the transfer of loans to loans held-for-sale at the end of the third quarter 2010. Commercial line usage, on an end of period basis for the fourth quarter, remained stable at 32.7 percent of committed lines versus 32.4 percent in the third quarter of 2010 and 32.7 percent in the fourth quarter of 2009.

Commercial portfolio period end loan balances were up $522 million, or 1 percent, driven by growth in C&I balances, which increased $889 million, or 3 percent, despite the approximate $850 million effect of the refinancing of the FTPS, LLC loan. This increase was partially offset by lower commercial construction and commercial mortgage loans as those portfolios continue to experience run-off.

Average consumer portfolio loan and lease balances were up 2 percent sequentially and increased 4 percent from the fourth quarter of 2009. Sequential comparisons were affected by the sale of $228 million of nonperforming residential mortgage loans at the end of the third quarter, but otherwise reflected growth in residential mortgage loans driven by increased originations and retention of loans in the portfolio. This growth was partially offset by lower home equity balances. Year-over-year growth in auto loans more than offset declines in home equity loans, consumer leases, and credit card balances. Mortgage growth included the effect of retaining approximately $890 million of mortgages, the majority of which were retail branch originated, initiated in the third quarter. Year-over-year comparisons were affected by $1.2 billion of securitized auto loans and $263 million of securitized home equity loans that were consolidated on January 1, 2010 due to the previously discussed accounting change.

Deposits

	For the Three Months Ended					% Change	
	December 2010	September 2010	June 2010	March 2010	December 2009	Seq	Yr/Yr
Average Deposits ($ in millions)							
Demand deposits	$ 21,066	$ 19,362	$ 19,406	$ 18,822	$ 18,137	9%	16%
Interest checking	17,578	17,142	18,652	19,533	16,324	3%	8%
Savings	20,602	19,905	19,446	18,469	17,540	4%	17%
Money market	4,985	4,940	4,679	4,622	4,279	1%	16%
Foreign office (a)	3,733	3,592	3,325	2,757	2,516	4%	48%
Subtotal - Transaction deposits	67,964	64,941	65,508	64,203	58,796	5%	16%
Other time	8,490	10,261	11,336	12,059	13,049	(17%)	(35%)
Subtotal - Core deposits	76,454	75,202	76,844	76,262	71,845	2%	6%
Certificates - $100,000 and over	4,858	6,096	6,354	7,049	8,200	(20%)	(41%)
Other	9	4	5	8	51	112%	(83%)
Total deposits	$ 81,321	$ 81,302	$ 83,203	$ 83,319	$ 80,096		2%

(a) Includes commercial customer Eurodollar sweep balances for which the Bancorp pays rates comparable to other commercial deposit accounts.

Average core deposits increased 2 percent sequentially and 6 percent from the fourth quarter of 2009. Growth across all transaction deposit account categories offset sequential and year-over-year declines in consumer CDs. Average transaction deposits, excluding consumer time deposits, increased 5 percent from the third quarter of 2010 and 16 percent over the prior year quarter. Sequential growth was primarily driven by seasonally strong demand deposit account (DDA) and savings balances. Year-over-year performance was also due to growth in savings and DDA balances.

Retail average transaction deposits increased 4 percent sequentially and 14 percent from the fourth quarter of 2009 and reflected growth in DDA, savings, and checking account balances. Consumer CDs included in core deposits declined 17 percent sequentially and 35 percent year-over-year, reflecting maturities of higher priced CDs as well as current pricing strategies given our robust liquidity position.

Commercial average transaction deposits increased 5 percent sequentially and 18 percent from the previous year. Excluding public funds balances, commercial average transaction deposits increased 6 percent sequentially and 33 percent from the fourth quarter of 2009 driven by interest checking and DDA balances, reflecting excess customer liquidity. Average public funds balances were $5.1 billion, relatively flat sequentially and down $1.1 billion from the fourth quarter of 2009 due to ongoing pricing adjustments, which continue to reflect our excess liquidity position.

Noninterest Income

	For the Three Months Ended					% Change	
	December 2010	September 2010	June 2010	March 2010	December 2009	Seq	Yr/Yr
Noninterest Income ($ in millions)							
Service charges on deposits	$ 140	$ 143	$ 149	$ 142	$ 159	(3%)	(12%)
Corporate banking revenue	103	86	93	81	89	21%	16%
Mortgage banking net revenue	149	232	114	152	132	(36%)	13%
Investment advisory revenue	93	90	87	91	86	4%	8%
Card and processing revenue	81	77	84	73	76	5%	7%
Other noninterest income	55	195	85	74	107	(72%)	(49%)
Securities gains, net	21	4	8	14	2	425%	950%
Securities gains, net - non-qualifying hedges on mortgage servicing rights	14					NM	NM
Total noninterest income	$ 656	$ 827	$ 620	$ 627	$ 651	(21%)	1%

NM: Not Meaningful

Noninterest income of $656 million decreased $171 million, or 21 percent, sequentially and was consistent with results a year ago. The sequential decline was driven by the $152 million benefit in the prior quarter from the settlement of litigation associated with one of the Bancorp s BOLI policies as well as lower mortgage banking revenue, partially offset by growth in corporate banking revenue and securities gains. The year-over-year comparison reflected securities gains in the fourth quarter of 2010 as well as higher mortgage banking revenue, corporate banking revenue, investment advisory revenue, and card and processing revenue, which was largely offset by lower other noninterest income, described in detail below, and lower deposit services charges driven by the effect of Regulation E.

Fourth quarter 2010 results included $11 million in revenue associated with the transition service agreement (TSA) entered into as part of our processing business sale, under which the Bancorp provides services to the processing business to support its operations during the deconversion period. TSA revenue was $13 million in the third quarter of 2010 and $39 million in the fourth quarter of 2009. Fourth quarter results also included a $3 million positive valuation adjustment on warrants and puts related to the processing business sale, compared with $5 million in negative valuation adjustments on these instruments in the third quarter of 2010 and $20 million in positive valuation adjustments in the fourth quarter of 2009. Third quarter 2010 results included a benefit of $152 million from the settlement of litigation associated with one of the Bancorp s BOLI policies. Excluding these items, as well as investment securities gains in all periods, noninterest income decreased $42 million, or 6 percent, from the previous quarter, driven by lower mortgage banking net revenue. On a year-over-year basis, noninterest income excluding the items mentioned above increased $31 million, or 5 percent, due to higher mortgage banking net revenue and investment advisory fees partially offset by lower service charges on deposits.

Service charges on deposits of $140 million decreased 3 percent sequentially and 12 percent compared with the same quarter last year. Retail service charges declined 9 percent from the previous quarter and declined 26 percent compared with the fourth quarter of 2009, largely due to the implementation of new overdraft regulations and overdraft policies. Commercial service charges increased 3 percent sequentially and increased 2 percent compared with last year.

Corporate banking revenue of $103 million increased 21 percent from the third quarter of 2010 and increased 16 percent from the same period last year. Sequential results were primarily driven by increased loan syndication fee revenue and lease remarketing fees, as well as growth in business lending fees and foreign exchange revenue due to higher loan volumes and seasonality. On a year-over-year basis, loan syndication fee revenue, lease remarketing fees, and revenue from interest rate derivative sales and business lending fees more than offset declines in institutional sales.

Investment advisory revenue of $93 million increased 4 percent sequentially and 8 percent from the fourth quarter of 2009. The sequential growth was driven by higher private client services revenue, institutional trust revenue, and brokerage fees due to market value increases as well as improved sales production resulting in strong net asset and account growth. On a year-over-year basis, improvement also reflected an overall increase in equity and bond market values.

Card and processing revenue was $81 million in the fourth quarter of 2010, up 5 percent sequentially and 7 percent from the fourth quarter of 2009. The sequential increase reflected positive seasonality and both sequential and year-over-year comparison periods were driven by higher transaction volumes.

Mortgage banking net revenue was $149 million in the fourth quarter of 2010, a decrease of $83 million from the very strong third quarter of 2010 and an increase of $17 million from the fourth quarter of 2009. Fourth quarter 2010 originations were $7.4 billion, an increase from $5.6 billion in the previous quarter and $4.8 billion in the fourth quarter of 2009. Fourth quarter 2010 originations resulted in gains of $158 million on mortgages sold compared with gains of $173 million during the previous quarter and $97 million during the same period in 2009. Gain on sale margins declined in the fourth quarter from record levels in the third quarter due to rising mortgage rates in the quarter and the closing of a higher than expected percentage of applications during the quarter. Mortgage servicing fees this quarter were $59 million, compared with $56 million in the third quarter of 2010 and $53 million in the fourth quarter of 2009. Mortgage banking revenue is also affected by net servicing asset value adjustments, which include mortgage servicing rights (MSR) amortization and MSR valuation adjustments (including mark-to-market adjustments on free-standing derivatives used to economically hedge the MSR portfolio). These net servicing asset valuation adjustments were negative $67 million in the fourth quarter (reflecting MSR amortization of $47 million and MSR valuation adjustments of negative $20 million); positive $3 million in the third quarter of 2010 (MSR amortization of $43 million and MSR valuation adjustments of positive $46 million); and negative $18 million in the fourth quarter of 2009 ($27 million in MSR amortization and positive $9 million in MSR valuation adjustments). The mortgage-servicing asset, net of the valuation reserve, was $822 million at quarter end on a servicing portfolio of $54 billion.

Gains on securities held as non-qualifying hedges for the MSR were $14 million in the fourth quarter of 2010.

Other noninterest income totaled $55 million in the fourth quarter of 2010 compared with $195 million in the previous quarter and $107 million in the fourth quarter of 2009. Fourth quarter 2010 results included net losses of $14 million on commercial loans held-for-sale, as outlined more fully below. This quarter s results also reflected $11 million of TSA revenue, $8 million of revenue from our equity interest in the processing business, and a $3 million positive valuation adjustment of warrants and puts related to the processing business sale. Third quarter 2010 results included the $152 million gain from the settlement of litigation related to a BOLI policy, $10 million of net losses on commercial loans held-for-sale, $13 million of TSA revenue, $7 million of revenue from our equity interest in the processing business, and a negative valuation adjustment of $5 million on warrants and puts related to the processing business sale. Fourth quarter 2009 results included $9 million of net losses on commercial loans held-for-sale, $39 million of TSA revenue, $8 million of revenue from our processing business equity interest, and a $20 million positive valuation adjustment of warrants and puts related to the processing business sale. Excluding these items, other noninterest income increased $9 million from the previous quarter, primarily due to the effects of lower credit-related costs, and decreased $2 million from the fourth quarter of 2009.

Net credit-related costs recognized in noninterest income were $34 million in the fourth quarter of 2010 versus $42 million last quarter and $31 million in the fourth quarter of 2009. This quarter we realized $21 million of net gains on sales of commercial loans held-for-sale and recorded $35 million of fair value charges on commercial loans held-for-sale. We also recorded $19 million of losses on other real estate owned (OREO). Third quarter 2010 results included net losses of $1 million on the sale of commercial loans held-for-sale, $9 million of fair value charges on commercial loans held-for-sale, and $29 million of losses on OREO. Fourth quarter 2009 results included net gains of $8 million on the sale of commercial loans held-for-sale, $17 million of fair value charges on commercial loans held-for-sale, and $21 million of losses on OREO.

Net gains on investment securities were $21 million in the fourth quarter of 2010, compared with investment securities gains of $4 million in the previous quarter and $2 million in the same period the previous year.

Noninterest Expense

	For the Three Months Ended					% Change	
	December 2010	September 2010	June 2010	March 2010	December 2009	Seq	Yr/Yr
Noninterest Expense ($ in millions)							
Salaries, wages and incentives	$ 385	$ 360	$ 356	$ 329	$ 331	7%	16%
Employee benefits	73	82	73	86	69	(11%)	5%
Net occupancy expense	76	72	73	76	75	5%	1%
Technology and communications	52	48	45	45	47	8%	9%
Equipment expense	32	30	31	30	31	5%	3%
Card and processing expense	26	26	31	25	27	2%	(2%)
Other noninterest expense	343	361	326	365	387	(5%)	(11%)
Total noninterest expense	$ 987	$ 979	$ 935	$ 956	$ 967	1%	2%

Noninterest expense of $987 million increased $8 million sequentially and $20 million from a year ago. Fourth quarter 2010 results included $17 million of expenses related to the termination of $1 billion in FHLB funding. Third quarter 2010 results included $25 million in legal expenses associated with the previously described

BOLI settlement. Fourth quarter 2009 results included a $22 million reserve established for litigation associated with bank card association memberships. Excluding these items, noninterest expense was $970 million in the fourth quarter of 2010, compared with $954 million in the third quarter of 2010 and $945 million in the fourth quarter of 2009. This sequential and year-over-year increase was driven by higher compensation expense primarily due to revenue-based incentives, as well as investment in sales force expansion, partially offset by lower credit-related expenses. Each period included operating expenses related to the processing business that were largely offset by revenue under the TSA reported in other noninterest income.

Noninterest expenses incurred related to problem assets totaled $53 million in the fourth quarter of 2010, compared with $67 million in the third quarter of 2010 and $73 million in the fourth quarter of 2009. Fourth quarter credit-related expenses included mortgage repurchase expense of $20 million, compared with $45 million in the third quarter of 2010 and $17 million a year ago. (Realized mortgage repurchase losses were $23 million in the fourth quarter of 2010, compared with $29 million last quarter and $15 million in the fourth quarter of 2009.) Provision expense for unfunded commitments was a $4 million reduction in the allowance for unfunded commitments in the current quarter, compared with a $23 million reduction last quarter and $11 million of expense to increase this allowance a year ago. Derivative valuation adjustments related to customer credit risk were positive $1 million this quarter versus $8 million of expense last quarter and $2 million in gains a year ago. OREO expense was $11 million this quarter, compared with $9 million last quarter and $9 million a year ago. Other work out-related expenses were $27 million in the fourth quarter, compared with $28 million the previous quarter and $37 million in the same period last year.

Credit Quality

	For the Three Months Ended				
	December 2010	September 2010	June 2010	March 2009	December 2010
Total net losses charged off ($ in millions)					
Commercial and industrial loans	($ 85)	($ 237)	($ 104)	($ 161)	($ 183)
Commercial mortgage loans	(80)	(268)	(78)	(99)	(142)
Commercial construction loans	(11)	(121)	(43)	(78)	(135)
Commercial leases	3	(1)		(4)	(8)
Residential mortgage loans	(62)	(204)	(85)	(88)	(78)
Home equity	(65)	(66)	(61)	(73)	(82)
Automobile loans	(19)	(17)	(20)	(31)	(32)
Credit card	(33)	(36)	(42)	(44)	(44)
Other consumer loans and leases	(4)	(6)	(1)	(4)	(4)
Total net losses charged off	(356)	(956)	(434)	(582)	(708)
Total losses	(399)	(992)	(472)	(622)	(743)
Total recoveries	43	36	38	40	35
Total net losses charged off	($ 356)	($ 956)	($ 434)	($ 582)	($ 708)
Ratios (annualized)					
Net losses charged off as a percent of average loans and leases (excluding held for sale)	1.86%	4.95%	2.26%	3.01%	3.62%
Commercial	1.59%	5.66%	2.03%	3.07%	4.08%
Consumer	2.20%	4.00%	2.57%	2.93%	2.97%

Net charge-offs were $356 million in the fourth quarter of 2010, or 186 bps of average loans on an annualized basis. Third quarter 2010 net charge-offs were $956 million, or 495 bps of average loans on an annualized basis and included net losses of $510 million realized on the sale or transfer of loans to held-for-sale.

Excluding these losses, fourth quarter 2010 portfolio net-charge offs declined $90 million from third quarter 2010 portfolio net charge-offs of $446 million. Fourth quarter 2009 net charge-offs were $708 million. The decreases in net charge-offs from the prior quarters reflected continued improvement in the credit quality of loans in our portfolio as well as the benefit from the credit actions taken during the third quarter of 2010.

Commercial net charge-offs were $173 million, or 159 bps, compared with $627 million, or 566 bps, in the third quarter of 2010, which included $387 million in net charge-offs on the transfer of loans held-for-sale. Excluding these losses, commercial net charge-offs decreased $67 million from the $240 million of net portfolio losses in the previous quarter. C&I net losses in the portfolio were $85 million, compared with net portfolio losses of $129 million in the previous quarter and $108 million in net losses realized on loans transferred to held-for-sale. The sequential decrease in net portfolio losses was primarily driven by $32 million of improvement in losses on loans to companies in real-estate related industries. Commercial mortgage net losses in the portfolio totaled $80 million compared with net portfolio losses of $66 million in the third quarter and $202 million in net losses realized on loans transferred to held-for-sale. Commercial construction net losses in the portfolio were $11 million, compared with net portfolio losses of $44 million in the prior quarter and $77 million in net losses realized on loans transferred to held-for-sale. Net losses on residential builder and developer portfolio loans across the C&I and commercial real estate categories totaled $19 million, the lowest level experienced in several years. Originations of homebuilder/developer loans were suspended in 2007 and the remaining portfolio balance is $699 million, down from a peak of $3.3 billion in the second quarter of 2008.

Consumer net charge-offs were $183 million, or 220 bps, in the fourth quarter of 2010, compared with $329 million, or 400 bps, in the third quarter, which included $123 million in net charge-offs on the sale of residential mortgage loans during the third quarter. Excluding these losses, consumer net charge-offs decreased $23 million from $206 million in the third quarter. Net charge-offs on residential mortgage loans in the portfolio were $62 million, compared with portfolio losses of $81 million in the previous quarter and $123 million in net charge-offs on loans sold during the third quarter. Home equity net charge-offs were $65 million, consistent with last quarter. Net losses on brokered home equity loans represented 38 percent of fourth quarter home equity losses and 15 percent of the total home equity portfolio. The home equity portfolio included $1.7 billion of brokered loans, down from a peak of $2.6 billion in 2007; originations of these loans were discontinued in 2007. Net charge-offs in the auto portfolio of $19 million increased $2 million from the third quarter, primarily due to seasonality, and net losses on consumer credit card loans were $33 million, down $3 million from the previous quarter.

	For the Three Months Ended				
	December 2010	September 2010	June 2010	March 2010	December 2009
Allowance for Credit Losses ($ in millions)					
Allowance for loan and lease losses, beginning	$ 3,194	$ 3,693	$ 3,802	$ 3,749	$ 3,681
Impact of cumulative effect of change in accounting principle				45	
Total net losses charged off	(356)	(956)	(434)	(582)	(708)
Provision for loan and lease losses	166	457	325	590	776
Allowance for loan and lease losses, ending	3,004	3,194	3,693	3,802	3,749
Reserve for unfunded commitments, beginning	231	254	260	294	284
Impact of cumulative effect of change in accounting principle				(43)	
Provision for unfunded commitments	(4)	(23)	(6)	9	10
Reserve for unfunded commitments, ending	227	231	254	260	294
Components of allowance for credit losses:					
Allowance for loan and lease losses	3,004	3,194	3,693	3,802	3,749
Reserve for unfunded commitments	227	231	254	260	