WACHOVIA CORP NEW
Form POS AM
April 23, 2003
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**As filed with the Securities and Exchange Commission on April 23, 2003**

**Registration No. 333-99847**

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## SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

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**POST - EFFECTIVE**
**AMENDMENT NO. 4**

**TO**
**FORM S-3**
**REGISTRATION STATEMENT**
***UNDER***
***THE SECURITIES ACT OF 1933***
**OF**

**WACHOVIA CORPORATION**
**(Formerly named First Union Corporation)**
**(Exact name of registrant as specified in its charter)**

**North Carolina**
**(State or other jurisdiction of incorporation or organization)**

**56-0898180**

**(I.R.S. Employer Identification No.)**

**One Wachovia Center**

**Charlotte, North Carolina 28288**

**(704) 374-6565**

**(Address, including zip code, and telephone number,**

**including area code, of registrant s principal executive offices)**

**WACHOVIA PREFERRED FUNDING CORP.**
**(Exact name of registrant as specified in its charter)**

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

**56-1986430**

**(I.R.S. Employer Identification No.)**

**1620 East Roseville Parkway**
**Roseville, California 95661**

**(877) 867-7378**

**(Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)**

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**Ross E. Jeffries, Jr., Esq.**

**Senior Vice President and Assistant General Counsel**

**WACHOVIA CORPORATION**

**One Wachovia Center**

**Charlotte, North Carolina 28288-0630**

**(704) 374-6611**

**(Name, address, including zip code, and telephone number, including area code, of agent for service)**

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*Copies to:*

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|---|---|
| **Mark J. Menting, Esq.**<br>**Robert W. Downes, Esq.**<br>**Sullivan & Cromwell**<br>**125 Broad Street**<br>**New York, New York 10004**<br>**(212) 558-4000** | **Kenneth L. Bachman, Esq.**<br>**Cleary, Gottlieb, Steen & Hamilton**<br>**2000 Pennsylvania Avenue**<br>**Washington, D.C. 20006**<br>**(202) 974-1500** |

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**Approximate date of commencement of proposed sale to the public: As soon as practicable after this Registration Statement becomes effective.**

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box. x

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. ¨

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The Registrants hereby amend the Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrants shall file a further amendment which specifically states that the Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the Registration Statement shall become effective on such date or dates as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

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**18,000,000 Series A Preferred Securities**

# Wachovia Preferred Funding Corp.

**7.25% Non-cumulative Exchangeable**

**Perpetual Series A Preferred Securities**

## (Liquidation Preference $25.00 Per Security)

## Automatically Exchangeable in Specified Circumstances into

## Depositary Shares representing Preferred Stock of Wachovia Corporation

Terms of the Series A preferred securities include:

- Dividends are:
  - payable quarterly only if declared, and
  - non-cumulative, which means that you will not receive them later if they are not declared in the applicable period.
- Conditionally exchangeable, without your approval or any action on your part, for depositary shares with substantially equivalent terms as to dividends, liquidation preference and redemption of Wachovia Corporation, our indirect parent company, except that the depositary shares will:
  - not have any voting rights,
  - not have the right to elect independent directors,
  - not have the benefit of similar favorable covenants as the Series A preferred securities, and
  - not be listed on any securities exchange.
- This exchange will be made only at the direction of the Office of the Comptroller of the Currency under the following specified circumstances:
  - Wachovia Bank, National Association, our indirect parent company, becomes undercapitalized under the OCC s prompt corrective action regulations, or
  - the Bank is placed into conservatorship or receivership, or
  - the OCC, in its sole discretion, anticipates that the Bank may become undercapitalized in the near term, or takes supervisory action that limits the payment of dividends by us and in connection therewith directs an exchange.
- Redeemable at our option on or after December 31, 2022, with the prior consent of the OCC.
- Senior to our common stock and our Series C preferred securities but on a parity with our Series B and D preferred securities.
- Entitled to 1/10th of one vote per security on all matters submitted to holders of our common stock.

We are qualified as a real estate investment trust, or REIT, for Federal income tax purposes.

Prior to this offering, there has been no public market for the Series A preferred securities. We have applied for the listing of the Series A preferred securities on the New York Stock Exchange under the symbol WNA Pr . Trading in the Series A preferred securities is expected to commence not later than 30 days after the delivery of the Series A preferred securities. Consequently, there will be no trading market for the Series A preferred securities, at least in the short term.

**See Risk Factors beginning on page 14 for a description of risk factors you should consider before you invest in these securities.**

The Series A preferred securities solely represent an interest in us and are not the obligation of, or guaranteed by, any other entity. These securities are not deposits or accounts and are not insured or guaranteed by the Federal Deposit Insurance Corporation or any other governmental agency.

**Neither the Securities and Exchange Commission, the OCC, nor any other federal agency or state securities regulator has approved or disapproved these securities or determined if this prospectus is accurate or complete. Any representation to the contrary is a criminal offense.**

Any broker-dealer affiliate of Wachovia Preferred Funding Corp., including, without limitation, Wachovia Securities, Inc., may use this prospectus in market-making transactions involving the Series A preferred securities after their initial sale or depositary shares of Wachovia Corporation after the occurrence of a conditional exchange in the circumstances described above.

*Wachovia Securities*

*Sole Bookrunner*

| | | |
|---|---|---|
| *A. G. Edwards & Sons, Inc.* | *Banc of America Securities LLC* | *Merrill Lynch & Co.* |
| *Morgan Stanley* | *Prudential Securities* | *UBS Warburg* |

Prospectus dated December 11, 2002

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*The following table of contents has been designed to help you find important information contained in this prospectus. We encourage you to read the entire prospectus.*

*Wachovia Funding , we , our and us refer to Wachovia Preferred Funding Corp. Wachovia Preferred Holding refers to Wachovia Preferred Funding Holding Corp., the Bank refers to Wachovia Bank, National Association, and Wachovia refers to Wachovia Corporation.*

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**FORWARD-LOOKING STATEMENTS**

This prospectus contains or incorporates statements that are forward-looking statements. These statements can be identified by the use of forward-looking language such as will likely result , may , are expected to , is anticipated , estimate , projected , intends to , or other simila

Wachovia Funding s and Wachovia s actual results, performance or achievements could be significantly different from the results expressed in or implied by these forward-looking statements. These statements are subject to certain risks and uncertainties, including but not limited to certain risks described in this prospectus or the documents incorporated by reference. When considering these forward-looking statements, you should keep in mind these risks, uncertainties and other cautionary statements made in this prospectus. You should not place undue reliance on any forward-looking statement, which speaks only as of the date made. You should refer to Wachovia Funding s and Wachovia s periodic and current reports filed with the SEC for specific risks which could cause actual results to be significantly different from those expressed or implied by these forward-looking statements.

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## PROSPECTUS SUMMARY

*Before you decide to invest in the Series A preferred securities, conditionally exchangeable into the Wachovia depositary shares representing interests in Wachovia Series G, Class A preferred stock, you should carefully read the following summary, together with the more detailed information and financial statements and related notes contained elsewhere in this prospectus, especially the risks of investing in the Series A preferred securities discussed under Risk Factors .*

*You should refer to the Glossary on page 116 for the definitions of certain capitalized and industry and proprietary terms used in this prospectus.*

### General

**Wachovia Preferred Funding Corp.**

We are a Delaware corporation, formed in July 2002 and the survivor of a merger with First Union Real Estate Asset Company of Connecticut, which was formed in 1996. Our principal business objective is to hold and manage mortgage assets and other authorized investments that will generate net income for distribution to our shareholders. We are qualified as a real estate investment trust, or REIT, for Federal income tax purposes. As a REIT, we generally will not be required to pay Federal income tax on distributed income if we distribute at least 90% of our earnings to our shareholders and continue to meet a number of other requirements as discussed below.

Upon our merger, we were a direct subsidiary of the Bank and an indirect subsidiary of Wachovia. By the completion of this offering, we will be a direct subsidiary of Wachovia Preferred Holding as a result of the Bank transferring certain assets, including 99.85% of our common stock and 87.62% of our Series D preferred securities, to Wachovia Preferred Holding in exchange for additional shares of Wachovia Preferred Holding common stock.

Our principal executive offices are located at 1620 East Roseville Parkway, Roseville, California 95661, and our telephone number is (877) 867-7378.

*Assets*

All of the financial information in this section is presented on a pro forma basis to reflect the following:

- $866 million of participation interests in home equity loans received by us as collateral for an intercompany loan to the Bank in October 2002. The underlying home equity loans were originated by the Bank; and the issuance of three new series of preferred securities (Series A, B and C ) to Wachovia Preferred Holding in exchange for participations in commercial and commercial real estate loans prior to this offering. The commercial and commercial real estate loans were originated by the Bank and contributed to Wachovia Preferred Holding. We will issue the preferred securities to Wachovia Preferred Holding in exchange for participations in the loans prior to this offering.

At September 30, 2002, we had total assets of $12.5 billion, total liabilities of $607 million, and stockholders equity of $11.9 billion. As of such date,

$9.8 billion, or 78.7% of our assets, were comprised of participation interests in commercial real estate loans;

$866 million, or 6.9% of our assets, were comprised of an intercompany loan to the Bank secured by participation interests in home equity loans;

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$661 million, or 5.3% of our assets, were comprised of participation interests in commercial loans;

$605 million, or 4.8% of our assets, were comprised of interest rate swaps;

$303 million, or 2.4% of our assets, were comprised of cash and cash equivalents;

$205 million, or 1.6% of our assets, were comprised of participation interests in home equity loans;

$89 million, or 0.7% of our assets, were comprised of residential mortgage loans; and

$31 million, or 0.3% of our assets, were comprised of net other assets;

each before the allowance for loan losses.

In the past, we have purchased or accepted as capital contributions, loans and participation interests in loans both secured and not secured by real property along with other assets. We anticipate that we will acquire, or receive as capital contributions, interests in additional real estate secured loans from the Bank or its affiliates. Although we are permitted to do so, we have no present plans or intentions to purchase loans or loan participation interests from unaffiliated third parties.

*Dividends*

We currently expect to pay an aggregate amount of dividends with respect to the outstanding shares of our capital stock equal to substantially all of our REIT taxable income, which excludes capital gains. In order to remain qualified as a REIT, we must distribute annually at least 90% of our REIT taxable income to stockholders. Dividends will be authorized and declared at the discretion of our board of directors after considering our distributable funds, financial condition and capital needs, the impact of current and pending legislation and regulations, economic conditions, tax considerations, our continued qualification as a REIT, and other factors. Although there can be no assurances, we currently expect that both our cash available for distribution and our REIT taxable income will be in excess of amounts needed to pay dividends on the Series A preferred securities, at the dividend rate of 7.25% per annum of the $25.00 liquidation preference per security, in the foreseeable future because:

substantially all of our mortgage assets and other authorized investments are interest-earning;

we do not anticipate incurring any indebtedness, although we may incur indebtedness that in an aggregate amount does not exceed 20% of our shareholders equity;

we expect that our interest-earning assets will continue to exceed the liquidation preference of all of our series of preferred stock;

the amount of loan servicing costs and management fees paid to the Bank are expected to be less than 4% of our income per year; and

we anticipate that, in addition to cash flows from operations, additional cash will be available from principal payments on our loan portfolio.

*Management*

Our board of directors is currently composed of one member who is also an employee of Wachovia and therefore not considered independent. Prior to this offering, we will elect three additional directors, two of whom will satisfy the definition of being independent as set forth in the corporate governance standards of the New York Stock Exchange, as amended from time to time. We refer to directors satisfying this NYSE independence definition as Independent Directors . We currently have two executive officers and approximately 15 additional officers. Our executive officers are also executive officers of Wachovia. All of our day-to-day activities and the servicing of the loans in our portfolio are administered, pursuant to participation and servicing agreements, by the Bank, which is our indirect parent company.

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**Risk Factors**

A purchase of our Series A preferred securities is subject to a number of risks described in more detail under Risk Factors beginning on page 14. These risks include, but are not limited to:

Dividends on the Series A preferred securities are not cumulative. Consequently, our board of directors may decide to declare less than a full dividend or no dividend on the Series A preferred securities for any quarterly period and you will not be entitled to receive that dividend whether or not funds are or subsequently become available.

The Series A preferred securities solely represent an interest in us and are not the obligation of, or guaranteed by, Wachovia, the Bank or any other entity. A decline in the performance and capital levels of the Bank or the placement by the Office of the Comptroller of the Currency, or the OCC , of the Bank into conservatorship or receivership could result in the automatic exchange of each Series A preferred security for one depositary share representing a one-sixth interest in one share of Wachovia Series G, Class A, preferred stock. Upon such an exchange, you would have an investment in Wachovia and not in us at a time when the Bank s and, ultimately, Wachovia s financial condition is deteriorating.

Based on our ownership immediately after the offering, the holders of our Series A preferred securities not affiliated with Wachovia will have the right to vote less than 2% of all votes on matters on which all our shareholders are entitled to vote and the right to vote 60% of all votes on any matter which requires the holders of Series A preferred securities to vote separately as a single class.

Due to, among other things, certain changes in legislation, regulations or our capital structure, we could fail to qualify as a REIT. As a result of such loss of qualification, we would suffer adverse tax consequences.

Our close relationship with Wachovia and the Bank may create potential conflicts of interest. Wachovia and the Bank are involved in virtually every aspect of our existence.

We have no control over changes in interest rates and such changes could negatively impact our financial condition, results of operations, and ability to pay dividends.

The loans in our portfolio are subject to economic conditions that could negatively affect the value of the collateral securing such loans and/or the results of our operations.

We cannot assure you that we paid the Bank fair value for all of our assets because we have not obtained any third party valuation of all those assets. Nor can we assure you that we will acquire or dispose of assets in the future at their fair market value.

The exchange of our Series A preferred securities for depositary shares representing an interest in Wachovia Series G, Class A, preferred stock would most likely be a taxable event to you under the Code, and you would incur a gain or loss.

A decline in Wachovia s financial condition following an exchange may restrict its ability to pay dividends and could result in a loss on your investment.

The holders of the depositary shares representing Wachovia Series G, Class A, preferred stock will:

- not have voting rights;
- not have the right to elect Independent Directors even if dividends are not authorized and declared by Wachovia s board of directors;
- not have the benefit of similar favorable covenants as the Series A preferred securities; and
- not be listed on any securities exchange.

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*Conflicts of Interest*

Because our day-to-day business affairs are managed by the Bank, conflicts of interest will arise from time to time between us and the Bank. These conflicts of interest relate to, among other things:

- the amount, type, and price of loan participation interests and other assets we acquire from or sell to the Bank;
- the servicing of the underlying loans, particularly with respect to loans that are placed on non-accrual status;
- the management of the cash collateral related to our interest rate swaps;
- the amount of loan servicing costs and management fees paid to the Bank;
- the treatment of new business opportunities identified by the Bank; and
- the modification of the loan participation and servicing agreements.

We have adopted policies with a view to ensuring that all financial dealings between the Bank and us will be fair to both parties and consistent with market terms.

**Wachovia Preferred Funding Holding Corp.**

Wachovia Preferred Holding is a California corporation which by completion of this offering will own:

- 99,851,752 (or 99.85%) of our common stock;
- 12,000,000 (or 40%) of our outstanding Series A preferred securities;
- 40,000,000 (or 100%) of our outstanding Series B preferred securities;
- 4,233,754 (or 100%) of our outstanding Series C preferred securities; and
- 800 (or approximately 88%) of our outstanding Series D preferred securities.

By the completion of this offering, the Bank will own 99.95% of the outstanding shares of common stock of Wachovia Preferred Holding. Approximately two weeks prior to this offering, the Bank will contribute its ownership of us, consisting of 99.85% of our common stock and 87.62% of our Series D preferred securities, as well as commercial and commercial real estate loan participations to Wachovia Preferred Holding in exchange for Wachovia Preferred Holding common stock. Immediately thereafter, pursuant to an assignment of a participation agreement, Wachovia Preferred Holding will acquire from us 30,000,000 Series A, 40,000,000 Series B and 4,233,754 Series C preferred securities, with liquidation preferences of $25.00, $25.00 and $1,000 per security, respectively, in exchange for participation interests in certain commercial and commercial real estate loans. Subsequent to this exchange, Wachovia Preferred Holding will offer for sale 18,000,000 Series A preferred securities in this offering.

Although a statutory underwriter in connection with this offering, Wachovia Preferred Holding will not sell the Series A preferred securities directly to the public and will not have the rights and obligations of an underwriter under the underwriting agreement that we will enter into with the underwriters of this offering.

Wachovia Preferred Holding s principal executive offices are located at 1620 East Roseville Parkway, Roseville, California 95661, and its telephone number is (877) 867-7378.

**Wachovia Corporation**

Wachovia was incorporated under the laws of North Carolina in 1967. Wachovia is registered as a financial holding company and a bank holding company under the Bank Holding Company Act of 1956, as amended, and is supervised and regulated by the Board of Governors of the Federal Reserve System. Wachovia s banking and securities subsidiaries are supervised and regulated by various Federal and state banking and securities regulatory authorities. On September 1, 2001, the former Wachovia Corporation merged with and into First Union Corporation, and First Union Corporation changed its name to Wachovia Corporation .

Wachovia s full-service banking subsidiaries provide a wide range of commercial and retail banking and trust services. Wachovia also provides a variety of other financial services through other subsidiaries, including mortgage banking, home equity lending, leasing, investment banking, insurance and securities brokerage services.

Wachovia is a separate and distinct legal entity from its banking and other subsidiaries. Dividends received by it from its subsidiaries are Wachovia s principal source of funds to pay dividends on its common and preferred stock and to service its debt. Various Federal and state statutes and regulations limit the amount of dividends that Wachovia s subsidiaries may pay to Wachovia without regulatory approval.

In 1985, the Supreme Court upheld regional interstate banking legislation. Since then, Wachovia has concentrated its efforts on building a large regional banking organization in what it perceives to be some of the better banking markets in the eastern United States. Since November 1985, Wachovia has completed over 90 banking-related acquisitions.

Wachovia continually evaluates its business operations and organizational structures to ensure they are aligned closely with its goal of maximizing performance in its core business lines. Therefore, Wachovia routinely explores acquisition opportunities, particularly in areas that would complement its core business lines, and frequently conducts due diligence activities in connection with possible acquisitions. As a result, acquisition discussions and, in some cases, negotiations frequently take place, and future acquisitions involving cash, debt or equity securities can be expected. When consistent with Wachovia s overall business strategy, Wachovia also considers the potential disposition of certain of its assets, branches, subsidiaries or lines of business.

The principal executive offices of Wachovia are located at One Wachovia Center, Charlotte, North Carolina 28288, and its telephone number is (704) 374-6565.

**Wachovia Bank, National Association**

The Bank is a national banking association with its principal office in Charlotte, North Carolina, that offers a wide range of domestic and international retail and commercial banking and trust services. The Bank has offices in Connecticut, Florida, Georgia, Maryland, New Jersey, New York, North Carolina, Pennsylvania, South Carolina, Virginia and Washington, D.C., and in several foreign countries. On April 1, 2002, the former Wachovia Bank, National Association merged with and into First Union National Bank, and First Union National Bank changed its name to Wachovia Bank, National Association . The Bank s business is subject to examination and regulation by United States Federal banking authorities. Based on deposits of $195.4 billion as of September 30, 2002, the Bank was the fifth largest bank in the United States. The Bank has numerous wholly-owned subsidiaries, none of which contributes over 30% of its consolidated net income. For more information see Information Concerning the Bank .

The principal executive offices of the Bank are located at One Wachovia Center, Charlotte, North Carolina 28288, and its telephone number is (704) 374-6565.

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**Our Organizational Structure**

Upon the completion of this offering, our legal and organizational structure will be as follows:

(1)The remaining 12.38% of our Series D preferred securities is held by employees of Wachovia or its affiliates.

**Conditional Exchange of Series A Preferred Securities**

The Series A preferred securities will be exchanged automatically for depositary shares representing Series G, Class A preferred stock of Wachovia at the direction of the OCC if any of the following events occurs:

- the Bank becomes undercapitalized under the OCC s prompt corrective action regulations;
- the Bank is placed into conservatorship or receivership; or
- the OCC, in its sole discretion, anticipates that the Bank may become undercapitalized in the near term or takes supervisory action that limits the payment of dividends by us and in connection therewith directs an exchange.

In an exchange, you would receive one depositary share representing a one-sixth interest in one share of Wachovia Series G, Class A preferred stock with a liquidation preference of $25.00 per depositary share for each of our Series A preferred securities you own. The Wachovia Series G, Class A preferred stock will be non-cumulative, perpetual, non-voting preferred stock of Wachovia ranking equally upon issuance with the most senior preferred stock of Wachovia then outstanding. If a Conditional Exchange occurs you would own an investment in Wachovia and not in us at a time when the Bank s and, ultimately, Wachovia s financial condition is deteriorating or the Bank may have been placed into conservatorship or receivership. Please see Where You Can Find More Information about Wachovia .

**Reasons for the Offering**

The Series A preferred securities are being offered for sale to increase the Bank s and Wachovia s regulatory capital. The proceeds from the sale of the Series A preferred securities will be included as Tier 1 capital of the Bank and Wachovia under relevant regulatory capital guidelines.

Additionally, the Series A preferred securities will be included in other liabilities on the consolidated balance sheet of Wachovia.

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**Selected Consolidated Financial Data**

The following selected consolidated financial data for the three years ended December 31, 2001, are derived from our audited consolidated financial statements. The following selected consolidated financial data for the nine months ended September 30, 2002 and 2001, are derived from unaudited consolidated financial statements and reflect all adjustments, consisting only of normal recurring adjustments, that, in the opinion of our management, are necessary for a fair and consistent presentation of such data. Operating results for the nine months ended September 30, 2002, are not necessarily indicative of results expected for the entire year. This data should be read in conjunction with the consolidated financial statements, related notes, and other financial information beginning on page F-1 of this prospectus and Wachovia s unaudited supplementary consolidating financial information as of and for the nine months ended September 30, 2002, and the years ended December 31, 2001 and 2000, which includes certain consolidated financial information for the Bank, beginning on Page F-22 of this prospectus.

| | Nine Months Ended September 30, | | Years Ended December 31, | | |
|---|---|---|---|---|---|
| **(In thousands, except per share data)** | **2002** | **2001** | **2001** | **2000** | **1999** |
| **Income Statement Data** | | | | | |
| Net interest income | $ 127,098 | 43,374 | 67,322 | 57,257 | 47,005 |
| Provision for loan losses | 7,033 | 6,290 | 5,262 | 3,602 | 1,034 |
| Other income (loss) | 68,356 | | (95,890) | 395 | 96 |
| Noninterest expense | 6,597 | 1,013 | 2,394 | 2,207 | 3,078 |
| Net income (loss) | $ 305,936 | 23,446 | (23,545) | 32,434 | 27,951 |
| **Balance Sheet Data** | | | | | |
| Cash and cash equivalents | $ 1,169,380 | 327,057 | 957,454 | 183,223 | 196,397 |
| Loans, net of unearned income | 4,297,280 | 440,040 | 4,378,961 | 558,756 | 512,858 |
| Allowance for loan losses | (37,335) | (5,655) | (37,158) | (3,833) | (1,285) |
| Interest rate swaps | 605,438 | | 573,620 | | |
| Total assets | 6,071,086 | 775,039 | 5,889,666 | 746,803 | 714,097 |
| Collateral held on interest rate swaps | 599,570 | | 570,340 | | |
| Total liabilities | 606,938 | 5,082 | 732,246 | 283 | |
| Total stockholders equity | $ 5,464,148 | 769,957 | 5,157,420 | 746,520 | 714,097 |
| **Selected Other Information** | | | | | |
| Nonperforming loans | $ 16,425 | 2,882 | 5,024 | 2,684 | 3,733 |
| Nonperforming loans as a % of total loans | 0.38% | 0.65 | 0.11 | 0.48 | 0.73 |
| Nonperforming loans as a % of total assets | 0.27 | 0.37 | 0.09 | 0.36 | 0.52 |
| Allowance for loan losses as a % of nonperforming loans | 227.31 | 196.22 | 739.61 | 142.81 | 34.42 |
| Allowance for loan losses as a % of total loans | 0.87% | 1.29 | 0.85 | 0.69 | 0.25 |

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## The Offering

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| **Issuer** | Wachovia Preferred Funding Corp., a Delaware corporation that will be an indirect subsidiary of Wachovia and the Bank and operates as a REIT for Federal income tax purposes. |
| **Securities Offered** | 18,000,000 7.25% Non-cumulative Exchangeable Perpetual Series A Preferred Securities. |
| **Ranking** | With respect to the payment of dividends and liquidation preference, the Series A preferred securities will rank equal to our Series B and D preferred securities and senior to our common stock and Series C preferred securities. Additional preferred stock ranking senior to the Series A preferred securities, which we refer to as Senior Stock , may not be issued without the approval of holders of at least two-thirds of the Series A preferred securities. Additional preferred stock ranking on a parity with the Series A preferred securities, which we refer to as Parity Stock , may be issued without your approval, but that issuance requires the approval of a majority of our Independent Directors. |
| **Dividends** | Dividends on the Series A preferred securities are payable at the rate of 7.25% per annum of the liquidation preference of $25.00 per security, if, when, and as declared by our board of directors. If declared, dividends are payable quarterly in arrears on March 31, June 30, September 30 and December 31 of each year or, if any such day is not a business day, on the next business day, unless the next business day falls in a different calendar year, in which case the dividend will be paid on the preceding business day, commencing December 31, 2002. A business day is any day other than a Saturday, Sunday or bank holiday. |
| | Dividends accrue in each quarterly period from the first day of such period, whether or not dividends are paid with respect to the preceding period. Dividends on the Series A preferred securities are not cumulative and, accordingly, if we do not declare a dividend or declare less than a full dividend on the Series A preferred securities for a quarterly dividend period, holders of the Series A preferred securities will have no right to receive a dividend or the full dividend, as the case may be, for that period, and we will have no obligation to pay a |

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| | dividend for that period, whether or not dividends are declared and paid for any future period with respect to either the Series A preferred securities, other series of preferred securities or our common stock. If the full dividend is not paid on the Series A preferred securities for a quarterly dividend period, the payment of dividends on our common stock (100% of which will be owned collectively by Wachovia and Wachovia Preferred Holding) and other preferred securities ranking subordinate to the Series A preferred securities will be prohibited for that period and at least the following three quarterly dividend periods. |
| **Liquidation Preference** | The liquidation preference for each Series A preferred security is $25.00, plus an amount equal to any authorized, declared, but unpaid dividends, if any. The Bank through Wachovia Preferred Holding may cause us to liquidate, dissolve or wind up at any time. |
| **Redemption** | The Series A preferred securities are not redeemable prior to December 31, 2022, except upon the occurrence of a Special Event which may be a Tax Event, an Investment Company Act Event or a Regulatory Capital Event. On and after December 31, 2022, the Series A preferred securities may be redeemed for cash at our option, with the prior approval of the OCC, in whole or in part, at any time and from time to time, at a redemption price of $25.00 per security, plus authorized, declared, but unpaid dividends, if any. Upon the occurrence of a Special Event, we will have the right prior to December 31, 2022, with the prior approval of the OCC, to redeem the Series A preferred securities in whole, but not in part, at a redemption price of $25.00 per security, plus authorized, declared, but unpaid dividends, if any. The Series A preferred securities are not subject to any sinking fund or mandatory redemption and are not convertible into any of our other securities. |
| **Conditional Exchange** | Each Series A preferred security will automatically be exchanged at the direction of the OCC upon the occurrence of a Supervisory Event for one depositary share representing a one-sixth interest in one share of Wachovia Series G, Class A preferred stock. Each depositary share will represent a one-sixth interest in the Wachovia Series G, Class A preferred stock and will: |
| | rank equal to the most senior preferred stock of Wachovia then outstanding; |

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pay dividends at the rate of 7.25% per annum of the liquidation preference of $25.00 per depositary share, if, when, and as declared by Wachovia s board of directors;

have a liquidation preference of $25.00 per depositary share;

be non-cumulative and non-voting;

be redeemable on the same terms as the Series A preferred securities; and

be evidenced by a depositary receipt.

**Voting Rights**

Holders of the Series A preferred securities are entitled to 1/10th of one vote per security on all matters submitted to a vote of the holders of our common stock. Without the consent of holders of two-thirds of the Series A preferred securities, voting as a separate class, we will not:

amend, alter or repeal our certificate of incorporation in a manner that materially and adversely affects the terms of the Series A preferred securities;

effect a consolidation or merger with or into another entity other than an entity controlled by, or under common control with, the Bank unless certain conditions have been met; or

approve the issuance of any Senior Stock.

Holders of the Series A preferred securities, voting together as a class with the holders of any Parity Stock with the same voting rights, will also have the right to elect two directors in addition to the directors then in office if we fail to pay, or declare and set aside for payment, dividends on the Series A preferred securities for six quarters. The term of such additional directors will terminate when we pay for three consecutive quarters and pay or declare and set aside for payment for the fourth consecutive quarter dividends on the Series A preferred securities or, if earlier, upon the redemption of all Series A preferred securities or a Conditional Exchange.

Holders of depositary shares representing Wachovia Series G, Class A preferred stock will not have voting rights.

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**Covenants**

Our certificate of incorporation provides certain covenants in favor of the holders of the Series A preferred securities. Specifically we will not, except with the consent or affirmative vote of the holders of at least two thirds of the Series A preferred securities, voting as a separate class:

make or permit to be made any payment to the Bank or its affiliates relating to our indebtedness or beneficial interests in us when we are precluded, as described under Dividends above, from making payments in respect of our common stock and all other stock ranking subordinate to our Series A preferred securities, which we refer to as Junior Stock , or make such payment or permit such payment to be made in anticipation of any liquidation, dissolution or winding up;

at any time incur indebtedness in an aggregate amount exceeding 20% of our shareholders equity;

pay dividends on our common stock or other Junior Stock unless our funds from operations, or FFO, for the four prior fiscal quarters equals or exceeds 150% of the amount that would be required to pay full annual dividends on the Series A preferred securities as well as any other Parity Stock, except as may be necessary to maintain our status as a REIT;

make any payment of interest or principal with respect to our indebtedness to the Bank or its affiliates unless our FFO for the four prior fiscal quarters equals or exceeds 150% of the amount that would be required to pay full annual dividends on the Series A preferred securities as well as any other Parity Stock, except as may be necessary to maintain our status as a REIT;

amend or otherwise change our policy of reinvesting the proceeds of our assets in other interest-earning assets such that our FFO over any period of four fiscal quarters will be anticipated to equal or exceed 150% of the amount that would be required to pay full annual dividends on the Series A preferred securities as well as any other Parity Stock, except as may be necessary to maintain our status as a REIT;

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| | issue any additional shares of common stock to anyone other than the Bank or its affiliates; or |
| | remove Wachovia from our name unless the name of either the Bank or Wachovia changes and we need to make a change to our name to be consistent with the new group name. |
| | Wachovia s articles of incorporation do not contain similar covenants regarding the Series G, Class A preferred stock. |
| **Transfer Restrictions** | Our certificate of incorporation prohibits any transfer of shares or securities that would result in more than 50% in value of our outstanding shares of capital stock being owned by five or fewer individuals, under the applicable attribution rules of the Code, or that would cause our shares of capital stock to be beneficially owned by fewer than 100 persons. This prohibition is necessary to maintain our status as a REIT. Any transfer of Series A preferred securities that would violate this prohibition will be null and void and the purported transferee will acquire no rights or economic interest in such Series A preferred securities. |
| **Listing** | We have applied for the listing of the Series A preferred securities on the New York Stock Exchange under the symbol WNA Pr . Trading in the Series A preferred securities is expected to commence not later than 30 days after the date of delivery of the Series A preferred securities. Consequently, there will be no trading market for the Series A preferred securities, at least in the short term. We do not anticipate that the depositary shares representing interests in Wachovia Series G, Class A preferred stock to be issued in the event of a Conditional Exchange will be listed on any securities exchange or quotation system. |
| **Use of Proceeds** | Prior to this offering, Wachovia Preferred Holding will acquire from us 30,000,000 Series A, 40,000,000 Series B and 4,233,754 Series C preferred securities in exchange for participation interests, with an aggregate fair market value of $6.0 billion, in certain commercial and commercial real estate loans. Wachovia Preferred Holding will subsequently sell the 18,000,000 Series A preferred securities offered hereby to the public for cash consideration of $25.00 per security. Wachovia Preferred Holding will receive all proceeds from this offering and will pay all expenses of and underwriting discounts and commissions associated with this offering. |

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| | Wachovia Preferred Holding intends to use the net proceeds from this offering for general corporate purposes. |
| | The pro forma condensed consolidated financial information included under Unaudited Pro Forma Condensed Consolidated Financial Information reflects, on a pro forma basis as of and for the nine months ended September 30, 2002, the assets we will acquire in connection with the issuance of the Series A, Series B and Series C preferred securities. |
| **Tax Consequences** | As long as we qualify as a REIT, corporate holders of the Series A preferred securities will not be entitled to a dividends-received deduction for any income recognized from the Series A preferred securities. |
| | Additionally, if the Series A preferred securities are exchanged for Wachovia Series G, Class A preferred stock, the exchange would most likely be a taxable event to holders of the Series A preferred securities. |
| | See Federal Income Tax Considerations . |
| **Settlement** | We expect that delivery of the Series A preferred securities will be made to investors through the facilities of The Depository Trust Company on or about December 16, 2002. |
| **ERISA Considerations** | If you are a fiduciary of a pension, profit-sharing or other employee benefit plan subject to Title I of the Employee Retirement Income Security Act of 1974, as amended ( ERISA ), or Section 4975 of the Code, you should consider the requirements of ERISA and the Code in the context of the plan s particular circumstances and ensure the availability of an applicable exemption before authorizing an investment in the Series A preferred securities (and the depositary shares representing the Wachovia Series G, Class A preferred stock into which the Series A preferred securities are exchangeable upon the occurrence of a Conditional Exchange). See ERISA Considerations . |

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## RISK FACTORS

*You should consider carefully the following risks before purchasing our Series A preferred securities, conditionally exchangeable into depositary shares representing interests in Wachovia s Series G, Class A preferred stock.*

*All of the financial information in this section is presented on a pro forma basis to reflect the following:*

- *$866 million of participation interests in home equity loans received by us as collateral for an intercompany loan to the Bank in October 2002. The underlying home equity loans were originated by the Bank; and*

- *the issuance of three new series of preferred securities (Series A, B and C) to Wachovia Preferred Holding in exchange for participations in commercial and commercial real estate loans prior to this offering. The commercial and commercial real estate loans were originated by the Bank and contributed to Wachovia Preferred Holding. We will issue the preferred securities to Wachovia Preferred Holding in exchange for participations in the loans prior to this offering.*

**Risks Relating to the Terms of the Series A Preferred Securities.**

*Dividends are not cumulative and you are not entitled to receive dividends unless authorized and declared by our board of directors.*

Dividends on the Series A preferred securities are not cumulative. Consequently, if our board of directors does not declare a dividend on the Series A preferred securities for any quarterly period, you will not be entitled to receive that dividend whether or not funds are or subsequently become available. Our board of directors may determine that it would be in our best interests to pay less than the full amount of the stated dividends on the Series A preferred securities or no dividends for any quarter even though funds are available. Factors that would generally be considered by our board of directors in making this determination are the amount of our distributable funds, our financial condition and capital needs, the impact of current and pending legislation and regulations, economic conditions, tax considerations, and our continued qualification as a REIT. If we fail to pay, or declare and set aside for payment, dividends on the Series A preferred securities for six quarters, the holders of the Series A preferred securities, voting together as a class with the holders of other stock ranking on parity with our Series A preferred securities, which we refer to as Parity Stock , with the same voting rights, will have the right to elect two directors in addition to those already on the board.

*The Series A preferred securities solely represent an interest in us and are not the obligation of, or guaranteed by, any other entity.*

The Series A preferred securities do not constitute obligations or equity securities of Wachovia, the Bank, or any other entity, nor are our obligations with respect to the Series A preferred securities guaranteed by any other entity. In particular, none of Wachovia, the Bank, or any other entity guarantees that we will declare or pay any dividends nor are they obligated to provide additional capital or other support to us to enable us to pay dividends in the event our assets and results of operations are insufficient for such purpose. The Series A preferred securities are not exchangeable for Wachovia preferred stock except in connection with a Supervisory Event. No holder of Series A preferred securities will have the right to require us to exchange such holder s Series A preferred securities for depositary shares of Wachovia.

*A decline in the Bank s capital levels may result in your Series A preferred securities being exchanged for depositary shares representing Wachovia preferred stock and such exchange is likely to occur at a time when the Bank s and Wachovia s financial condition has deteriorated.*

The returns from your investment in the Series A preferred securities will be dependent to a significant extent on the performance and capital of the Bank. A decline in the performance and capital levels of the Bank

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or the placement by the OCC of the Bank into conservatorship or receivership could result in the automatic exchange of each Series A preferred security for one depositary share representing a one-sixth interest in one share of Wachovia Series G, Class A preferred stock, which would represent an investment in Wachovia and not in us. Under these circumstances:

- you would become a preferred shareholder of Wachovia at a time when the Bank s and, ultimately, Wachovia s financial condition has deteriorated or when the Bank may have been placed into conservatorship or receivership and, accordingly, it is unlikely that Wachovia would be in a financial position to make any dividend payments on Wachovia preferred stock;

- in the event of a liquidation of Wachovia, the claims of depositors and creditors of Wachovia would be entitled to priority in payment over the claims of holders of equity interests such as the depositary shares representing Wachovia Series G, Class A preferred stock, and, therefore, you may receive substantially less than you would receive had the Series A preferred securities not been exchanged for the depositary shares;

- the exchange of the Series A preferred securities for depositary shares representing Wachovia Series G, Class A preferred stock would most likely be a taxable event to you under the Code, and in that event you would incur a gain or loss, as the case may be, measured by the difference between your basis in the Series A preferred securities and the fair market value of depositary shares representing Wachovia Series G, Class A preferred stock received in the exchange; and

- although the terms of the Wachovia Series G, Class A preferred stock are substantially similar to the terms of our Series A preferred securities, there are differences that you might deem to be important, such as the fact that holders of depositary shares representing Wachovia Series G, Class A preferred stock will not have any voting rights, any right to elect additional directors regardless of whether dividends are paid and will not benefit from any covenants. In addition, neither the Wachovia Series G, Class A preferred stock nor the depositary shares representing an interest in that stock will be listed on any securities exchange.

*We may liquidate, dissolve or wind up at any time without your approval or consent.*

Our certificate of incorporation provides that, subject to the terms of the capital stock we have outstanding at the time, we may liquidate, dissolve or wind up upon the affirmative vote of a majority of our Independent Directors. However, since the Series A preferred securities will not have voting rights as a separate class with respect to these matters, Wachovia Preferred Holding, which will be the holder of substantially all of our common stock, will have control over our liquidation, dissolution or winding up. Although Wachovia Preferred Holding has no present intention to cause such an event to occur, there can be no assurance that it will not cause us to liquidate, dissolve or wind up at any time or for any reason. If such an event were to occur, you may not be able to invest your liquidation proceeds in securities with a dividend yield comparable to that of the Series A preferred securities.

*The holders of Series A preferred securities have limited voting rights.*

Holders of Series A preferred securities are entitled to 1/10th of one vote per security on all matters to be voted on by all our shareholders. Immediately after the offering, Wachovia and its affiliates will have the right to vote approximately 98% of all votes and the holders of Series A preferred securities not affiliated with Wachovia will have the right to vote less than 2% of all votes on any matter to be voted on by all our shareholders. In addition, each of Wachovia Preferred Holding and the holders of Series A preferred securities not affiliated with Wachovia will have the right to vote 60% of all votes on any matter which requires the holders of Series A preferred securities to vote separately as a single class. The consent or vote of the holders of at least two-thirds of the outstanding Series A preferred securities is required for an adoption of any matter on which the holders of Series A preferred securities have a right to vote separately as a single class. See Description of the Series A Preferred Securities Voting Rights .

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*We may redeem the Series A preferred securities upon the occurrence of a Special Event.*

At any time following the occurrence of a Special Event, even if such Special Event occurs prior to December 31, 2022, we will have the right to redeem the Series A preferred securities in whole, subject to the prior written approval of the OCC. The occurrence of such a Special Event will not, however, give a shareholder any right to request that the Series A preferred securities be redeemed. There are three types of Special Events: Tax Events, Investment Company Events and Regulatory Capital Events.

A Tax Event occurs when we receive an opinion of counsel to the effect that, as a result of a judicial decision or administrative pronouncement, ruling, or other action or as a result of certain changes in the tax laws, regulations, or related interpretations, there is a significant risk that dividends with respect to our capital stock will not be fully deductible by us or we will be subject to additional taxes or governmental charges.

An Investment Company Event occurs when we receive an opinion of counsel to the effect that, as a result of certain changes in the applicable laws, regulations, or related interpretations, there is a significant risk that we will be considered an investment company under the Investment Company Act of 1940 (the Investment Company Act ).

A Regulatory Capital Event occurs when, as a result of certain changes in the applicable laws, regulations, or related interpretations, there is a significant risk that our Series A preferred securities will no longer constitute Tier 1 capital of the Bank or Wachovia.

If we redeem the Series A preferred securities, you may not be able to invest your redemption proceeds in securities with a dividend yield comparable to that of the Series A preferred securities.

*The Series A preferred securities will rank subordinate to claims of our creditors and on a parity with our Series B and D preferred securities and any other Parity Stock we may issue.*

The Series A preferred securities will rank subordinate to all claims of our creditors. The Series A, B and D preferred securities will rank on parity with each other with respect to dividend rights and upon our liquidation, dissolution or winding up. In addition, we may issue additional Parity Stock at any time in the future without your consent or approval but upon the approval of a majority of our Independent Directors. Accordingly, if

we do not have funds legally available to pay full dividends on the Series A, B and D preferred securities and any other Parity Stock we may issue; or

in the event of our liquidation, dissolution or winding up, we do not have funds legally available to pay the full liquidation value of the Series A, B and D preferred securities and any other Parity Stock,

any funds that are legally available to pay such amounts will be paid *pro rata* to the Series A, B and D preferred securities and any other Parity Stock outstanding. See Description of Other Wachovia Funding Capital Stock Preferred Stock Series B Preferred Securities and Series D

Preferred Securities .

*There has never been a market for the Series A preferred securities.*

Prior to this offering, there has been no public market for the Series A preferred securities. We have applied for the listing of the Series A preferred securities on the New York Stock Exchange under the symbol WNA Pr . Trading in the Series A preferred securities is expected to commence not later than 30 days after the date of delivery of the Series A preferred securities. Consequently, there will be no trading market for the Series A preferred securities, at least in the short term. We cannot assure you that an active and liquid trading market for the Series A preferred securities will develop or be sustained. If such a market were to develop, the prices at which the Series A preferred securities trade would depend on many factors, including prevailing interest rates, our operating results, and the market for similar securities. You may not be able to resell your Series A preferred securities at or above the initial price to the public or at all.

**Risks Relating to Our Status as a REIT.**

*We would suffer adverse tax consequences if we fail to qualify as a REIT.*

Although we currently conduct our operations so as to qualify as a REIT under the Code, we may not be able to continue to qualify as a REIT. Qualification as a REIT involves the application of highly technical and complex tax law provisions for which there are only limited judicial or administrative interpretations and involves the determination of various factual matters and circumstances not entirely within our control. No assurance can be given that new legislation or new regulations, administrative interpretations, or court decisions will not significantly change the tax laws in the future with respect to qualification as a REIT or the Federal income tax consequences of such qualification in a way that would materially and adversely affect our ability to operate. Any such new legislation, regulation, interpretation or decision could be the basis of a Tax Event that would permit us to redeem the Series A preferred securities. See Description of the Series A Preferred Securities Redemption .

If we were to fail to qualify as a REIT, the dividends on our preferred stock, including the Series A preferred securities, would not be deductible by us for Federal income tax purposes, and we would likely become part of the consolidated group of which the Bank is a member. Consequently, the consolidated group would face a greater tax liability which could result in a reduction in the Bank s net earnings after taxes. We would also become jointly and severally liable for the consolidated group s United States Federal income tax liabilities. A reduction in the Bank s net earnings after taxes could adversely affect the Bank s ability to raise additional capital, as well as its ability to generate additional capital internally, and consequently its ability to add interest-earning assets to its portfolio.

If in any taxable year we fail to qualify as a REIT, unless we are entitled to relief under certain statutory provisions, we would also be disqualified from treatment as a REIT for the four taxable years following the year our qualification was lost. As a result, the amount of funds available for distribution to our shareholders would be reduced for the year or years involved.

As a REIT, we generally will be required each year to distribute as dividends to our shareholders at least 90% of our REIT taxable income, excluding capital gains. Failure to comply with this requirement would result in our earnings being subject to tax at regular corporate rates. In addition, we would be subject to a 4% non-deductible excise tax on the amount by which certain distributions considered as paid by us with respect to any calendar year are less than the sum of:

85% of our ordinary income for the calendar year;

95% of our capital gains net income for the calendar year; and

100% of undistributed taxable income from prior periods.

We currently intend to operate in a manner designed to qualify as a REIT. However, future economic, market, legal, tax, or other considerations may cause us to determine that it is in our best interests and the best interests of holders of our common stock and preferred stock to revoke our

REIT election. As long as any Series A preferred securities are outstanding, any such determination by us may not be made without the approval of a majority of our Independent Directors.

*If ownership of our capital stock becomes concentrated in a small number of individuals, we may fail to qualify as a REIT.*

In order to maintain our qualification as a REIT under the Code, not more than 50% in value of our outstanding shares of capital stock may be owned, directly or constructively, by five or fewer individuals (as defined in the Code to include certain entities) at any time during the last half of a taxable year, and the shares of capital stock must be beneficially owned by 100 or more persons during at least 335 days of a taxable year of 12 months (or during a proportionate part of a shorter taxable year, other than the first 12 months as a REIT). Therefore, our certificate of incorporation contains provisions restricting the ownership and transfer of our preferred securities.

Our certificate of incorporation provides that a transfer of shares that would otherwise result in more than 50% in value of our outstanding shares of capital stock being owned by five or fewer individuals, under the applicable attribution rules of the Code, or which would cause our shares of capital stock to be beneficially owned by fewer than 100 persons, will be null and void and the purported transferee will acquire no rights or economic interest in such shares.

These transfer restrictions imposed by us could impair the liquidity of the Series A preferred securities and thereby affect the secondary market for the Series A preferred securities.

**Risks Associated with Our Business.**

*We are effectively controlled by Wachovia and our relationship with Wachovia and/or the Bank may create potential conflicts of interest.*

All of our officers and certain of our directors are also either officers or directors of Wachovia or the Bank or their affiliates. After this offering, Wachovia, the Bank and Wachovia Preferred Holding will continue to control a substantial majority of our outstanding voting shares. In effect, Wachovia, the Bank and Wachovia Preferred Holding will have the right to elect all of our directors, including Independent Directors, except under limited circumstances if we fail to pay dividends.

The Bank may have interests that are not identical to our interests. Wachovia, the owner of the Bank s common stock, may have investment goals and strategies that differ from those of the holders of the Series A preferred securities. Consequently, conflicts of interest between us, on one hand, and the Bank and/or Wachovia, on the other hand, may arise.

*We are dependent on the officers and employees of Wachovia and the Bank for the selection, structuring and monitoring of the loans in our portfolio and our relationship with Wachovia and/or the Bank may create potential conflicts of interest.*

Wachovia and the Bank are involved in virtually every aspect of our existence. The Bank administers our day-to-day activities under the terms of participation and servicing agreements between the Bank and us. We are dependent on the diligence and skill of the officers and employees of the Bank for the selection, structuring and monitoring of the loans in our portfolio and our other authorized investments.

This dependency and our close relationship with Wachovia and the Bank may create potential conflicts of interest. Specifically, such conflicts of interest may arise because the employees of Wachovia and the Bank (i) were directly involved in the decisions regarding the amount, type and price of loan participation interests and other assets acquired indirectly from the Bank prior to the offering, and (ii) will make decisions on the amount, type and price of future acquisitions of loan participation interests and other assets from the Bank as well as future dispositions of loan participation interests to the Bank or third parties.

*We are dependent on the officers and employees of the Bank for the servicing of the loans in our portfolio and our relationship with the Bank may create potential conflicts of interest.*

We are dependent on the Bank and others for the servicing of the loans in our portfolio. The Bank administers our day-to-day activities under the terms of participation and servicing agreements relating to our

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assets. These agreements contain terms which we believe are consistent with those resulting from arm s length negotiations and contain the following fees:

with respect to the commercial, commercial real estate and home equity loans, an annual service fee of 0.03% multiplied by the outstanding principal balance of each loan, and

with respect to residential mortgages, $48.00 per loan. Additionally, we are subject to Wachovia s management fee policy and thus reimburse Wachovia on a monthly basis for general overhead expenses.

Despite our belief that the terms of the loan participation and servicing agreements between the Bank and us reflect terms consistent with those negotiated on an arms-length basis, our dependency on the Bank s officers and employees and our close relationship with the Bank may create potential conflicts of interest. Specifically, such conflicts of interest may arise because the employees of the Bank have the power to set the amount of the service fees paid to the Bank, modify the loan participation and servicing agreements, and make business decisions with respect to servicing of the underlying loans, particularly the loans that are placed on non-accrual status or are otherwise non-performing.

*We are dependent on the officers and employees of the Bank for the management of the cash collateral related to the interest rate swaps and our relationship with the Bank may create potential conflicts of interest.*

Wachovia and the Bank are involved in virtually every aspect of our existence. The Bank manages our cash collateral related to the interest rate swaps. We are dependent on the diligence, skill and discretion of the officers and employees of the Bank for the selection and monitoring of the investments made with our cash collateral. This dependency and our close relationship with Wachovia and the Bank may create potential conflicts of interest.

*We are dependent on the officers and employees of the Bank for the identification and treatment of new business opportunities and our relationship with the Bank may create potential conflicts of interest.*

Wachovia and the Bank are involved in virtually every aspect of our existence. The employees of the Bank identify any new business opportunities for us and the Bank decides whether such opportunities are directed to us or other affiliates. As a result, we are dependent on the diligence, skill and discretion of the officers and employees of the Bank for the identification and treatment of new business opportunities and this dependency and our close relationship with Wachovia and the Bank may create potential conflicts of interest.

*Bank regulators may limit our ability to implement our business plan and may restrict our ability to pay dividends.*

Because we are an indirect subsidiary of the Bank, bank regulatory authorities will have the right to examine us and our activities and, under certain circumstances, to impose restrictions on the Bank or us that could impact our ability to conduct business pursuant to our business plan and that could adversely effect our financial condition and results of operations.

If the OCC, which is the Bank s primary regulator, determines that the Bank s relationship with us results in an unsafe and unsound banking practice, the Bank s regulators have the authority to:

restrict our ability to transfer assets;

restrict our ability to make distributions to our shareholders, including dividends to holders of the Series A preferred securities;

restrict our ability to redeem our preferred stock; or

require the Bank to sever its relationship with us or divest its ownership of us.

If the OCC determines that the Bank is operating with an insufficient level of capital, or that the payment of dividends by either the Bank or its subsidiaries is under the then present circumstances an unsafe and unsound banking practice, the OCC could restrict our ability to pay dividends.

Certain of these actions by the OCC would likely result in our failure to qualify as a REIT.

*If we lose our exemption under the Investment Company Act it could have a material adverse effect on us and would likely result in a redemption of the Series A preferred securities.*

We believe that we are not, and intend to conduct our operations so as not to become, regulated as an investment company under the Investment Company Act. Under the Investment Company Act, a non-exempt entity that is an investment company is required to register with the SEC and is subject to extensive, restrictive and potentially adverse regulation relating to, among other things, operating methods, management, capital structure, dividends and transactions with affiliates. The Investment Company Act exempts entities that, directly or through majority-owned subsidiaries, are primarily engaged in the business of purchasing or otherwise acquiring mortgages and other liens on and interests in real estate (which we refer to as Qualifying Interests ). Under current interpretations of the staff of the SEC, in order to qualify for this exemption, we, among other things, must maintain at least 55% of our assets in Qualifying Interests and also may be required to maintain an additional 25% in Qualifying Interests or other real estate-related assets. The assets that we may acquire therefore may be limited by the provisions of the Investment Company Act. We have established a policy of limiting authorized investments which are not Qualifying Interests to no more than 20% of the value of our total assets. The Investment Company Act does not treat cash and cash equivalents as either Qualifying Interests or other real estate-related assets.

Based on the criteria outlined above, we believe that, as of the time of this offering, our Qualifying Interests will be comprised of approximately 87% of the estimated fair market value of our total assets. As a result, we believe that we are not required to register as an investment company under the Investment Company Act. We do not intend, however, to seek an exemptive order, no-action letter or other form of interpretive guidance from the SEC or its staff on this position. If the SEC or its staff were to take a different position with respect to whether our assets constitute Qualifying Interests, we could be required either (a) to change the manner in which we conduct our operations to avoid being required to register as an investment company or (b) to register as an investment company, either of which could have a material adverse effect on us, the price of our securities and our ability to make payments in respect of the Series A preferred securities. Further, in order to ensure that we at all times continue to qualify for the above exemption from the Investment Company Act, we may be required at times to adopt less efficient methods of financing certain of our assets than would otherwise be the case and may be precluded from acquiring certain types of assets whose yield is somewhat higher than the yield on assets that could be purchased in a manner consistent with the exemption. The net effect of these factors may be to lower at times our net interest income. Finally, if we were an unregistered investment company, there would be a risk that we would be subject to monetary penalties and injunctive relief in an action brought by the SEC, that we would be unable to enforce contracts with third parties and that third parties could seek to obtain rescission of transactions undertaken during the period we were determined to be an unregistered investment company. In the event we are ever considered an investment company under the Investment Company Act as a result of an Investment Company Act Event, we would likely redeem the Series A preferred securities. See above under We may redeem the Series A preferred securities upon the occurrence of a Special Event .

*We have no control over changes in interest rates and such changes could negatively impact our financial condition, results of operations, and ability to pay dividends.*

Our income consists primarily of interest payments on the loans in our portfolio. At September 30, 2002, 14% of the loans in our portfolio, as measured by the aggregate outstanding principal amount, bore

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interest at fixed rates and the remainder bore interest at adjustable rates. Adjustable-rate loans decrease the risks to a lender associated with changes in interest rates but involve other risks. As interest rates rise, the payment by the borrower rises to the extent permitted by the terms of the loan, and the increased payment increases the potential for default. At the same time, the marketability of the underlying property may be adversely affected by higher interest rates. In a declining interest rate environment, there may be an increase in prepayments on the loans in our portfolio as the borrowers refinance their mortgages at lower interest rates. Under these circumstances, we may find it more difficult to purchase additional participation interests with rates sufficient to support the payment of the dividends on the Series A preferred securities. A declining interest rate environment would adversely affect our ability to pay full, or even partial, dividends on the Series A preferred securities.

*The loans in our portfolio are subject to economic conditions that could negatively affect the value of the collateral securing such loans and/or the results of our operations.*

The value of the collateral underlying our loans and/or the results of our operations could be affected by various conditions in the economy, such as:

- local and other economic conditions affecting real estate and other collateral values;
- sudden or unexpected changes in economic conditions, including changes that might result from terrorist attacks and the United States response to such attacks;
- the continued financial stability of a borrower and the borrower s ability to make loan principal and interest payments, which may be adversely affected by job loss, recession, divorce, illness or personal bankruptcy;
- the ability of tenants to make lease payments;
- the ability of a property to attract and retain tenants, which may be affected by conditions such as an oversupply of space or a reduction in demand for rental space in the area, the attractiveness of properties to tenants, competition from other available space, and the ability of the owner to pay leasing commissions, provide adequate maintenance and insurance, pay tenant improvement costs, and make other tenant concessions;
- interest rate levels and the availability of credit to refinance loans at or prior to maturity; and
- increased operating costs, including energy costs, real estate taxes, and costs of compliance with environmental controls and regulations.

*The loans in our portfolio are concentrated in five states, and adverse conditions in those states, in particular, could negatively impact our operations.*

At September 30, 2002, 71% (as a percentage of loan principal balances) of the assets in our portfolio were located in Florida, North Carolina, Pennsylvania, New Jersey and Virginia. Because of the concentration of our interests in those states, in the event of adverse economic conditions in those states, we would likely experience higher rates of loss and delinquency on our loan portfolio than if the underlying loans were more geographically diversified. Additionally, the loans in our portfolio may be subject to a greater risk of default than other comparable loans in the event of adverse economic, political, or business developments or natural hazards that may affect Florida, North Carolina, Pennsylvania, New Jersey or Virginia, and the ability of property owners or commercial borrowers in those states to make payments of principal and interest on the underlying loans. In the event of any adverse development or natural disaster, our ability to pay dividends on the Series A preferred securities could be adversely affected.

*Our acquisitions of participation interests in commercial and commercial mortgage loans subjects us to risks that are not present in our portfolio of residential mortgage loans, including the fact that some commercial loans are unsecured.*

As of September 30, 2002, 84% of our assets, as measured by aggregate outstanding principal amount, consisted of participation interests in commercial and commercial real estate loans. Commercial and

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commercial real estate loans generally tend to have shorter maturities than residential mortgage loans and may not be fully amortizing, meaning that they may have a significant principal balance or balloon payment due on maturity. Commercial real estate properties tend to be unique and are more difficult to value than single-family residential real estate properties. They are also subject to relatively greater environmental risks and to the corresponding burdens and costs of compliance with environmental laws and regulations. In addition, some of our commercial loans are unsecured. Such unsecured loans are more likely than loans secured by real estate or personal property collateral to result in a loss upon a default.

*We cannot assure you that we paid the Bank fair value for all of our assets because we have not obtained any third party valuation of all those assets. Nor can we assure you that we will acquire or dispose of assets in the future at their fair market value.*

We have adopted policies with a view to ensuring that all financial dealings between the Bank and us will be fair to both parties and consistent with market terms. However, there has been no third party valuation of all our assets. In addition, it is not anticipated that third party valuations will be obtained in connection with future acquisitions or dispositions of assets even in circumstances where an affiliate of ours is selling the assets to us, or purchasing the assets from us. Accordingly, we cannot assure you that the purchase price we paid for all of our assets was equal to the fair value of those assets. Nor can we assure you that the consideration to be paid by us to, or received by us from, the Bank or any of our affiliates in connection with future acquisitions or dispositions of assets will be equal to the fair value of such assets.

*We could incur losses as a result of environmental liabilities of properties underlying our assets through foreclosure action.*

We may be forced to foreclose on an underlying commercial, commercial real estate or residential loan where the borrower has defaulted on its obligation to repay the loan. It is possible that we may be subject to environmental liabilities with respect to foreclosed property, particularly industrial and warehouse properties, which are generally subject to relatively greater environmental risks than non-commercial properties. The discovery of these liabilities and any associated costs for removal of hazardous substances, wastes, contaminants, or pollutants, could have a material adverse effect on the fair value of such loan and therefore we may not recover any or all of our investment in the underlying commercial, commercial real estate or residential loan.

*We do not have insurance to cover our exposure to borrower defaults and bankruptcies and special hazard losses that are not covered by standard insurance.*

Generally, neither we nor the Bank obtain credit enhancements such as borrower bankruptcy insurance or obtain special hazard insurance for the loans in our portfolio, other than standard hazard insurance typically required by the Bank, which relates only to individual loans. Without third party insurance, we are subject to risks of borrower defaults and bankruptcies and special hazard losses that are not covered by standard hazard insurance.

*Delays in liquidating defaulted loans could occur which could cause our business to suffer.*

Substantial delays could be encountered in connection with the liquidation of the collateral securing defaulted loans in our portfolio, with corresponding delays in our receipt of related proceeds. An action to foreclose on a mortgaged property or repossess and sell other collateral securing a loan is regulated by state statutes and rules. Any such action is subject to many of the delays and expenses of lawsuits, which may impede our ability to foreclose on or sell the collateral or to obtain proceeds sufficient to repay all amounts due on the related loan in our portfolio.

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*We may invest in assets which involve new risks and need not maintain the current asset coverage.*

Although our portfolio currently consists primarily of commercial, commercial real estate and residential loan interests, and we presently intend to reinvest proceeds of such interests in similar assets, we are not required to limit our investments to assets of the types currently in our portfolio. Assets such as mortgage-backed securities, equipment loans or real estate may involve different risks not described in this prospectus. Nevertheless, we will not invest in assets that are not REIT Qualified Assets if such investments would cause us to violate the requirements for taxation as a REIT. Moreover, while our policies will call for maintaining specified levels of funds from operations coverage as to expected dividend distributions, we are not required to maintain the levels of asset coverage that currently exist.

**Risk Factors Applicable Only to Wachovia Depositary Shares Representing the Wachovia Series G, Class A Preferred Stock Issued upon the Occurrence of a Conditional Exchange.**

*You may have adverse tax consequences as a result of a Conditional Exchange.*

The exchange of our Series A preferred securities for depositary shares representing an interest in Wachovia Series G, Class A preferred stock would most likely be a taxable event to you under the Code, and you would incur a gain or loss, as the case may be, measured by the difference between your basis in our Series A preferred securities and the fair market value of the depositary shares.

*A decline in Wachovia s financial condition may restrict its ability to pay dividends and could result in a loss on your investment.*

If Wachovia s financial condition were to deteriorate, the holders of the depositary shares representing the Wachovia Series G, Class A preferred stock could suffer direct and materially adverse consequences, including suspension of the payment of non-cumulative dividends on the Wachovia Series G, Class A preferred stock and, if a liquidation, dissolution or winding up of Wachovia were to occur, loss by holders of depositary shares of all or part of their investment. See Description of Wachovia Series G, Class A Preferred Stock .

*A Conditional Exchange may be based on the Bank s receivership, which could lead to Wachovia s receivership and would mean that others may have liquidation claims senior to yours.*

A Supervisory Event triggering a Conditional Exchange will occur if the Bank is placed into conservatorship or receivership. The Bank s conservatorship or receivership could lead to Wachovia being placed into conservatorship or receivership. In the event of Wachovia s receivership, the claims of Wachovia s secured, senior, general and subordinated creditors would be entitled to a priority of payment over the claims of holders of equity interests such as the Wachovia Series G, Class A preferred stock. As a result of such subordination, either if Wachovia were to be placed into receivership after a Conditional Exchange or if a Conditional Exchange were to occur after Wachovia s receivership, the holders of the depositary shares would likely receive, if anything, substantially less than they would have received had our Series A preferred securities not been exchanged.

*Upon the occurrence of a Conditional Exchange, the holders of the depositary shares will not have any voting rights, the right to elect Independent Directors nor have the benefit of the same favorable covenants as the Series A preferred securities.*

Upon the occurrence of a Conditional Exchange, the holders of the depositary shares representing Wachovia Series G, Class A preferred stock will not have voting rights, the right to elect Independent Directors if dividends are not authorized and declared by Wachovia s board of directors nor have the benefit of the same favorable covenants as the Series A preferred securities. Therefore, Wachovia may authorize and issue additional shares of preferred stock that may rank junior to, on parity with or senior to the Series G, Class A preferred stock as to dividend rights and rights upon liquidation, winding up, or dissolution without the consent of the holders of the Series G, Class A preferred stock.

*Wachovia is not obligated to pay, and is subject to certain limitations on the payment of, dividends on the Wachovia Series G, Class A preferred stock and dividends on these securities are not cumulative.*

Dividends on the Wachovia Series G, Class A Preferred stock are not cumulative. Consequently, if Wachovia s board of directors does not declare dividends on the Wachovia Series G, Class A preferred stock for any quarterly period, the holders of the Wachovia Series G, Class A preferred stock and the depositary shares represented thereby would not be entitled to any such dividend whether or not funds are or subsequently become available. Under an indenture between Wachovia and Wilmington Trust Company, as trustee, Wachovia has agreed not to pay any dividends on, or make a liquidation payment relating to, any of Wachovia s common stock or preferred stock, including its Series G, Class A preferred stock, if, at that time, there is a default under the indenture or a related Wachovia guarantee or Wachovia has delayed interest payments on trust preferred securities issued under the indenture. Currently, there are $1.3 billion aggregate principal amount of trust preferred securities outstanding under such indenture.

The Wachovia board of directors may determine that it would be in Wachovia s best interests to pay less than the full amount of the stated dividends on the Wachovia Series G, Class A preferred stock or no dividends for any quarter even if funds are available. Factors that would be considered by the Wachovia board of directors in making this determination are Wachovia s financial condition and capital needs, the impact of current and pending legislation and regulations, economic conditions, tax considerations, and such other factors as the board of directors may deem relevant. In addition, as a bank holding company, Wachovia is subject to various general regulatory policies and requirements relating to the payment of dividends, including requirements to maintain adequate capital above regulatory minimums. The Federal Reserve Board is authorized to determine, under certain circumstances relating to the financial condition of a bank holding company, such as Wachovia, that the payment of dividends would be an unsound and unsafe practice and to prohibit payment thereof. See Description of Wachovia Series G, Class A Preferred Stock Dividends .

*There is no active trading market for the Wachovia Series G, Class A preferred stock or the depositary shares representing that stock and no such trading market may develop.*

The Wachovia Series G, Class A preferred stock and the depositary shares representing that stock will be new issues of securities. Prior to this offering, there has been no public market for the Wachovia Series G, Class A preferred stock or the depositary shares. Wachovia does not intend to cause the listing or quotation of the Wachovia Series G, Class A preferred stock or the depositary shares representing an interest in that stock on the New York Stock Exchange or on any other national securities exchange or quotation system on which the Series A preferred securities are then listed or quoted. Consequently, it is unlikely that an active and liquid trading public market for the depositary shares or the underlying Wachovia Series G, Class A preferred stock will develop or be maintained. The lack of liquidity and an active trading market could adversely affect your ability to dispose of the depositary shares representing an interest in the Wachovia Series G, Class A preferred stock.

## INFORMATION CONCERNING THE BANK

### General

The Bank is a national banking association organized under the laws of the United States and with its principal office in Charlotte, North Carolina. The Bank offers a wide range of domestic and international , retail and commercial banking and trust services. At September 30, 2002, the Bank operated 2,769 branches in Connecticut, Florida, Georgia, Maryland, New Jersey, New York, North Carolina, Pennsylvania, South Carolina, Virginia and Washington, D.C., and in several foreign countries. At September 30, 2002, the Bank had total assets of $312 billion, total liabilities of $280 billion and total shareholders equity of $32 billion. On April 1, 2002, the former Wachovia Bank, National Association merged with and into First Union National Bank, and First Union National Bank changed its name to Wachovia Bank, National Association . Presentation of certain financial information in this prospectus for periods prior to April 1, 2002, will be for First Union National Bank only.

The Series A preferred securities will be exchangeable, without your approval or any action on your part, for depositary shares representing interests in the Wachovia Series G, Class A preferred stock if the OCC so directs under the following circumstances, each of which is referred to as a Supervisory Event:

- the Bank becomes undercapitalized under prompt corrective action regulations,
- the Bank is placed into conservatorship or receivership, or
- the OCC, in its sole discretion, anticipates that the Bank may become undercapitalized in the near term or takes supervisory action that limits the payment of dividends by us and in connection therewith directs an exchange.

The Series A preferred securities are exchangeable only for the depositary shares. Under no circumstances will you ever receive securities of the Bank upon the occurrence of a Supervisory Event or for any other reason.

### Capital Adequacy

The OCC has issued regulations addressing the capital adequacy of national banks. Under these regulations, capital adequacy is measured by three different ratios: a ratio of total capital to risk-weighted assets; a ratio of Tier 1 capital to risk-weighted assets; and a leverage ratio of Tier 1 capital to balance sheet assets. For purposes of determining risk-weighted assets for the risk-based capital ratios, the book value of each of the bank s on-balance sheet assets, and a portion of certain off-balance sheet items and exposures, are weighted from 0% to 100% based on broad categories. For instance, U.S. government debt obligations are generally risk weighted at 0%; residential real estate mortgage loans on one-to-four family dwellings are generally risk weighted at 50%; and commercial loans and most other assets are generally risk-weighted at 100%. Off-balance sheet items (including letters of credit, loan commitments, swaps and other derivatives) are converted into on-balance sheet equivalent amounts for risk-based capital purposes, then assigned a risk weight like other assets. Under amendments adopted in November 2001 and being phased in by year-end 2002, the capital risk weighting assigned to certain asset-backed securities may vary from 20% to 200% depending on credit rating. Subordinated residual interests retained in asset securitizations, credit enhancement and forms of recourse can result in higher capital charges. The sum of all risk-weighted assets are measured against total capital and Tier 1 capital to determine risk-based capital ratios. A bank s leverage ratio represents Tier 1 capital divided by average total on-balance sheet assets, without recognizing off-balance sheet exposures or applying risk weights. As noted below, to be considered adequately capitalized, a national bank generally must maintain a total risk-based capital ratio of at least 8%, a Tier 1 risk-based ratio of at least 4%, and a Tier 1 leverage ratio of at least 4% (or 3% in exceptional cases).

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For purposes of these regulations, total capital is defined as the sum of Tier 1 capital and Tier 2 capital. Tier 1 capital generally includes common shareholders equity; non-cumulative perpetual preferred stock and related surplus; and qualifying minority interests in the equity accounts of consolidated subsidiaries (which may include such instruments as qualifying REIT preferred stock and trust preferred stock). Tier 2 capital generally includes (subject to certain limits and sub-limits): cumulative perpetual preferred stock; limited-life preferred stock; Dutch auction and money market preferred stock; hybrid capital instruments (including certain mandatory convertible notes); term subordinated debt; the bank s allowance for loan and lease losses (up to a maximum of 1.25% of total risk-weighted assets); and up to 45% of the pretax net unrealized gains of available-for-sale equity securities investments. Tier 2 capital is permitted to count towards only one-half of total capital. In addition, limited-life instruments generally can represent not more than one-half of Tier 2 capital and are phased out of capital over the last five years before maturity. Deductions from Tier 1 capital include goodwill, certain other intangible assets, and deferred tax assets in excess of certain limits.

For national banks with large trading portfolios, a different method known as the Market Risk Measure is applied to determine the risk-based capital requirements for items booked in the trading account and for foreign exchange and commodity positions, wherever booked. Under the Market Risk Measure, capital requirements for these portfolios are based on value-at-risk calculations and certain other factors, and the result is combined into the bank s total risk-based capital ratio. For purposes of the Market Risk Measure only, a portion of a bank s total capital can consist of certain Tier 3 capital instruments subordinated two-year notes with lock-in clauses restricting payment of principal or interest (even at maturity) if the bank falls below required capital ratios.

Under the OCC s prompt corrective action regulations, issued pursuant to the Federal Deposit Insurance Corporation Improvement Act of 1991, national banks are placed into one of five capital categories, as follows:

1. Well capitalized banks:

   have a total risk-based capital ratio of 10% or greater;

   have a Tier 1 risk-based capital ratio of 6% or greater;

   have a leverage ratio of 5% or greater; and

   are not subject to any other OCC action directed at a specific level of capital.

2. Adequately capitalized banks:

   have a total risk-based capital ratio of 8% or greater;

   have a Tier 1 risk-based capital ratio of 4% or greater;

   have a leverage ratio of

(a) 4% or greater; or

(b) 3% or greater for certain exceptionally well managed and well run banks; and

do not meet the definition of well capitalized.

3. Undercapitalized banks:

have a total risk-based capital that is less than 8%;

have a Tier 1 risk-based capital ratio that is less than 4%; or

have a leverage ratio of less than 4% or, if the bank is exceptionally well managed and well run, less than 3%.

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4. Significantly undercapitalized banks:

   have a total risk-based capital ratio that is less than 6%;

   have a Tier 1 risk-based capital that is less than 3%; or

   have a leverage ratio that is less than 3%.

5. Critically undercapitalized banks:

   have a ratio of tangible equity capital (Tier 1 capital plus cumulative preferred stock less certain intangible capital) that is equal to or less than 2%.

Under prompt corrective action provisions, if a national bank becomes undercapitalized , significantly undercapitalized or critically undercapitalized , the OCC may undertake (and, in some cases, may be compelled by statute to undertake) a variety of actions of increasing severity. Among other things, an undercapitalized bank must submit an acceptable capital restoration plan and is generally restricted from paying dividends, redeeming stock or making other capital distributions. Failure to achieve the goals of a capital restoration plan could subject a bank to penalties and to being considered significantly undercapitalized . A significantly undercapitalized bank is subject to a broad range of restrictions, including restrictions on growth, limits on activities, divestiture requirements, limits on interest rates paid on deposits, restrictions on transactions with affiliates, limits on executive compensation, and mandated changes in directors or management. Critically undercapitalized banks face even stricter measures, including possible receivership.

In addition, the OCC from time to time may impose higher specific capital requirements on any national bank that is perceived to have risks, exposures, asset concentrations, rapid growth or other circumstances warranting special attention. Failure to satisfy such a capital directive could subject a bank to civil money penalties, judicial enforcement and administrative remedies available to the OCC, as well as a finding that the bank is undercapitalized .

A national bank s capital ratios are monitored through the quarterly reports of condition submitted by each national bank pursuant to 12 U.S.C. §181 (frequently referred to as call reports ). These call reports are filed with the Federal Deposit Insurance Corporation.

Whether the Bank would ever be determined by the OCC to be undercapitalized , or at risk of becoming undercapitalized in the near term thereby triggering the exchange of the Series A preferred securities into depositary shares representing Wachovia Series G, Class A preferred stock could be influenced not only by the OCC s capital adequacy regulations, but also by the regulator s interpretations and judgment on other matters. For example, the OCC s views on asset credit quality could potentially affect a bank s capital status. Among other things, the OCC typically evaluates asset quality, loan loss reserves and procedures during periodic regulatory examinations of each national bank. If, following such an examination or otherwise, the OCC in its discretion were to require the Bank to significantly increase its reserves against credit losses (*i.e.*, the allowance for loan and lease losses), this could potentially reduce the Bank s retained earnings and regulatory capital. As noted above, a bank s allowance for loan and lease losses is includible within Tier 2 capital only up to a limit, and is not includible at all in Tier 1 capital.

A bank s regulatory capital status, and the risk of being deemed undercapitalized also could be affected by other developments or by future changes in regulatory capital and other standards. The Banking Supervision Committee of the Bank for International Settlements (the Basel Committee ) has proposed for comment, and is continuing to study and revise, substantial changes to its 1988 Basel Accord on international bank capital adequacy. We and the Bank are unable to predict whether or when the Basel Committee s proposed new capital accord may be finalized, how the new accord might be interpreted and implemented by the OCC, or what impact any such new standards might have on the Bank and its capital status.

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The following table presents the capital ratios reported to the OCC by the Bank, as well as those of Wachovia, the Bank s parent company, compared to the standards for adequately capitalized and well capitalized status, as of the dates indicated.

| | | | Regulatory Standards | |
|---|---|---|---|---|
| | The Bank | Wachovia | Adequately Capitalized | Well Capitalized |
| **September 30, 2002** | | | | |
| Tier 1 capital | 7.63 | 8.11 | 4.00 | 6.00 |
| Total capital | 12.12 | 12.02 | 8.00 | 10.00 |
| Leverage | 6.61 | 6.82 | 4.00 | 5.00 |
| **December 31, 2001** | | | | |
| Tier 1 capital | 7.55 | 7.04 | 4.00 | 6.00 |
| Total capital | 11.68 | 11.08 | 8.00 | 10.00 |
| Leverage | 6.29 | 6.19 | 4.00 | 5.00 |
| **December 31, 2000** | | | | |
| Tier 1 capital | 6.92 | 7.02 | 4.00 | 6.00 |
| Total capital | 10.73 | 11.19 | 8.00 | 10.00 |
| Leverage | 6.04% | 5.92 | 4.00 | 5.00 |

The Bank currently intends to maintain its capital ratios in excess of the well capitalized levels under the prompt corrective action regulations. However, there is no guarantee that the Bank s capital ratios will be maintained in the future at their current or historical levels. Accordingly, there is no assurance that the Bank will not be deemed to be undercapitalized by the OCC in the future or that the Bank will not be placed in conservatorship or receivership in the future. Consequently, there can be no assurance that a Supervisory Event will not occur and that the Series A preferred securities will not be exchanged for depositary shares in the future. You should therefore carefully consider the description of the Wachovia Series G, Class A preferred stock set forth under the caption Description of Wachovia Series G, Class A Preferred Stock and the description of the depositary shares representing interests in that stock set forth under the caption Description of Wachovia Depositary Shares before investing in the Series A preferred securities.

Supplementary consolidating financial information for Wachovia, which includes certain financial information for the Bank as of and for the nine months ended September 30, 2002, and as of and for the years ended December 31, 2001 and 2000, is included in the prospectus beginning on page F-22. We will continue to provide annual unaudited financial information for the Bank on an ongoing basis in the reports we file under the Securities Exchange Act of 1934, as amended (the Exchange Act ). We will also continue to provide in those reports current unaudited capital and capital ratio information. Additional information regarding the Bank can be obtained on Wachovia s website, www.wachovia.com, but that information is not incorporated by reference in this prospectus.

**Benefits to the Bank and Wachovia**

The Bank has received confirmation from the OCC that proceeds from the public sale of Series A preferred securities will qualify as Tier 1 capital of the Bank under relevant regulatory capital guidelines. Those guidelines limit the inclusion of our Series A preferred securities, together with all other outstanding non-cumulative perpetual preferred securities, to 25% of the Bank s Tier 1 capital, with the balance treated as Tier 2 capital of the Bank. The Bank and Wachovia expect that as of December 31, 2002, all of the proceeds from the public sale of Series A preferred securities will qualify as Tier 1 capital of the Bank and Wachovia. The increase in the Bank s Tier 1 risk-based capital level that will result from the treatment of the Series A preferred securities as Tier 1 capital will enable the Bank to retain a higher base of interest-earning assets, resulting in incrementally higher related earnings.

## USE OF PROCEEDS

Prior to this offering, Wachovia Preferred Holding will acquire from us 30,000,000 Series A, 40,000,000 Series B and 4,233,754 Series C preferred securities with liquidation preferences of $25.00, $25.00, and $1,000 per security, respectively. Wachovia Preferred Holding will acquire these preferred securities in exchange for participation interests with an aggregate fair market value of $6.0 billion, calculated using a discounted cash-flow methodology, in certain commercial and commercial real estate loans originated by and acquired from the Bank. Wachovia Preferred Holding acquired these participation interests from the Bank in exchange for 2,400 newly issued shares of Wachovia Preferred Holding s common stock valued at $6.0 billion. We intend to hold these participation interests as long-term investments.

Wachovia Preferred Holding, a statutory underwriter, will subsequently sell the 18,000,000 Series A preferred securities offered hereby through an underwriting syndicate to the public for cash consideration of $25.00 per security. We will not receive any of the proceeds from the sale of our Series A preferred securities owned by Wachovia Preferred Holding. The proceeds, before expenses and commissions, to be received by Wachovia Preferred Holding from the sale of the 18,000,000 Series A preferred securities are expected to be $450 million in the aggregate. Wachovia Preferred Holding intends to use the net proceeds from this offering for general corporate purposes and will not use the proceeds to purchase additional assets for contribution to us.

The Series A preferred securities are being offered for sale to increase the Bank s and Wachovia s regulatory capital. The proceeds from the sale of the Series A preferred securities will be included as Tier 1 capital of the Bank and Wachovia under relevant regulatory capital guidelines.

Wachovia Preferred Holding will pay all expenses and underwriting discounts and commissions involved with the offering to the public.

The depositary shares each representing a one-sixth interest in a share of Series G, Class A preferred stock of Wachovia will be made available, if ever, in connection with a Conditional Exchange of our Series A preferred securities at the direction of the OCC following a Supervisory Event. Wachovia will not receive any proceeds, directly or indirectly, from the subsequent exchange of the Series A preferred securities for the depositary shares.

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## CAPITALIZATION

The following table sets forth our unaudited capitalization as of September 30, 2002, and as adjusted to reflect the issuance of our Series A, B and C preferred securities to Wachovia Preferred Holding.

| (In thousands) | September 30, 2002 Actual | September 30, 2002 Pro Forma |
|---|---|---|
| **Long-term debt** | $ | |
| **Stockholders equity** | | |
| Preferred stock | | |
| Series A preferred securities, $0.01 par value, $25.00 liquidation preference, non-cumulative and conditionally exchangeable, 30,000,000 shares authorized, issued and outstanding(1) | | 300 |
| Series B preferred securities, $0.01 par value, $25.00 liquidation preference, non-cumulative and conditionally exchangeable, 40,000,000 shares authorized, issued and outstanding | | 400 |
| Series C preferred securities, $0.01 par value, $1,000 liquidation preference, cumulative, 5,000,000 shares authorized, 4,233,754 shares issued and outstanding | | 42 |
| Series D preferred securities, $0.01 par value, $1,000 liquidation preference, non-cumulative, 913 shares authorized, issued and outstanding | | |
| Common stock, $0.01 par value, 100,000,000 shares authorized, 99,999,900 shares issued and outstanding | 1,000 | 1,000 |
| Paid-in capital | 5,086,474 | 11,519,803 |
| Retained earnings | 376,674 | 376,674 |
| Total stockholders equity | 5,464,148 | 11,898,219 |
| Total capitalization | $ 5,464,148 | 11,898,219 |

(1) Our Series A preferred securities are exchangeable, without the approval or any action on the part of the holder, for depositary shares representing one-sixth of a share of Series G, Class A preferred stock of Wachovia if such an exchange is directed by the OCC upon the occurrence of a Supervisory Event.

The following table sets forth the unaudited capitalization of Wachovia at September 30, 2002.

| (In millions) | September 30, 2002 |
|---|---|
| **Long-term debt** | $ 39,758 |

| | |
|---|---|
| **Stockholders equity** | |
| Dividend Equalization Preferred shares, issued 97 million shares | 2 |
| Common stock, authorized 3 billion shares, issued 1.373 billion shares | 4,577 |
| Paid-in capital | 18,233 |
| Retained earnings | 7,221 |
| Accumulated other comprehensive income, net | 2,072 |
| Total stockholders equity | 32,105 |
| Total capitalization | $ 71,863 |

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**RATIOS OF EARNINGS TO FIXED CHARGES**

The following table provides our consolidated ratio of earnings to fixed charges for the nine months ended September 30, 2002 and the year ended December 31, 2001. Data for the four years ended December 31, 2000, is not meaningful due to the immaterial amount of fixed charges in each of the four years.

| | Nine Months Ended September 30, 2002 | Year Ended December 31, 2001 |
|---|---|---|
| Pretax income (loss) from continuing operations | $ 181,824 | (36,224) |
| Fixed charges, excluding capitalized interest | 8,287 | 857 |
| Earnings (loss) | $ 190,111 | (35,367) |
| Interest | $ 8,287 | 857 |
| One-third of rents | | |
| Capitalized interest | | |
| Fixed charges | $ 8,287 | 857 |
| Consolidated ratios of earnings to fixed charges | 22.94x | n/m |

n/m not meaningful.

For purposes of computing the ratio in the table above, earnings represent income from continuing operations and fixed charges represent interest.

The following table provides Wachovia s consolidated ratios of earnings to fixed charges and preferred stock dividends.

| | Nine Months Ended September 30, | Years Ended December 31, | | | | |
|---|---|---|---|---|---|---|
| | 2002 | 2001 | 2000 | 1999 | 1998 | 1997 |
| **Consolidated Ratios of Earnings to Fixed Charges and Preferred Stock Dividends** | | | | | | |
| Excluding interest on deposits | 2.87x | 1.61 | 1.13 | 2.29 | 2.13 | 2.50 |
| Including interest on deposits | 1.79x | 1.27 | 1.06 | 1.62 | 1.51 | 1.57 |

For purposes of computing the ratios in the table above:

- earnings represent income from continuing operations before extraordinary items and cumulative effect of a change in accounting principles, plus income taxes and fixed charges (excluding capitalized interest);

- fixed charges, excluding interest on deposits, represent interest (including capitalized interest), one-third of rents and all amortization of debt issuance costs; and

- fixed charges, including interest on deposits, represent all interest (including capitalized interest), one-third of rents and all amortization of debt issuance costs.

One-third of rents is used because it is the proportion deemed representative of the interest factor.

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## BUSINESS

### General

We are a Delaware corporation, formed in July 2002 and the survivor of a merger with First Union Real Estate Asset Company of Connecticut, which was formed in 1996. By the completion of this offering, we will be a direct subsidiary of Wachovia Preferred Holding and Wachovia and an indirect subsidiary of the Bank. Wachovia Preferred Holding will own 99.85% of our common stock and Wachovia will own the remaining .15%. The Bank will own 99.95% of the common stock of Wachovia Preferred Holding and Wachovia will own the remaining 0.05%. Wachovia Preferred Holding will own 87.62% of our Series D preferred securities, while the remaining 12.38% is owned by 113 employees of Wachovia or its affiliates.

After our merger with First Union Real Estate Asset Company of Connecticut, we issued and sold 913 shares of our Series D preferred securities to Wachovia Realty Management Corporation, an affiliate of Wachovia. In a series of related corporate reorganization transactions that occurred in July 2002, Wachovia Realty Management Corporation merged with and into its parent, Wachovia Realty Management Holding Company, Inc., a Delaware corporation, with the then holders of its preferred securities (113 employees of Wachovia or its affiliates ) receiving Series D preferred securities as merger consideration. Wachovia Realty Management Holding Company, Inc. in turn merged with and into its parent, Wachovia Management Company, Inc., a Delaware corporation. Wachovia Management Company, Inc. then liquidated and distributed all of its assets, including the Series D preferred securities, to the Bank. As a result of this series of related corporate reorganization transactions, 87.62% of our Series D preferred securities are now owned by the Bank and the remaining 12.38% by 113 employees of Wachovia or its affiliates. Upon our merger with First Union Real Estate Asset Company of Connecticut, we were a direct subsidiary of the Bank and an indirect subsidiary of Wachovia. By the completion of this offering, we will be a direct subsidiary of Wachovia Preferred Holding as a result of the Bank transferring certain interests in mortgage assets and other authorized investments through a loan participation agreement, 99.85% of our common stock and 87.62% of our Series D preferred securities to Wachovia Preferred Holding in exchange for additional shares of Wachovia Preferred Holding common stock.

One of our subsidiaries, Wachovia Real Estate Investment Corp., was formed as a Delaware corporation in 1996 and has operated as a REIT since its formation. Of the 645 shares of Wachovia Real Estate Investment Corp. common stock outstanding, we own 644 shares or 99.84% and the remaining 1 share is owned by Wachovia. Of the 667 shares of preferred stock outstanding, we own 529.3 shares, 131 shares are owned by employees of Wachovia or its affiliates and 6.7 shares are owned by Wachovia.

Our other subsidiary, Wachovia Preferred Realty, LLC ( WPR ), was formed as a Delaware limited liability company in October 2002. Under the REIT Modernization Act, which became effective on January 1, 2001, a REIT is permitted to own taxable REIT subsidiaries which are subject to taxation similar to corporations that do not qualify as REITs or for other special tax rules. Our ownership of WPR provides us with additional flexibility by allowing us to hold assets which earn non-qualifying REIT income while maintaining our REIT status. Following formation of WPR, we transferred our interest-rate swaps and related cash collateral, including those described below, to WPR. We are the sole member of WPR.

In December 2001, the Bank contributed received-fixed interest rate swaps, commercial loans and commercial real estate loans to us in exchange for shares of our common stock. The swaps had a notional amount of $4.25 billion and a fair value of $673 million. The commercial and commercial real estate loans had a book value of $4.0 billion. Prior to this transaction, our consolidated assets primarily consisted of home equity loans and residential mortgage loans.

All of the financial information and other data in this section is presented on a pro forma basis to reflect the following:

$866 million of participation interests in home equity loans received by us as collateral for an intercompany loan to the Bank in October 2002. The underlying home equity loans were originated by the Bank; and the issuance of three new series of preferred securities (Series A, B and C) to Wachovia Preferred Holding in exchange for participations in commercial and commercial real estate loans prior to this offering. The commercial and commercial real estate loans were originated by the Bank and contributed to Wachovia Preferred Holding. We will issue the preferred securities to Wachovia Preferred Holding in exchange for participations in the loans prior to this offering.

Our principal business objective is to acquire, hold, and manage mortgage assets and other authorized investments that will generate net income for distribution to our stockholders. At September 30, 2002, we had total assets of $12.5 billion, total liabilities of $607 million, and stockholders equity of $11.9 billion. As of such date,

$9.8 billion, or 78.7% of our assets, were comprised of participation interests in commercial real estate loans;

$866 million, or 6.9% of our assets, were comprised of an intercompany loan to the Bank secured by participation interests in home equity loans;

$661 million, or 5.3% of our assets, were comprised of participation interests in commercial loans;

$605 million, or 4.8% of our assets, were comprised of interest rate swaps;

$303 million, or 2.4% of our assets, were comprised of cash and cash equivalents;

$205 million, or 1.6% of our assets, were comprised of participation interests in home equity loans;

$89 million, or 0.7% of our assets, were comprised of residential mortgage loans; and

$31 million, or 0.3% of our assets, were comprised of net other assets;

each before the allowance for loan losses.

Additionally, unfunded commitments and letters of credit at September 30, 2002, were $1.5 billion and $216 million, respectively.

The weighted average yield earned on total interest-earning assets for the nine months ended September 30, 2002, was 3.31%.

Although we have the authority to acquire interests in an unlimited number of mortgage and other assets from unaffiliated third parties, the majority of our interests in mortgage and other assets acquired prior to this offering have been acquired from the Bank or an affiliate pursuant to loan participation agreements between the Bank or an affiliate and us. The remainder of our assets were acquired directly from the Bank. The Bank either originated the mortgage assets or acquired them as part of the acquisition of other financial institutions. We may also acquire from time to time mortgage-backed securities and a limited amount of additional non-mortgage related securities. We have no present plans or expectations with respect to purchases of mortgage assets or other assets from unaffiliated third parties.

The loans in our portfolio are serviced by the Bank pursuant to the terms of participation and servicing agreements between the Bank and us. The Bank has delegated servicing responsibility of the residential mortgage loans to third parties which are not affiliated with us or the Bank.

**General Description of Mortgage Assets and Other Authorized Investments; Investment Policy**

The Code requires us to invest at least 75% of the total value of our assets in real estate assets, which includes residential mortgage loans and commercial mortgage loans, including participation interests in residential or commercial mortgage loans, mortgage-backed securities eligible to be held by REITs, cash, cash equivalents, including receivables and government securities, and other real estate assets. We refer to these types of assets as REIT Qualified Assets . We may invest up to 25% of the value of a REIT s total assets in non-mortgage-related securities as defined in the Investment Company Act. Under the Investment Company Act, the term security is defined broadly to include, among other things, any note, stock, treasury stock, debenture, evidence of indebtedness, or certificate of interest or participation in any profit sharing agreement or a group or index of securities. The Code also requires that the value of any one issuer s securities, other

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than those securities included in the 75% test, may not exceed 5% by value of the total assets of the REIT. In addition, under the Code, the REIT may not own more than 10% of the voting securities or more than 10% of the value of the outstanding securities of any one issuer, other than those securities included in the 75% test and the securities of wholly-owned, qualified REIT subsidiaries. Generally, the Code designation for REIT Qualified Assets is less stringent than the Investment Company Act designation for Qualifying Interests, due to the ability under the Code to treat cash and cash equivalents as REIT Qualified Assets and a lower required ratio of REIT Qualified Assets to total assets.

All of the financial information and other data in the following discussion is presented on a pro forma basis to reflect the following:

- $866 million of participation interests in home equity loans received by us as collateral for an intercompany loan to the Bank in October 2002. The underlying home equity loans were originated by the Bank; and

- the issuance of three new series of preferred securities (Series A, B and C) to Wachovia Preferred Holding in exchange for participations in commercial and commercial real estate loans prior to this offering. The commercial and commercial real estate loans were originated by the Bank and contributed to Wachovia Preferred Holding. We will issue the preferred securities to Wachovia Preferred Holding in exchange for participations in the loans prior to this offering.

Under the Code, as of the time of this offering approximately 90% of our assets will be invested in REIT Qualified Assets and approximately 10% will be invested in commercial loans and other assets that are not REIT Qualified Assets. We do not hold any securities nor do we intend to hold securities in any one issuer that exceed 5% of our total assets or more than 10% of the voting securities of any one issuer. Our assets will consist of the following as of the time of this offering:

| | Pro Forma | |
|---|---|---|
| **(Dollars in thousands)** | **Amount** | **Percentage of Assets** |
| **REIT Qualified Assets** | | |
| Cash and cash equivalents | $ 303,327 | 2.4% |
| Participation interests | | |
| Commercial real estate loans | 9,846,391 | 78.7 |
| Home equity loans | 205,305 | 1.6 |
| Residential mortgage loans | 88,668 | 0.7 |
| Intercompany loan to Bank secured by participation interests in home equity loans | 866,053 | 6.9 |
| Allowance for loans losses | (101,230) | (0.8) |
| Total REIT Qualified Assets | 11,208,514 | 89.6 |
| **Other Non-Qualified Assets** | | |
| Commercial loans | 660,549 | 5.3 |
| Interest rate swaps | 605,438 | 4.8 |
| Accounts receivable-affiliates | 22,274 | 0.2 |
| Other assets and unearned income | 8,382 | 0.1 |
| Total other non-qualified assets | 1,296,643 | 10.4 |
| Total assets | $ 12,505,157 | 100.0% |

REITs generally are subject to tax at the maximum corporate rate on income from foreclosure property less deductible expenses directly connected with the production of that income. Income from foreclosure property includes gain from the sale of foreclosure property and income from operating foreclosure property, but income that would be qualifying income for purposes of the 75% gross income test is not treated as income from foreclosure property. Qualifying income for purposes of the 75% gross income test includes, generally, rental income and gain from the sale of property not held as inventory or for sale in the ordinary course of a trade or business. In accordance with the terms of the commercial, commercial mortgage and residential mortgage participation and servicing agreements, we maintain the authority to decide whether to foreclose on collateral that secures a loan. In the event we determine a foreclosure proceeding is appropriate, we may direct the Bank to prosecute the foreclosure on our behalf. Upon sale or other disposition of foreclosure property, the Bank will remit to us the proceeds less the cost of holding and selling the foreclosure property.

*Commercial and Commercial Real Estate Loans*

We own participation interests in commercial loans secured by non-real property such as industrial equipment, aircraft, livestock, furniture and fixtures, and inventory. Participation interests acquired in commercial real estate loans are secured by real property such as office buildings, multi-family properties of five units or more, industrial, warehouse and self-storage properties, office and industrial condominiums, retail space, strip shopping centers, mixed use commercial properties, mobile home parks, nursing homes, hotels and motels, churches, and farms. In addition, some of our commercial loans are unsecured. Such unsecured loans are more likely than loans secured by real estate or personal property collateral to result in a loss upon default. Commercial and commercial real estate loans also may not be fully amortizing. This means that the loans may have a significant principal balance or balloon payment due on maturity. Additionally, there is no requirement regarding the percentage of any commercial or commercial real estate property that must be leased at the time we acquire a participation interest in a commercial or commercial real estate loan secured by such property nor are commercial loans required to have third party guarantees.

Commercial properties, particularly industrial and warehouse properties, generally are subject to relatively greater environmental risks than non-commercial properties. This gives rise to increased costs of compliance with environmental laws and regulations. We may be affected by environmental liabilities related to the underlying real property which could exceed the value of the real property. Although the Bank has exercised and will continue to exercise due diligence to discover potential environmental liabilities prior to our acquisition of any participation in loans secured by such property, hazardous substances or wastes, contaminants, pollutants, or their sources may be discovered on properties during our ownership of the participation interests. There can be no assurance that we would not incur full recourse liability for the entire cost of any removal and clean-up on a property, that the cost of removal and clean-up would not exceed the value of the property, or that we could recoup any of the costs from any third party.

The credit quality of a commercial or commercial real estate loan may depend on, among other factors:

- the existence and structure of underlying leases;
- the physical condition of the property, including whether any maintenance has been deferred;
- the creditworthiness of tenants;
- the historical and anticipated level of vacancies;
- rents on the property and on other comparable properties located in the same region;
- potential or existing environmental risks;

the availability of credit to refinance the loan at or prior to maturity; and

the local and regional economic climate in general.

Foreclosures of defaulted commercial or commercial real estate loans generally are subject to a number of complicating factors, including environmental considerations, which are not generally present in foreclosures of residential mortgage loans.

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The following table sets forth certain information at September 30, 2002, with respect to the types of loans underlying the commercial and commercial real estate loan participations.

**Type of Commercial Loans**

| | Pro Forma | |
|---|---|---|
| **(Dollars in thousands)** | **Aggregate Principal Balance** | **Percentage by Aggregate Principal Balance** |
| **Type** | | |
| Commercial loans | $ 660,549 | 6.3% |
| Commercial mortgage loans | 9,846,391 | 93.7 |
| Total | $ 10,506,940 | 100.0% |

The following table shows data with respect to the collateral, if any, securing the loans underlying the commercial and commercial real estate loan participations and the weighted average maturity by primary collateral, if any, of the loans underlying the commercial and commercial real estate loan participations at September 30, 2002.

**Commercial and Commercial Real Estate Loans by Primary Collateral and Maturity**

| | Pro Forma | | |
|---|---|---|---|
| **(Dollars in thousands)** | **Aggregate Principal Balance** | **Percentage by Aggregate Principal Balance** | **Weighted Average Months to Maturity** |
| **Collateral, if any** | | | |
| Real estate | $ 9,846,391 | 93.7% | 80 |
| Receivables | 49,329 | 0.5 | 13 |
| Equipment/inventory | 52,359 | 0.5 | 41 |
| Assignments | 42,682 | 0.4 | 34 |
| Securities | 12,054 | 0.1 | 22 |
| Miscellaneous | 6,040 | 0.1 | 59 |
| Unsecured | 498,085 | 4.7 | 19 |
| Total | $ 10,506,940 | 100.0% | 76 |

The following table shows data with respect to the geographic distribution of the loans underlying the commercial and commercial real estate loan participations at September 30, 2002.

**Geographic Distribution of Commercial and Commercial Real Estate Loans**

| | Pro Forma | | |
|---|---|---|---|
| **(Dollars in thousands)** | **Number of Loans** | **Aggregate Principal Balance** | **Percentage by Aggregate Principal Balance** |
| **State** | | | |
| Connecticut | 101 | $ 242,058 | 2.3% |
| Florida | 722 | 1,997,197 | 19.0 |
| Georgia | 217 | 602,043 | 5.7 |
| Maryland | 78 | 272,271 | 2.6 |
| New Jersey | 371 | 1,240,761 | 11.8 |
| New York | 79 | 229,901 | 2.2 |
| North Carolina | 666 | 1,968,901 | 18.7 |
| Ohio | 19 | 124,758 | 1.2 |
| Pennsylvania | 456 | 1,364,944 | 13.0 |
| South Carolina | 169 | 497,072 | 4.7 |
| Virginia | 316 | 960,386 | 9.1 |
| Other states, each less than 1% of aggregate principal balance | 336 | 1,006,648 | 9.7 |
| Total | 3,530 | $ 10,506,940 | 100.0% |

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The following table shows data with respect to the principal balance of the loans underlying the commercial and commercial real estate loan participations at September 30, 2002.

**Principal Balances of Commercial and Commercial Real Estate Loans**

| | Pro Forma | | | |
|---|---|---|---|---|
| **(Dollars in thousands)** | **Number of Loans** | | **Aggregate Principal Balance** | **Percentage by Aggregate Principal Balance** |
| **Principal Balance** | | | | |
| Less than $50,000 | 14 | $ | 283 | % |
| $50,000 to $99,999 | 7 | | 510 | |
| $100,000 to $249,999 | 18 | | 3,321 | |
| $250,000 to $499,999 | 40 | | 17,956 | 0.2 |
| $500,000 to $999,999 | 1,039 | | 759,713 | 7.2 |
| $1,000,000 to $1,999,999 | 1,054 | | 1,504,099 | 14.3 |
| $2,000,000 to $2,999,999 | 395 | | 962,966 | 9.2 |
| $3,000,000 to $3,999,999 | 275 | | 961,742 | 9.2 |
| $4,000,000 to $4,999,999 | 179 | | 804,438 | 7.7 |
| $5,000,000 to $9,999,999 | 322 | | 2,216,496 | 21.1 |
| Greater than $10,000,000 | 187 | | 3,275,416 | 31.1 |
| Total | 3,530 | $ | 10,506,940 | 100.0% |

Some of the loans underlying our commercial and commercial real estate loan participations bear interest at fixed rates and some bear interest at variable rates based on indices such as LIBOR and the prime rate. The following tables show data with respect to interest rates of the loans underlying our commercial and commercial real estate loan participations at September 30, 2002.

**Fixed and Variable Rate Commercial and Commercial Real Estate Loans**

| | Pro Forma | | | | |
|---|---|---|---|---|---|
| **(Dollars in thousands)** | **Number of Loans** | | **Aggregate Principal Balance** | **Percentage by Aggregate Principal Balance** | **Weighted Average Interest Rate** |
| **Type** | | | | | |
| Fixed rate | 124 | $ | 459,749 | 4.4% | 4.95% |
| Variable rate | 3,406 | | 10,047,191 | 95.6 | 3.44 |
| Total | 3,530 | $ | 10,506,940 | 100.0% | 3.51% |

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**Interest Rate Distribution Commercial and Commercial Real Estate Loans**

| | Pro Forma | | | | | |
|---|---|---|---|---|---|---|
| | Fixed Rate | | | Variable Rate | | |
| (Dollars in thousands) | Number of Loans | Aggregate Principal Balance | Percentage by Aggregate Principal Balance | Number of Loans | Aggregate Principal Balance | Percentage by Aggregate Principal Balance |
| **Interest Rate** | | | | | | |
| Less than 2.00% | | $ | % | 8 | $ 40,595 | 0.4% |
| 2.00% to 2.99% | 6 | 51,695 | 0.5 | 374 | 1,810,849 | 17.2 |
| 3.00% to 3.99% | 32 | 179,731 | 1.7 | 2,152 | 6,667,226 | 63.5 |
| 4.00% to 4.99% | 12 | 47,810 | 0.4 | 738 | 1,358,998 | 12.9 |
| 5.00% to 5.99% | 8 | 19,149 | 0.2 | 93 | 123,035 | 1.2 |
| 6.00% to 6.99% | 25 | 48,375 | 0.5 | 16 | 21,220 | 0.2 |
| 7.00% to 7.99% | 29 | 79,807 | 0.8 | 15 | 18,044 | 0.2 |
| 8.00% to 8.99% | 9 | 25,510 | 0.2 | 6 | 4,673 | |
| 9.00% and greater | 3 | 7,672 | 0.1 | 4 | 2,551 | |
| Total | 124 | $ 459,749 | 4.4% | 3,406 | $ 10,047,191 | 95.6% |

The following table provides delinquency information for the underlying loans in the commercial and commercial real estate loan participations at September 30, 2002.

**Commercial and Commercial Real Estate Loan Delinquencies**

| | Pro Forma | | | | | |
|---|---|---|---|---|---|---|
| | Fixed Rate | | | Variable Rate | | |
| (Dollars in thousands) | Number of Loans | Aggregate Principal Balance | Percent of Total | Number of Loans | Aggregate Principal Balance | Percent of Total |
| **Delinquencies** | | | | | | |
| Current | 124 | $ 459,749 | 4.4% | 3,262 | $ 9,711,476 | 92.4% |
| 1 to 30 days delinquent | | | | 142 | 333,570 | 3.2 |
| 31 to 60 days delinquent | | | | 2 | 2,145 | |
| 61 to 90 days delinquent | | | | | | |
| Over 90 days delinquent | | | | | | |
| Total | 124 | $ 459,749 | 4.4% | 3,406 | $ 10,047,191 | 95.6% |

*Home Equity Loans*

We own participation interests in home equity loans secured by a first, second or third mortgage which primarily is on the borrowers residence. These loans typically are made for reasons such as home improvements, acquisition of furniture and fixtures, purchases of automobiles, and debt consolidation. Generally, second and third liens are repaid on an installment basis and income is accrued based on the outstanding balance of the loan. First liens are repaid on an amortizing basis. All of the loans currently underlying the home equity loan participations bear interest at fixed rates.

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The following table shows data with respect to the geographic distribution of the loans underlying the home equity loan participations at September 30, 2002, and includes $866 million of participation interests in home equity loans received as collateral for an intercompany loan to the Bank in October 2002.

**Geographic Distribution of Home Equity Loans**

| | Pro Forma | | |
|---|---|---|---|
| **(Dollars in thousands)** | **Number of Loans** | **Aggregate Principal Balance** | **Percentage by Aggregate Principal Balance** |
| **State** | | | |
| Connecticut | 837 | $ 39,704 | 3.7% |
| Delaware | 369 | 12,426 | 1.2 |
| Florida | 2,620 | 86,954 | 8.1 |
| Georgia | 1,006 | 33,649 | 3.1 |
| Illinois | 225 | 11,286 | 1.1 |
| Maryland | 938 | 32,842 | 3.1 |
| Missouri | 226 | 10,271 | 1.0 |
| New Jersey | 4,555 | 206,438 | 19.3 |
| New York | 1,288 | 55,160 | 5.1 |
| North Carolina | 2,707 | 107,352 | 10.0 |
| Ohio | 462 | 18,598 | 1.7 |
| Pennsylvania | 6,843 | 235,566 | 22.0 |
| South Carolina | 648 | 26,106 | 2.4 |
| Tennessee | 292 | 13,058 | 1.2 |
| Virginia | 2,480 | 86,339 | 8.1 |
| Other states, each less than 1% of aggregate principal balance | 2,717 | 95,609 | 8.9 |
| Total | 28,213 | $ 1,071,358 | 100.0% |

**Interest Rate Distribution Home Equity Loans**

| | Pro Forma | | |
|---|---|---|---|
| | Fixed Rate | | |
| **(Dollars in thousands)** | **Number of Loans** | **Aggregate Principal Balance** | **Percentage by Aggregate Principal Balance** |
| **Interest Rate** | | | |
| 5.00% to 5.99% | 6 | $ 273 | % |
| 6.00% to 6.99% | 639 | 37,018 | 3.5 |

| | | | |
|---|---|---|---|
| 7.00% to 7.99% | 9,726 | 421,082 | 39.3 |
| 8.00% to 8.99% | 10,254 | 354,554 | 33.1 |
| 9.00% to 9.99% | 2,899 | 99,904 | 9.3 |
| 10.00% to 10.99% | 3,602 | 110,958 | 10.4 |
| 11.00% to 11.99% | 455 | 26,721 | 2.5 |
| 12.00% to 12.99% | 450 | 15,629 | 1.5 |
| 13.00% to 13.99% | 112 | 3,515 | 0.3 |
| 14.00% to 14.99% | 70 | 1,704 | 0.1 |
| Total | 28,213 | $ 1,071,358 | 100.0% |

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The home equity loans have a weighted average of 151 months to maturity and a weighted average interest rate of 8.60%.

The following table provides delinquency information for the underlying loans in the home equity loan participations at September 30, 2002, and includes $866 million of participation interests in home equity loans received as collateral for an intercompany loan to the Bank in October 2002.

**Home Equity Loan Delinquencies**

| | Pro Forma | | |
|---|---|---|---|
| | Fixed Rate | | |
| (Dollars in thousands) | Number of Loans | Aggregate Principal Balance | Percent of Total |
| **Delinquencies** | | | |
| Current | 27,791 | $ 1,047,344 | 97.8% |
| 1 to 30 days delinquent | 184 | 9,423 | 0.9 |
| 31 to 60 days delinquent | 78 | 4,620 | 0.4 |
| 61 to 90 days delinquent | 37 | 2,367 | 0.2 |
| Over 90 days delinquent | 123 | 7,604 | 0.7 |
| Total | 28,213 | $ 1,071,358 | 100.0% |

*Residential Mortgage Loans*

We have acquired both conforming and non-conforming residential mortgage loans from the Bank. Conforming residential mortgage loans comply with the requirements for inclusion in a loan guarantee or purchase program sponsored by either the FHLMC or FNMA. Under current regulations, the maximum principal balance allowed on conforming residential mortgage loans ranges from $300,700 for one-unit residential loans to $578,150 for four-unit residential loans. Nonconforming residential mortgage loans are residential mortgage loans that do not qualify in one or more respects for purchase by FHLMC or FNMA under their standard programs. A majority of the non-conforming residential mortgage loans acquired by us to date are non-conforming because they have original principal balances which exceeded the requirements for FHLMC or FNMA programs, the original terms are shorter than the minimum requirements for FHLMC or FNMA programs at the time of origination, the original balances are less than the minimum requirements for FHLMC or FNMA programs, or generally because they vary in certain other respects from the requirements of such programs other than the requirements relating to creditworthiness of the mortgagors. A substantial portion of our non-conforming residential mortgage loans are expected to meet the requirements for sale to national private mortgage conduit programs or other investors in the secondary mortgage market. However, we have no intent to sell any of our residential mortgage loans.

Each residential mortgage loan is evidenced by a promissory note secured by a mortgage or deed of trust or other similar security instrument creating a first lien on one-to-four family residential property. Residential real estate properties underlying residential mortgage loans consist of single-family detached units, individual condominium units, two-to-four-family dwelling units, and townhouses.

Our portfolio of residential mortgage loans currently consists of both adjustable and fixed rate mortgage loans and we may purchase additional interests in both types of residential mortgage loans in the future, although the mix of variable and fixed rate mortgage loans may change. Fixed rate mortgage loans currently consist of the following fixed rate product types:

*Fixed Rate Mortgage Loans:* A mortgage loan that bears interest at a fixed rate for the term of the loan. Such loans generally mature in 15, 20, 25 or 30 years.

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*Government Fixed Rate Loans:* A fixed rate mortgage loan originated under a specific governmental agency program, for example, the Federal Housing Authority or the Veterans Administration. Such loans generally mature in 15 or 30 years and may be guaranteed by a government agency.

*Balloon Mortgage Loans*: A fixed rate mortgage loan having original or modified terms to maturity for a specified period, which is typically 5, 7, 10 or 15 years, at which time the full outstanding principal balance on the loan will be due and payable. Such loans provide for level monthly payments of principal and interest based on a longer amortization schedule, generally 30 years. Some of these loans may have a conditional refinancing option at the balloon maturity, which provides that, in lieu of repayment in full, the loan may be modified to a then-current market interest rate for the remaining unamortized term. None of the residential balloon mortgage loans in the portfolio have yet reached the balloon maturity.

Adjustable rate mortgage loans, or ARMs, currently consist of the following adjustable rate product types:

*Conventional:*

*One-year Adjustable Rate Loans:* A loan with interest adjustments in 12-month intervals. Payment frequencies may include biweekly, semimonthly, or monthly. Such loans may have yearly and lifetime caps on the amount the interest rate may change at an interval. The interest rate change calculation is typically tied to a Treasury index rate. Typically, the interest rate is based on the weekly average yield on United States Treasury securities adjusted to a constant maturity of one year plus the margin stated in the note, subject to rounding and any caps.

*3/1 Adjustable Rate Loans:* A one-year ARM that is fixed for the first three years of the loan. After the initial three-year period, the interest adjusts in 12-month intervals with caps on the initial change and each subsequent annual change and may be subject to a maximum cap on lifetime changes. Typically, the interest is based on the same Treasury security as the one-year ARM and is calculated using the margin and caps stated in the note.

*5/1 Adjustable Rate Loans:* A one-year ARM that is fixed for the first five years of the loan. After the initial five-year period, the interest adjusts in 12-month intervals with caps on the initial change and each subsequent annual change and may be subject to a maximum cap on lifetime changes. Typically, the interest is based on the same Treasury security as the one-year ARM and is calculated using the margin and caps stated in the note.

*7/1 Adjustable Rate Loans:* A one-year ARM that is fixed for the first seven years of the loan. After the initial seven-year period, the interest adjusts in 12-month intervals with caps on the initial change and each subsequent annual change and may be subject to a maximum cap on lifetime changes. Typically, the interest is based on the same Treasury security as the one-year ARM and is calculated using the margin and caps stated in the note.

*10/1 Adjustable Rate Loans:* A one-year ARM that is fixed for the first ten years of the loan. After the initial 10-year period, the interest adjusts in 12-month intervals with caps on the initial change and each subsequent annual change and may be subject to a maximum cap on lifetime changes. Typically, the interest is based on the same Treasury security as the one-year ARM and is calculated using the margin and caps stated in the note.

*Government:* An adjustable rate loan originated under a specific government agency program. Generally, the interest rate adjusts in 12-month intervals, and is based on specific requirements for date of index and calculations.

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**Type of Residential Mortgage Loans**

| | Pro Forma | | | | |
|---|---|---|---|---|---|
| (Dollars in thousands) | Number of Loans | Aggregate Principal Balance | Percentage by Aggregate Principal Balance | Weighted Average Months to Maturity | Weighted Average Interest Rate |
| **Type** | | | | | |
| Conventional | | | | | |
| **Fixed rate** | | | | | |
| First lien | 330 | $ 49,487 | 55.8% | 199 | 7.14% |
| **Adjustable rate** | | | | | |
| First lien | 274 | 39,181 | 44.2 | 207 | 6.15 |
| Total | 604 | $ 88,668 | 100.0% | 202 | 6.70% |

The following table sets forth data with respect to the geographic distribution of the residential mortgage loans in our portfolio at September 30, 2002.

**Geographic Distribution of Residential Mortgage Loans**

| | Pro Forma | | |
|---|---|---|---|
| (Dollars in thousands) | Number of Loans | Aggregate Principal Balance | Percentage by Aggregate Principal Balance |
| **State** | | | |
| Arizona | 2 | $ 445 | 0.5% |
| California | 2 | 512 | 0.6 |
| Colorado | 1 | 256 | 0.3 |
| Connecticut | 546 | 72,294 | 81.5 |
| Florida | 9 | 5,431 | 6.1 |
| Georgia | 3 | 501 | 0.6 |
| Illinois | 2 | 439 | 0.5 |
| Maryland | 2 | 615 | 0.7 |
| Massachusetts | 4 | 556 | 0.6 |
| New Jersey | 2 | 607 | 0.7 |
| New Mexico | 1 | 445 | 0.5 |
| New York | 8 | 902 | 1.0 |
| North Carolina | 5 | 1,104 | 1.2 |
| Oklahoma | 1 | 523 | 0.6 |
| Pennsylvania | 2 | 426 | 0.5 |

| | | | |
|---|---|---|---|
| South Carolina | 2 | 486 | 0.5 |
| Texas | 7 | 1,838 | 2.1 |
| Vermont | 1 | 163 | 0.2 |
| Virginia | 2 | 509 | 0.6 |
| Washington | 2 | 616 | 0.7 |
| Total | 604 | $ 88,668 | 100.0% |

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The following table shows data with respect to the principal balance of the loans in our residential mortgage loan portfolio at September 30, 2002.

**Principal Balances of Residential Mortgage Loans**

| (Dollars in thousands) | Pro Forma Number of Loans | Pro Forma Aggregate Principal Balance | Pro Forma Percentage by Aggregate Principal Balance |
|---|---|---|---|
| **Principal Balance** | | | |
| Less than $25,000 | 88 | $ 1,125 | 1.3% |
| $25,000 to $49,999 | 101 | 3,721 | 4.2 |
| $50,000 to $74,999 | 84 | 5,266 | 5.9 |
| $75,000 to $99,999 | 69 | 5,923 | 6.7 |
| $100,000 to $249,999 | 156 | 27,105 | 30.6 |
| $250,000 to $499,999 | 87 | 28,753 | 32.4 |
| $500,000 to $749,999 | 13 | 7,845 | 8.8 |
| $750,000 to $999,999 | 3 | 2,679 | 3.0 |
| $1,000,000 to $1,499,999 | 1 | 1,497 | 1.7 |
| $1,500,000 to $1,999,999 | 1 | 1,761 | 2.0 |
| Greater than $2,000,000 | 1 | 2,993 | 3.4 |
| Total | 604 | $ 88,668 | 100.0% |

Of the residential mortgage loans in our portfolio, approximately 55.8% by principal balance bear interest at fixed rates and 44.2% at variable rates. The following table contains additional data with respect to the interest rates of such fixed and variable rate residential mortgage loans at September 30, 2002.

**Interest Rate Distribution Residential Mortgage Loans**

| | Pro Forma | | | | | |
|---|---|---|---|---|---|---|
| | Fixed Rate | | | Variable Rate | | |
| (Dollars in thousands) | Number of Loans | Aggregate Principal Balance | Percentage by Aggregate Principal Balance | Number of Loans | Aggregate Principal Balance | Percentage by Aggregate Principal Balance |
| **Interest Rate** | | | | | | |
| Under 6.00% | 33 | $ 3,074 | 3.5% | 86 | $ 15,773 | 17.8% |

| | | | | | | |
|---|---|---|---|---|---|---|
| 6.00% to 6.99% | 110 | 20,488 | 23.1 | 145 | 15,800 | 17.8 |
| 7.00% to 7.99% | 84 | 18,769 | 21.2 | 33 | 6,390 | 7.2 |
| 8.00% to 8.99% | 64 | 5,415 | 6.1 | 10 | 1,218 | 1.4 |
| 9.00% to 9.99% | 28 | 1,438 | 1.6 | | | |
| 10.00% to 10.99% | 8 | 247 | 0.3 | | | |
| 11.00% to 11.99% | 2 | 47 | | | | |
| 12.00% to 12.99% | | | | | | |
| 13.00% to 13.99% | 1 | 9 | | | | |
| Total | 330 | $ 49,487 | 55.8% | 274 | $ 39,181 | 44.2% |

Gross Margin with respect to a residential mortgage loan that is an adjustable rate residential mortgage loan means the applicable fixed rate that, when added to the applicable index, results in the current interest rate paid by the borrower of such residential mortgage loan without taking into account any interest

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rate caps or minimum interest rates. The following table sets forth certain additional data with respect to the gross margin on residential mortgage loans at September 30, 2002.

**Gross Margin of Adjustable Rate Residential Mortgage Loans**

| | Pro Forma | | |
|---|---|---|---|
| **(Dollars in thousands)** | **Number of Loans** | **Aggregate Principal Balance** | **Percentage by Aggregate Principal Balance** |
| **Gross Margin** | | | |
| Greater than 3.00% | 274 | $ 39,181 | 44.2% |

The following table provides certain delinquency and other information for the loans in our residential mortgage portfolio at September 30, 2002.

**Residential Mortgage Loan Delinquencies**

| | Pro Forma | | |
|---|---|---|---|
| **(Dollars in thousands)** | **Number of Loans** | **Aggregate Principal Balance** | **Percent of Total** |
| **Delinquencies** | | | |
| Current | 561 | $ 84,320 | 95.1% |
| 1 to 30 days delinquent | 31 | 3,030 | 3.4 |
| 31 to 60 days delinquent | 7 | 863 | 1.0 |
| 61 to 90 days delinquent | 1 | 132 | 0.1 |
| Over 90 days delinquent | 4 | 323 | 0.4 |
| Total | 604 | $ 88,668 | 100.0% |

**Interest Rate Swaps**

In December 2001, the Bank contributed receive-fixed interest rate swaps with a notional amount of $4.25 billion and a fair value of $673 million to us in exchange for 89 shares of our common stock. After the contribution, we entered into pay-fixed interest rate swaps with a notional amount of $4.25 billion that serve as an off-setting economic hedge of the contributed swaps. All interest rate swaps are entered into with the same unaffiliated third party. The receive-fixed swaps are financial derivatives contracts under which we have agreed to receive specified fixed rates on the notional amounts of the contracts in exchange for payment of floating rates on the notional amounts of the contracts to the counterparties. The pay-fixed swaps are financial derivatives contracts under which we have agreed to pay specified fixed rates on the notional amounts of the contracts in exchange for the receipt of floating rates on the notional amounts of the contracts from the counterparties. Although the pay-fixed interest rate swaps are considered an economic hedge, we expect volatility of unrealized gains and losses as a result of certain interest rate fluctuations due to a difference in fixed rates between the receive-fixed and pay-fixed interest rate swaps. Realized and unrealized gains and losses are recorded immediately in earnings as a net gain or loss on interest rate swaps. At any point in time, the fair value of the interest rate swaps is based on then-prevailing interest rates on that day compared to the fixed interest rates associated with the interest rate swaps. As a result of the difference in the fixed rates of the receive-fixed and pay-fixed interest rate swaps of 7.41% and 5.69%, respectively, our net position will always be reflected as an asset on our consolidated balance sheet.

Because the $4.25 billion of receive-fixed interest rate swaps reprice using the same index as the $4.25 billion of pay-fixed interest rate swaps, we have no index basis risk related to the swaps.

At September 30, 2002, our total credit risk, as represented by the fair value of all derivatives in a gain position, amounted to $1.2 billion. Credit risk is reduced significantly by entering into master netting

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agreements. The net fair value is the most relevant measure of credit risk when there is a master netting agreement. As our swap transactions are with one counterparty and there is a legally enforceable master netting agreement between the parties, the exposure to our counterparty represents the net of the gain and loss positions with that counterparty, which was $605 million as of September 30, 2002 all of which is substantially collateralized by cash.

None of the swaps are used for the purpose of hedging, but the swaps introduce no interest rate risk to us because the floating rate components of the swaps offset each other. The net effect of the swaps is to lock in a gain on which we will receive cash over the duration of the instruments.

We use collateral arrangements, credit approvals, limits and monitoring procedures to manage credit risk for derivatives. Collateral for dealer transactions is delivered by either party when the credit risk associated with a particular transaction, or group of transactions to the extent netting exists, exceeds defined thresholds of credit risk. Thresholds are determined based on the strength of the individual counterparty.

At September 30, 2002, our receive-fixed interest rate swaps with a notional amount of $4.25 billion had a weighted average maturity of 9.50 years, weighted average receive rate of 7.41% and weighted average pay rate of 1.82%. Our pay-fixed interest rate swaps with a notional amount of $4.25 billion had a weighted average maturity of 9.50 years, weighted average receive rate of 1.82% and weighted average pay rate of 5.69% at September 30, 2002. All of the interest rate swaps have variable pay or receive rates based on three- or six-month LIBOR, and they are the pay or receive rates in effect at September 30, 2002.

**Dividend Policy**

We expect to distribute annually an aggregate amount of dividends with respect to our outstanding capital stock equal to approximately 100% of our REIT taxable income, which excludes capital gains. In order to remain qualified as a REIT, we are required to distribute annually at least 90% of our REIT taxable income to our shareholders.

Dividends will be authorized and declared at the discretion of our board of directors. Factors that would generally be considered by our board of directors in making this determination are our distributable funds, financial condition and capital needs, the impact of current and pending legislation and regulations, economic conditions, tax considerations, and our continued qualification as a REIT. We currently expect that both our cash available for distribution and our REIT taxable income will be in excess of the amounts needed to pay dividends on all outstanding Series A, Series B and Series D preferred securities, even in the event of a significant drop in interest rate levels because:

- substantially all of our mortgage assets and other authorized investments are interest-bearing;
- we do not anticipate incurring any indebtedness, although we may incur indebtedness that in an aggregate amount does not exceed 20% of our shareholders equity;
- we expect that our interest-earning assets will continue to exceed the liquidation preference of our preferred stock;
- the amount of loan servicing costs and management fees paid to the Bank are expected to be less than 4% of our income per year; and

we anticipate that, in addition to cash flows from operations, additional cash will be available from principal payments on our loan portfolio.

Accordingly, we expect that we will, after paying the dividends on all classes of preferred securities, pay dividends to holders of shares of our common stock in an amount sufficient to comply with applicable requirements regarding qualification as a REIT. There are, however, certain limitations that restrict our ability to pay dividends on our common stock which are more fully described in this prospectus under the heading Description of Other Wachovia Funding Capital Stock Preferred Stock .

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Under certain circumstances, including any determination that the Bank s relationship to us results in an unsafe and unsound banking practice, the OCC will have the authority to issue an order that restricts our ability to make dividend payments to our shareholders, including holders of the Series A preferred securities. Banking capital adequacy rules limit the total dividend payments made by a consolidated banking entity to be the sum of earnings for the current year and prior two years less dividends paid during the same periods. Any dividends paid in excess of this amount can only be made with the approval of the Bank s regulator. This could have a material adverse effect on the financial condition of the Bank due to our size and the Bank s reliance on our payment of dividends on our common stock.

**Conflicts of Interest and Related Management Policies and Programs**

*General*

In administering our loan portfolio and other authorized investments pursuant to the participation and servicing agreements, the Bank has a high degree of autonomy. The Bank has, however, adopted certain policies to guide our administration with respect to the acquisition and disposition of assets, use of capital and leverage, credit risk management, and certain other activities. These policies, which are discussed below, may be amended or revised from time to time at the discretion of our board of directors and, in certain circumstances subject to the approval of a majority of our Independent Directors, but without a vote of our shareholders, including holders of the Series A preferred securities.

*Underwriting Standards*. Described below are underwriting standards used by the Bank or its affiliates, as applicable, to originate loans that have been or may be transferred to us from the Bank or its affiliates. We do not have lending operations. The Bank or its applicable affiliates perform all of these lending and underwriting operations.

*Commercial and Commercial Real Estate Loans*

Real estate loans are loans secured by real estate and for which the primary source of repayment is based on the quality and sufficiency of a stream of rental income from the property. The income stream from a real estate loan either amortizes the loan or permits the property s sale or refinance. The Bank makes the following types of real estate loans:

office (including multi-tenant, single tenant and condominiums);

retail;

apartments;

commercial development;

- warehouse/industrial (including self-storage facilities);
- continuing care retirement communities;
- senior living facilities;
- lodging;
- loans to residential builders for the purpose of developing residential home sites or construction; and
- commercial and industrial real estate loans (where the primary source of repayment is based on the financial strength of the business operations or the borrower instead of the income stream from the real estate).

The Bank analyzes the borrower s creditworthiness, repayment capacity, and adequacy of the real property provided as collateral. For each product type listed above, the Bank utilizes underwriting guidelines

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for loan-to-value, debt service coverage and amortization. These guidelines are adjusted based upon the overall market conditions or local market-specific requirements. The Bank also takes into account the following factors when underwriting real estate loans:

- preference to lend to existing customers;
- the risk and return to the Bank on the use of its capital;
- preference to lend within its existing market in its franchise;
- secondary sources of repayment, including guarantees;
- the amount of borrower equity;
- preference for loan terms of three years or less;
- exposure limits per customer and project;
- knowledge of the repayment sources, including permanent loan conditions, interest rate sensitivity and property values;
- need for property type diversification in its portfolio; and
- preference against financing projects with speculative market risk.

*Home Equity Loans*

The Bank and Wachovia Bank of Delaware, National Association (a subsidiary of Wachovia and our affiliate, which we refer to as Wachovia Delaware ), originates and underwrites, or purchases and re-underwrites, home equity loans secured by a first, second or third mortgage primarily on the borrower s residence. The underwriting process is intended to assess both the prospective borrower s ability to repay and the adequacy of the real property security as collateral for the loan. Factors analyzed in determining the borrower s ability to repay the loan include:

- income;
- credit history (including credit scores and credit bureau information); and
- debt-to-income ratio.

Factors analyzed in determining the adequacy of the real property security include:

- Loan-to-Value Ratio;
- appraisals; and
- homeowners insurance.

*Residential Mortgage Loans*

Wachovia Mortgage Corporation, a subsidiary of Wachovia and an affiliate of the Bank and us, which we refer to as Wachovia Mortgage , originates and underwrites, or purchases and re-underwrites, consumer first mortgage loans. These loans typically are used to acquire or re-finance customers primary residences. Wachovia Mortgage s underwriting criteria are focused primarily on secondary market guidelines. The underwriting process is intended to assess both the prospective borrower s ability to repay and the adequacy of the real property security as collateral for the loan. Factors analyzed in determining the borrower s ability to repay the loan include:

- stability of income;
- credit history (including credit scores and credit bureau information); and
- debt-to-income ratio.

Factors analyzed in determining the adequacy of the real property security include:

- Loan-to-Value Ratio;
- appraisals; and
- homeowners and title insurance.

*Asset Acquisition and Disposition Policies.* It is our policy to purchase, or accept as capital contributions, loans or participation interests in loans from the Bank or its affiliates that generally are:

- performing, meaning they have no more than two payments past due, if any;
- in accrual status; and
- secured by real property such that they are REIT Qualified Assets.

Our policy also allows for investment in loans or assets which are not REIT Qualified Assets up to but not exceeding the statutory limitations imposed on organizations that qualify as a REIT under the Code. In the past, we have purchased or accepted as capital contributions loans and participation interests in loans both secured and not secured by real property along with other assets. We anticipate that we will acquire, or receive as capital contributions, interests in additional real estate secured loans from the Bank or its affiliates. We may use any proceeds received in connection with the repayment or disposition of loan participation interests in our portfolio to acquire additional loans. Although we are not precluded from purchasing additional types of loans, loan participation interests or other assets, we anticipate that participation interests in additional loans acquired by us will be of the types described above under the heading General Description of Mortgage Assets and Other Authorized Investments; Investment Policy . Although we are permitted to do so, we have no present plans or intentions to purchase loans or loan participation interests from unaffiliated third parties. In addition, we will not invest in assets that are not REIT Qualified Assets if such investments would cause us to violate the requirements for taxation as a REIT under the Code.

We may from time to time acquire a limited amount of other authorized investments. Although we currently do not intend to acquire any mortgage-backed securities representing interests in or obligations backed by pools of mortgage loans that are secured by single-family residential, multi-family or commercial real estate properties located throughout the United States, we are not restricted from doing so. We do not intend to acquire any interest-only or principal-only mortgage-backed securities. At September 30, 2002, we did not hold any mortgage-backed securities.

We currently anticipate that the Bank or its affiliates will continue to act as servicer of any additional loans that we acquire through purchase or participation interests. We anticipate that any servicing arrangement that we enter into in the future with the Bank or its affiliates will contain fees and other terms that most likely will be substantially equivalent to but may be more favorable to us than those that would be contained in servicing arrangements entered into with unaffiliated third parties.

In accordance with the terms of the commercial, commercial real estate and residential loan participation and servicing agreements, we maintain the authority to decide whether to foreclose on collateral that secures a loan. In the event we determine a foreclosure proceeding is appropriate, we may direct the Bank to prosecute the foreclosure on our behalf. Upon sale or other disposition of foreclosure property, the Bank will remit to us the proceeds less the cost of holding and selling the foreclosure property.

*Credit Risk Management Policies.* For a description of our credit risk management policies, see below under Management s Discussion and Analysis of Financial Condition and Results of Operations Risk Governance and Administration .

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*Conflict of Interest Policies.* Because of the nature of our relationship with the Bank or its affiliates, it is likely that conflicts of interest will arise with respect to certain transactions, including, without limitation, our acquisition of participation interests in loans from, or disposition of participation interests in loans to, the Bank, foreclosure on defaulted loans, management of the cash collateral related to the interest rate swaps and the modification of either the participation or servicing agreements. It is our policy that the terms of any financial dealings with the Bank will be consistent with those available from third parties in the lending industry.

Conflicts of interest among us and the Bank or its affiliates may also arise in connection with making decisions that bear upon the credit arrangements that the Bank or its affiliates may have with a borrower under a loan. Conflicts also could arise in connection with actions taken by us or the Bank or its affiliates. It is our intention that any agreements and transactions between us on the one hand, and the Bank or its affiliates on the other hand, including, without limitation, any loan participation agreements, be fair to all parties and consistent with market terms for such types of transactions. The requirement in our certificate of incorporation that certain of our actions be approved by a majority of our Independent Directors also is intended to ensure fair dealings among us and the Bank or its affiliates. There can be no assurance, however, that any such agreement or transaction will be on terms as favorable to us as could have been obtained from unaffiliated third parties.

There are no provisions in our certificate of incorporation limiting any of our officers, directors, shareholders, or affiliates from having any direct or indirect pecuniary interest in any asset to be acquired or disposed of by us or in any transaction in which we have an interest or from engaging in acquiring, holding, and managing our assets. As described in this prospectus, it is expected that the Bank will have direct interests in transactions with us including, without limitation, the sale of assets to us; however, none of our officers or directors will have any interests in such mortgage assets.

*Other Policies.* We intend to operate in a manner that will not subject us to regulation under the Investment Company Act. Therefore, we do not intend to:

- invest in the securities of other issuers for the purpose of exercising control over such issuers;
- underwrite securities of other issuers;
- actively trade in loans or other investments;
- offer securities in exchange for property; or
- make loans to third parties, including our officers, directors or other affiliates.

The Investment Company Act exempts entities that, directly or through majority-owned subsidiaries, are primarily engaged in the business of purchasing or otherwise acquiring mortgages and other liens on and interests in real estate . We refer to these interests as Qualifying Interests . Under current interpretations by the staff of the SEC, in order to qualify for this exemption, we, among other things, must maintain at least 55% of our assets in Qualifying Interests and also may be required to maintain an additional 25% in Qualifying Interests or other real estate-related assets. The assets that we may acquire therefore may be limited by the provisions of the Investment Company Act. We have established a policy of limiting authorized investments which are not Qualifying Interests to no more than 20% of the value of our total assets.

We may, under certain circumstances, purchase the Series A preferred securities and other shares of capital stock in the open market or otherwise. We have no present intention of repurchasing any of our shares of capital stock, and any such action would be taken only in conformity with applicable Federal and state laws and regulations and the requirements for qualifying as a REIT.

We intend to distribute to our shareholders, in accordance with the Exchange Act, annual reports containing consolidated financial statements prepared in accordance with accounting principles generally

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accepted in the United States of America and certified by our independent auditors. Our certificate of incorporation provides that we will maintain our status as a reporting company under the Exchange Act for so long as any of the Series A preferred securities are outstanding and held by unaffiliated shareholders.

We currently make investments and operate our business in such a manner consistent with the requirements of the Code to qualify as a REIT. However, future economic, market, legal, tax, or other considerations may cause our board of directors, subject to approval by a majority of our Independent Directors, to determine that it is in our best interest and the best interest of our shareholders to revoke our REIT status. The Code prohibits us from electing REIT status for the four taxable years following the year of such revocation.

**Servicing**

The loans in our portfolio are serviced by the Bank or its affiliates pursuant to the terms of participation and servicing agreements between the Bank and its affiliates and us. The Bank has delegated servicing responsibility of the residential mortgage loans to third parties that are not affiliated with us or the Bank or its affiliates.

We pay the Bank a monthly loan servicing fee for its services under the terms of the loan participation and servicing agreements. The amount and terms of the fee are determined by mutual agreement of the Bank and us from time to time during the terms of the participation and servicing agreements.

We paid the Bank total servicing fees of $0.4 million, $1.2 million and $1.8 million for the years ended December 31, 2001, 2000, and 1999, respectively. Total servicing fees paid to the Bank for the nine months ended September 30, 2002, were $0.7 million. For 2002, the annual servicing fee with respect to the commercial real estate, commercial, and home equity loans is equal to the outstanding principal balance of each loan multiplied by a fee of 0.03% and the annual servicing fee with respect to residential mortgages is equal to $48 per loan.

The participation and servicing agreements require the Bank to service the loans in our portfolio in a manner substantially the same as for similar work performed by the Bank for transactions on its own behalf. The Bank or its affiliates collect and remit principal and interest payments, maintain perfected collateral positions, and submit and pursue insurance claims. The Bank and its affiliates also provide accounting and reporting services required by us for our participation interests and loans. We also may direct the Bank to dispose of any loans that become classified as non-performing, placed in a non-performing status, or are renegotiated due to the financial deterioration of the borrower. The Bank is required to pay all expenses related to the performance of its duties under the participation and servicing agreements, including any payment to its affiliates or third parties for servicing the loans.

In accordance with the terms of the commercial, commercial real estate and residential loan participation and servicing agreements, we maintain the authority to decide whether to foreclose on collateral that secures a loan. In the event we determine a foreclosure proceeding is appropriate, we may direct the Bank to prosecute the foreclosure on our behalf. Upon sale or other disposition of foreclosure property, the Bank will remit to us the proceeds less the cost of holding and selling the foreclosure property.

**Competition**

In order to qualify as a REIT under the Code, we can only be a passive investor in real estate loans and certain other assets. Thus, we will not originate loans. We anticipate that we will continue to possess interests in mortgage and other loans in addition to those in the current portfolio and that substantially all of these

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loans will be owned by the Bank, although we may purchase loans from unaffiliated third parties. Accordingly, while the Bank competes with mortgage conduit programs, investment banking firms, savings and loan associations, banks, thrift and loan associations, finance companies, mortgage bankers, or insurance companies in acquiring and originating loans, we do not. Because we will not originate loans and do not anticipate purchasing loans from unaffiliated third parties, we do not expect to compete with other REITs holding similar assets.

**Regulatory Considerations**

As a financial holding company and a bank holding company under the Bank Holding Company Act, Wachovia is regulated, supervised and examined by the Federal Reserve Board. For a discussion of the material elements of the regulatory framework applicable to financial holding companies, bank holding companies and their subsidiaries and specific information relevant to Wachovia, please refer to Wachovia s annual report on Form 10-K for the fiscal year ended December 31, 2001, and any subsequent reports Wachovia files with the SEC, which are incorporated by reference in this prospectus. This regulatory framework is intended primarily for the protection of depositors and the Federal deposit insurance funds and not for the protection of security holders. As a result of this regulatory framework, Wachovia s earnings are affected by actions of the Federal Reserve Board, the OCC, which regulates its banking subsidiaries such as the Bank, the Federal Deposit Insurance Corporation, which insures the deposits of Wachovia s banking subsidiaries within certain limits, and the SEC, which regulates the activities of certain subsidiaries engaged in the securities business.

Wachovia s earnings are also affected by general economic conditions, its management policies and legislative action.

In addition, there are numerous governmental requirements and regulations that affect Wachovia s business activities. A change in applicable statutes, regulations or regulatory policy may have a material effect on Wachovia s business.

Depository institutions, like Wachovia s bank subsidiaries, are also affected by various Federal laws, including those relating to consumer protection and similar matters. Wachovia also has other financial services subsidiaries regulated, supervised and examined by the Federal Reserve Board, as well as other relevant state and Federal regulatory agencies and self-regulatory organizations. Wachovia s non-bank subsidiaries may be subject to other laws and regulations of the Federal government or the various states in which they are authorized to do business.

**Legal Proceedings**

We are not the subject of any litigation. We, Wachovia and the Bank are not currently involved in nor, to our knowledge, currently threatened with any material litigation with respect to the assets included in our portfolio, other than routine litigation arising in the ordinary course of business.

**Employees**

We have 2 executive officers, each of whom is described further below under Management, and approximately 15 additional non-executive officers. Our executive officers are also executive officers of Wachovia. We do not anticipate that we will require any additional employees because employees of the Bank and its affiliates are servicing the loans under the participation and servicing agreements. All of our officers are also officers or employees of Wachovia and/or the Bank. We maintain corporate records and audited financial statements that are separate from those of the Bank. Except as borrowers under home equity or residential mortgage loans, none of our officers, employees or directors will have any direct or indirect pecuniary interest in any mortgage asset to be acquired or disposed of by us or in any transaction in which we have an interest or will engage in acquiring, holding, and managing mortgage assets. However, 113 employees of Wachovia or its affiliates, including certain of the executive officers and non-executive officers discussed above, own one Series D preferred security each.

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## SELECTED CONSOLIDATED FINANCIAL DATA

The following selected consolidated financial data for the three years ended December 31, 2001, are derived from our audited consolidated financial statements. The following selected consolidated financial data for the two years ended December 31, 1998 and for the nine months ended September 30, 2002 and 2001, are derived from unaudited consolidated financial statements and reflect all adjustments, consisting only of normal recurring adjustments, that, in the opinion of our management, are necessary for a fair and consistent presentation of such data. Operating results for the nine months ended September 30, 2002, are not necessarily indicative of results expected for the entire year. This data should be read in conjunction with the consolidated financial statements, related notes, and other financial information beginning on page F-1 of this prospectus and Wachovia s unaudited supplementary consolidating financial information as of and for the nine months ended September 30, 2002, and the years ended December 31, 2001 and 2000, which includes certain consolidated financial information for the Bank, beginning on Page F-22 of this prospectus.

| | Nine Months Ended September 30, | | Years Ended December 31, | | | | |
|---|---|---|---|---|---|---|---|
| (In thousands, except per share data) | 2002 | 2001 | 2001 | 2000 | 1999 | 1998 | 1997 |
| **Income Statement Data** | | | | | | | |
| Net interest income | $ 127,098 | 43,374 | 67,322 | 57,257 | 47,005 | 47,520 | 47,370 |
| Provision for loan losses | 7,033 | 6,290 | 5,262 | 3,602 | 1,034 | 1,099 | (228) |
| Other income (loss) | 68,356 | | (95,890) | 395 | 96 | (172) | 669 |
| Noninterest expense | 6,597 | 1,013 | 2,394 | 2,207 | 3,078 | 3,083 | 2,953 |
| Net income (loss) | $ 305,936 | 23,446 | (23,545) | 32,434 | 27,951 | 28,057 | 29,458 |
| **Balance Sheet Data** | | | | | | | |
| Cash and cash equivalents | $ 1,169,380 | 327,057 | 957,454 | 183,223 | 196,397 | 97,978 | 187,992 |
| Loans, net of unearned income | 4,297,280 | 440,040 | 4,378,961 | 558,756 | 512,858 | 586,616 | 483,904 |
| Allowance for loan losses | (37,335) | (5,655) | (37,158) | (3,833) | (1,285) | (849) | (541) |
| Interest rate swaps | 605,438 | | 573,620 | | | | |
| Total assets | 6,071,086 | 775,039 | 5,889,666 | 746,803 | 714,097 | 686,269 | 690,241 |
| Collateral held on interest rate swaps | 599,570 | | 570,340 | | | | |
| Total liabilities | 606,938 | 5,082 | 732,246 | 283 | | 115 | 32,144 |
| Total stockholders equity | $ 5,464,148 | 769,957 | 5,157,420 | 746,520 | 714,097 | 686,154 | 658,097 |
| **Selected Other Information** | | | | | | | |
| Nonperforming loans | $ 16,425 | 2,882 | 5,024 | 2,684 | 3,733 | 2,910 | 6,603 |
| Nonperforming loans as a % of total loans | 0.38% | 0.65 | 0.11 | 0.48 | 0.73 | 0.50 | 1.36 |
| Nonperforming loans as a % of total assets | 0.27 | 0.37 | 0.09 | 0.36 | 0.52 | 0.42 | 0.96 |
| Allowance for loan losses as a % of nonperforming loans | 227.31 | 196.22 | 739.61 | 142.81 | 34.42 | 29.18 | 8.19 |
| Allowance for loan losses as a % of total loans | 0.87% | 1.29 | 0.85 | 0.69 | 0.25 | 0.14 | 0.11 |

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## UNAUDITED PRO FORMA CONDENSED CONSOLIDATED FINANCIAL INFORMATION

The unaudited pro forma condensed consolidated financial information includes our historical consolidated balance sheet as of September 30, 2002, and our historical consolidated statements of income for the nine months ended September 30, 2002, and the year ended December 31, 2001, each giving effect to the issuance of our Series A, Series B and Series C preferred securities in exchange for loan participations, as if such transactions had occurred at the beginning of the period presented.

These unaudited pro forma results include management s best estimate of the impact of the issuance of the Series A, Series B and Series C preferred securities in exchange for loan participations and the issuance of our Series D preferred securities. The unaudited pro forma condensed consolidated financial information may not be indicative of the financial position or results of operations that actually would have occurred had the transactions been consummated during the period or as of the date indicated, or which will be attained in the future. The unaudited pro forma condensed consolidated financial information should be read in conjunction with our historical consolidated financial statements, which appear elsewhere in this prospectus.

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**WACHOVIA PREFERRED FUNDING CORP.**

**AND SUBSIDIARY**

**PRO FORMA COMBINED BALANCE SHEET**

**(Unaudited)**

The following unaudited pro forma combined balance sheet combines our historical consolidated balance sheet as of September 30, 2002, with the transactions described in the accompanying note to the pro forma condensed consolidated financial information, including the issuance of our Series A, B and C preferred securities to Wachovia Preferred Holding.

| | September 30, 2002 | | |
|---|---|---|---|
| (In thousands) | Wachovia Funding | Pro Forma Adjustments | Wachovia Funding Combined |
| **ASSETS** | | | |
| Cash and cash equivalents | $ 1,169,380 | (866,053) | 303,327 |
| Loans | 4,302,947 | 6,497,966 | 10,800,913 |
| Intercompany loan to Bank secured by participation interests in home equity loans | | 866,053 | 866,053 |
| Total loans | 4,302,947 | 7,364,019 | 11,666,966 |
| Unearned income | (5,667) | | (5,667) |
| Loans, net of unearned income | 4,297,280 | 7,364,019 | 11,661,299 |
| Allowance for loan losses | (37,335) | (63,895) | (101,230) |
| Loans, net | 4,259,945 | 7,300,124 | 11,560,069 |
| Interest rate swaps | 605,438 | | 605,438 |
| Accounts receivable affiliates | 22,274 | | 22,274 |
| Other assets | 14,049 | | 14,049 |
| Total assets | $ 6,071,086 | 6,434,071 | 12,505,157 |
| **LIABILITIES AND STOCKHOLDERS EQUITY** | | | |
| Liabilities | | | |
| Collateral held on interest rate swaps | 599,570 | | 599,570 |
| Other liabilities | 7,368 | | 7,368 |
| Total liabilities | 606,938 | | 606,938 |
| Stockholders equity | | | |
| Preferred stock | | | |
| Series A preferred securities, $0.01 par value, $25.00 liquidation preference, non-cumulative and conditionally exchangeable, 30,000,000 shares authorized, issued and outstanding | | 300 | 300 |

| | | | |
|---|---|---|---|
| Series B preferred securities, $0.01 par value, $25.00 liquidation preference, non-cumulative and conditionally exchangeable, 40,000,000 shares authorized, issued and outstanding | | 400 | 400 |
| Series C preferred securities, $0.01 par value, $1,000 liquidation preference, cumulative, 5,000,000 shares authorized, 4,233,754 shares issued and outstanding | | 42 | 42 |
| Series D preferred securities, $0.01 par value, $1,000 liquidation preference, non-cumulative, 913 shares authorized, issued and outstanding | | | |
| Common stock, $.01 par value, 100,000,000 shares authorized, 99,999,900 shares issued and outstanding | 1,000 | | 1,000 |
| Paid-in capital | 5,086,474 | 6,433,329 | 11,519,803 |
| Retained earnings | 376,674 | | 376,674 |
| Total stockholders equity | 5,464,148 | 6,434,071 | 11,898,219 |
| Total liabilities and stockholders equity | $ 6,071,086 | 6,434,071 | 12,505,157 |

See accompanying note to pro forma condensed consolidated financial information.

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**WACHOVIA PREFERRED FUNDING CORP.**

**AND SUBSIDIARY**

**PRO FORMA COMBINED STATEMENT OF INCOME**

**(Unaudited)**

The following unaudited pro forma combined statement of income combines our historical consolidated statement of income for the nine months ended September 30, 2002, with the transactions described in the accompanying note to the pro forma condensed consolidated financial information.

| | Nine Months Ended September 30, 2002 | | |
|---|---|---|---|
| (In thousands, except per share data and average shares) | Wachovia Funding | Pro Forma Adjustments | Wachovia Funding Combined |
| **INTEREST INCOME** | $ 135,385 | 220,326 | 355,711 |
| **INTEREST EXPENSE** | 8,287 | | 8,287 |
| Net interest income | 127,098 | 220,326 | 347,424 |
| Provision for loan losses | 7,033 | | 7,033 |
| Net interest income after provision for loan losses | 120,065 | 220,326 | 340,391 |
| **OTHER INCOME** | | | |
| Gain on interest rate swaps | 68,352 | | 68,352 |
| Other income | 4 | | 4 |
| Total other income | 68,356 | | 68,356 |
| **NONINTEREST EXPENSE** | | | |
| Loan servicing costs | 1,082 | 1,357 | 2,439 |
| Management fees | 4,371 | 5,482 | 9,853 |
| Other | 1,144 | | 1,144 |
| Total noninterest expense | 6,597 | 6,839 | 13,436 |
| Income before income tax expense (benefit) | 181,824 | 213,487 | 395,311 |
| Income tax expense (benefit) | (124,112) | 148,035 | 23,923 |
| Net income | 305,936 | 65,452 | 371,388 |
| Dividends on preferred securities | | 152,397 | 152,397 |
| Net income available to common stockholders | $ 305,936 | (86,945) | 218,991 |

| | | | |
|---|---|---|---|
| **PER COMMON SHARE DATA** | | | |
| Basic earnings | $ 3.06 | | 2.19 |
| Diluted earnings | $ 3.06 | | 2.19 |
| **AVERAGE SHARES** | | | |
| Basic | 99,999,900 | | 99,999,900 |
| Diluted | 99,999,900 | | 99,999,900 |

See accompanying note to pro forma condensed consolidated financial information.

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**WACHOVIA PREFERRED FUNDING CORP.**

**AND SUBSIDIARY**

**PRO FORMA COMBINED STATEMENT OF INCOME (LOSS)**

**(Unaudited)**

The following unaudited pro forma combined statement of income (loss) combines our historical consolidated statement of income (loss) for the year ended December 31, 2001, with the transactions described in the accompanying note to the pro forma condensed consolidated financial information.

| | Year Ended December 31, 2001 | | |
|---|---|---|---|
| (In thousands, except per share data and average shares) | Wachovia Funding | Pro Forma Adjustments | Wachovia Funding Combined |
| **INTEREST INCOME** | $ 68,179 | 216,053 | 284,232 |
| **INTEREST EXPENSE** | 857 | | 857 |
| Net interest income | 67,322 | 216,053 | 283,375 |
| Provision for loan losses | 5,262 | | 5,262 |
| Net interest income after provision for loan losses | 62,060 | 216,053 | 278,113 |
| **OTHER INCOME** | | | |
| Loss on interest rate swaps | (95,890) | | (95,890) |
| Total other income | (95,890) | | (95,890) |
| **NONINTEREST EXPENSE** | | | |
| Loan servicing costs | 602 | 1,293 | 1,895 |
| Other | 1,792 | | 1,792 |
| Total noninterest expense | 2,394 | 1,293 | 3,687 |
| Income (loss) before income tax benefit | (36,224) | 214,760 | 178,536 |
| Income tax benefit | (12,679) | (20,883) | (33,562) |
| Net income (loss) | (23,545) | 235,643 | 212,098 |
| Dividends on preferred securities | | 203,196 | 203,196 |
| Net income (loss) available to common stockholders | $ (23,545) | 32,447 | 8,902 |
| **PER COMMON SHARE DATA** | | | |
| Basic earnings | $ (1.07) | | 0.41 |

| | | | |
|---|---|---|---|
| Diluted earnings | $ (1.07) | | 0.41 |
| **AVERAGE SHARES** | | | |
| Basic | 21,925,904 | | 21,925,904 |
| Diluted | 21,925,904 | | 21,925,904 |

See accompanying note to pro forma condensed consolidated financial information.

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**WACHOVIA PREFERRED FUNDING CORP.**

**AND SUBSIDIARY**

**NOTE TO PRO FORMA CONDENSED CONSOLIDATED FINANCIAL INFORMATION**

**(Unaudited)**

**September 30, 2002 and December 31, 2001**

**NOTE 1: DESCRIPTION OF PRO FORMA ADJUSTMENTS**

The pro forma adjustments assume the issuance of Series A and Series B preferred securities with a $25.00 liquidation preference and Series C preferred securities with a $1,000 liquidation preference, to Wachovia Preferred Holding.

It has been assumed that Wachovia Preferred Holding will pay $25.00 per Series A and Series B preferred security and $1,000 per Series C preferred security. Wachovia Preferred Holding's payment for the three Series of preferred securities will be in the form of additional participation interests in commercial and commercial real estate loans. We intend to hold these participation interests as long-term investments.

This pro forma condensed consolidated financial information assumes that Wachovia Preferred Holding receives all 30,000,000 Series A preferred securities, all 40,000,000 Series B preferred securities and 4,233,754 Series C preferred securities in exchange for commercial and commercial real estate loan participation interests, which have a book value of approximately $6.5 billion and a fair market value of approximately $6.0 billion.

Wachovia Preferred Holding, a statutory underwriter, will sell 18,000,000 Series A preferred securities through underwriters to the public for cash consideration of $25.00 per preferred security. We will not receive any proceeds from the sale of our Series A preferred securities owned by Wachovia Preferred Holding. The proceeds, before expenses and commissions to be received by Wachovia Preferred Holding from the sale of 18,000,000 Series A preferred securities, are expected to be $450 million. Wachovia Preferred Holding will pay all expenses and underwriting discounts and commissions related to the public offering of the preferred securities.

Pro forma combined balance sheet adjustments include: (i) cash of $866 million loaned to the Bank and secured by participation interests in home equity loans; and (ii) participation interests in commercial and commercial real estate loans with a book value of $6.5 billion, received by us in exchange for the issuance to Wachovia Preferred Holding of $750 million, $1.0 billion and $4.2 billion in Series A, Series B and Series C preferred securities, respectively, and a related increase in paid-in capital of $430 million reflecting the excess of the book value of the loan participations over the fair market value of the loan participations or the liquidation preference of the Series A, Series B and Series C preferred securities. The adjustments also include an additional allowance for loan losses of $64 million related to the participation interests in home equity loans and commercial and commercial real estate loans referred to in (i) and (ii).

Pro forma combined statement of income adjustments include interest income of $220 million and $216 million for the nine months ended September 30, 2002, and the year ended December 31, 2001, respectively, representing the interest assumed to be earned on the $866 million loan to the Bank secured by participation interests in home equity loans net of loan servicing costs and management fees and the $6.5 billion participation interests in commercial and commercial real estate loans contributed, and $6.8 million and $1.3 million of loan servicing costs and management fees for the nine months ended September 30, 2002, and the year ended December 31, 2001, respectively, representing additional estimated expenses that would have been incurred on the $6.5 billion in commercial and commercial real estate loans contributed, and dividends on preferred securities of $152 million and $203 million for the nine months ended September 30, 2002, and the year ended December 31, 2001, respectively. Management fees represent reimbursement to Wachovia for general overhead expenses paid on our behalf that are charged by Wachovia to affiliates that have over $10

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million in assets and over $2 million in estimated noninterest expense. In 2001, we did not meet the second of these criteria and were not charged a management fee; accordingly, we did not include a pro forma adjustment for management fees for 2001. We expect to meet these criteria in 2002 and as a result, we included a pro forma adjustment for management fees for 2002. The income and expense adjustments were estimated on the received and contributed loan participations as if they had been outstanding during each period, unless the underlying loans were originated during the respective period. In cases where the underlying loans were originated during either period, we estimated income from the date of origination to the end of the respective period. Approximately $2.6 billion of the commercial and commercial real estate loan participations contributed were from a recent merger where no origination data was available for early 2001, therefore no income was estimated for those loan participations for 2001. Income on these loan participations was $73 million for the nine months ended September 30, 2002, and resulted in pro forma adjustments of $586,000 and $2.4 million of loan servicing costs and management fees, respectively. The weighted average yield for 2001 was 6% compared with 4% for the nine months ended September 30, 2002, which offsets income not included for 2001. The impact of these items results in similar interest income in both periods in the accompanying pro forma combined statements of income. For the nine months ended September 30, 2002, an income tax benefit of $124 million associated with our change in tax status from a taxable corporation to a REIT has been eliminated. In addition, for the nine months ended September 30, 2002, and the year ended December 31, 2001, an income tax expense (benefit) of $24 million and ($34) million, respectively, is provided to the extent of the income or loss of our taxable REIT subsidiary, Wachovia Preferred Realty, LLC ( WPR ). Because WPR s assets consist primarily of our interest rate swap assets, our income tax expense (benefit) is based on our income from these assets. No income tax expense is provided on the remainder of our income due to our status as a REIT.

The interest income estimates are equal to the actual interest income earned on the loan to the Bank secured by home equity loan participations net of loan servicing costs and management fees, and commercial and commercial real estate loan participations for the nine months ended September 30, 2002, and the year ended December 31, 2001 (except as noted above). Loan servicing costs and management fees represent estimates based on actual costs for the nine months ended September 30, 2002, and the year ended December 31, 2001.

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**MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND**

**RESULTS OF OPERATIONS**

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with Selected Consolidated Financial Data and our audited and unaudited consolidated financial statements and related notes included elsewhere in this prospectus. In addition to historical information, the discussion in this prospectus contains certain forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated by these forward-looking statements due to factors including, but not limited to, those factors set forth under Risk Factors and elsewhere in this prospectus. See also Forward-Looking Statements .

The financial information presented in this section is derived from our historical consolidated financial statements and has not been adjusted for the effect of the issuance of our four series of preferred securities or the related contributions of loan participations.

For the tax year ending December 31, 2002, we will be taxed as a REIT, and we intend to comply with the relevant provisions of the Code to be taxed as a REIT. Accordingly, with the exception of the income of our taxable REIT subsidiary, WPR, we will not be subject to Federal income tax on net income currently distributed to shareholders to the extent we meet these provisions, including distributing the majority of our earnings to shareholders and satisfying certain asset, income and stock ownership tests. As a result of our change in tax status from a taxable corporation to a REIT, our net deferred tax liability as of December 31, 2001, was written off as a benefit to income tax expense in January 2002. Due to the establishment of WPR in October 2002, a deferred tax expense will be recorded to establish the initial deferred tax liability on the book versus tax basis differences of the assets contributed to WPR. In addition, we will incur Federal income tax to the extent of the earnings of WPR.

**Critical Accounting Policies**

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. We have identified the allowance for loan losses as a significant policy that involves a significant amount of judgment and requires use of estimates that are difficult to validate by reference to outside sources, which is discussed below. We also identified the accounting for nonperforming assets and derivatives as policies that impact our business.

*Allowance for Loan Losses*

The allowance for loan losses is maintained at a level that we believe is adequate to cover probable losses inherent in the loan portfolio as of the respective dates of the consolidated financial statements. We employ a variety of techniques as well as our judgment in assessing the adequacy of the allowance. Our methodology for assessing the adequacy of the allowance is comprised of both an allocated and an unallocated component. The allocated component of the allowance for commercial loans is based principally on current loan grades and historical loss rates. For residential loans, it is based on loan payment status and historical loss rates. The unallocated component of the allowance represents the results of analyses that estimate probable losses inherent in the portfolio that are not fully captured in the allocated allowance. These analyses include industry concentrations, model imprecision and the estimated impact of current economic conditions on historical loss rates. We continuously monitor trends in the loan portfolio including trends in the levels of past due, criticized and nonperforming loans. The trends in these factors are used to evaluate the reasonableness of the unallocated component.

We believe we have developed appropriate policies and processes in the determination of an allowance for loan losses reflective of our assessment of credit risk after careful consideration of known relevant facts and trends. In developing this assessment, we must rely on estimates and exercise judgment regarding matters where the ultimate outcome is unknown. Depending on changes in circumstances, future assessments of credit risk may yield materially different results that may result in increases or decreases in the allowance for loan losses.

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*Nonperforming Assets*

Nonperforming assets consist of underlying loans that no longer accrue interest. The accrual of interest is generally discontinued on loans, except residential loans, that become 90 days past due as to principal or interest unless collection of both principal and interest is assured by way of collateralization, guarantees or other security. Generally, loans past due 180 days or more are classified as nonaccrual regardless of security. Home equity loans that become 120 days past due are generally charged to the allowance for loan losses. When borrowers demonstrate over an extended period the ability to repay a loan in accordance with the contractual terms of a loan classified as nonaccrual, the loan is returned to accrual status. When loans or participation interests in loans are obtained from the Bank, the underlying loans are performing at the date of purchase.

The participation and servicing agreements require the Bank to service loan portfolios in a manner substantially the same as for similar work performed by the Bank for transactions on its own behalf. The Bank collects and remits principal and interest payments, maintains perfected collateral positions, and submits and pursues insurance claims. The Bank also provides to us accounting and reporting services required by our participations. We also may direct the Bank to dispose of any underlying loan that becomes classified as nonaccrual, is placed in a nonperforming status, or is renegotiated due to the financial deterioration of the borrower. The Bank is required to pay all expenses related to the performance of its duties under the participation and servicing agreements. In accordance with the terms of the commercial, commercial real estate and residential loan participation and servicing agreements, we maintain the authority to decide whether to foreclose on collateral that secures a loan. In the event we determine a foreclosure proceeding is appropriate, we may direct the Bank to prosecute the foreclosure on our behalf. Upon sale or other disposition of foreclosure property, the Bank will remit to us the proceeds less the cost of holding and selling the foreclosure property.

*Derivatives*

We account for derivative financial instruments in accordance with Statement of Financial Accounting Standards (referred to as SFAS ) No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as subsequently amended by SFAS 137 and SFAS 138, which establishes accounting and reporting standards for derivatives and hedging activities. Under SFAS 133, all of our derivatives (currently consisting of interest rate swaps) are recorded at fair value in the balance sheet. When we have more than one transaction with a counterparty and there is a legally enforceable master netting agreement between the parties, the net of the gain and loss positions are recorded as an asset or liability on our consolidated balance sheet. Realized and unrealized gains and losses are recorded as a net gain or loss on interest rate swaps on our consolidated statement of operations.

In December 2001, the Bank contributed receive-fixed interest rate swaps with a notional amount of $4.25 billion and a fair value of $673 million to us in exchange for common stock. The unaffiliated counterparty to the receive-fixed interest rate swaps provided cash collateral to us. We pay interest to the counterparty on the collateral at a short-term market rate. We also invest the cash in overnight eurodollar investments and earn a short-term market rate. After the contribution of the receive-fixed interest rate swaps, we entered into pay-fixed interest rate swaps with a notional amount of $4.25 billion that serve as an economic hedge of the contributed swaps. All interest rate swaps are transacted with the same unaffiliated third party. Prior to the time that we entered into the pay-fixed interest rate swaps, we realized a decrease in fair value of $95.6 million in the receive-fixed interest rate swaps as a result of changes in then-prevailing interest rates.

At September 30, 2002, receive-fixed interest rate swaps with a notional amount of $4.25 billion had a weighted average maturity of 9.5 years, weighted average receive rate of 7.41% and weighted average pay rate of 1.82%. Pay-fixed interest rate swaps with a notional amount of $4.25 billion had a weighted average maturity of 9.5 years, weighted average receive rate of 1.82% and weighted average pay rate of 5.69% at

September 30, 2002. All of the interest rate swaps have variable pay or receive rates based on three- or six-month LIBOR, and they are the pay or receive rates in effect at September 30, 2002.

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Although the pay-fixed interest rate swaps are considered an economic hedge, we expect volatility of unrealized gains and losses as a result of certain interest rate fluctuations due to a difference in fixed rates between the receive-fixed and pay-fixed interest rate swaps. At any point in time, the fair value of the interest rate swaps is based on then-prevailing interest rates on that day compared to the fixed interest rates associated with the interest rate swaps. As a result of the difference in the fixed rates of the receive-fixed and pay-fixed interest rate swaps of 7.41% and 5.69%, respectively, our net position will always be reflected as an asset on our consolidated balance sheet. At September 30, 2002, our net position was an asset of $605 million.

**Results of Operations**

For purposes of this discussion, the term residential loans includes home equity loans and residential mortgages and the term commercial loans includes commercial and commercial real estate loans. See Table 1 in Accounting and Regulatory Matters for certain performance and dividend payout ratios for the nine months ended September 30, 2002 and 2001, and for the two years ended December 31, 2001.

*2002 to 2001 Nine Month Comparison*

*Interest Income*. Interest income increased $92.0 million from the first nine months of 2001, or 212%, to $135.4 million in the first nine months of 2002. Interest on commercial loans increased to $101.1 million in the first nine months of 2002 from zero in the first nine months of 2001 representing nine months of interest in 2002 on commercial loans contributed to us by the Bank in December 2001. Interest on residential loans decreased $11.9 million, or 34%, to $23.1 million in the first nine months of 2002 from $35.0 million in the first nine months of 2001 as a result of a decrease in residential loan balances and a declining interest rate environment. Interest income on cash invested in overnight eurodollar investments increased $2.8 million, or 33%, in the first nine months of 2002 to $11.2 million from the first nine months of 2001 due to cash investment balances increasing from loan collections and cash received in December 2001 as collateral for interest rate swaps.

The average balances, interest income and rates related to interest-earning assets for the nine months ended September 30, 2002 and 2001, are presented below.

| | **Nine Months Ended September 30, 2002** | | | Nine Months Ended September 30, 2001 | | |
|---|---|---|---|---|---|---|
| **(In thousands)** | **Average Balance** | **Interest Income** | **Rate** | Average Balance | Interest Income | Rate |
| Loan participations | | | | | | |
| Commercial and commercial real estate loans | $ 4,082,323 | 101,102 | 3.31% | $ | | % |
| Home equity loans | 244,783 | 18,058 | 9.86 | 371,575 | 27,460 | 9.90 |
| Total loan participations | 4,327,106 | 119,160 | 3.68 | 371,575 | 27,460 | 9.90 |
| Residential mortgages | 100,532 | 5,038 | 6.68 | 133,585 | 7,507 | 7.49 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Interest-bearing deposits in banks | 1,047,483 | 11,187 | 1.43 | 253,011 | 8,407 | 4.44 |
| Total interest-earning assets | $ 5,475,121 | 135,385 | 3.31% | $ 758,171 | 43,374 | 7.65% |

*Interest Expense.* Interest expense increased to $8.3 million in the first nine months of 2002 from zero in the first nine months of 2001 representing interest paid on cash collateral received related to interest rate swaps that were contributed in December 2001. Interest is paid based on a short-term market rate.

*Gain on Interest Rate Swaps.* The gain on interest rate swaps was $68.4 million in the first nine months of 2002 compared with zero in the first nine months of 2001 representing the net increase in fair value of interest rate swaps. The receive-fixed interest rate swaps were contributed to us by the Bank in December 2001 and the pay-fixed interest rate swaps were entered into by us shortly thereafter as an economic hedge. See Critical Accounting Policies Derivatives above for more information.

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*Loan Servicing Costs.* Loan servicing costs increased $0.7 million, or 151%, to $1.1 million in the first nine months of 2002 from $0.4 million in the first nine months of 2001 due to higher average loans from the commercial loan contribution in December 2001 and an increase in fees paid for residential loan servicing. The loans are serviced by the Bank pursuant to our participation and servicing agreements. For commercial loans, the fee is equal to the average outstanding principal balance of each loan multiplied by 0.03%.

*Management Fees*. Management fees were $4.4 million in the first nine months of 2002 compared with zero in the first nine months of 2001. Management fees represent reimbursements to Wachovia for general overhead expenses paid on our behalf, plus a 10% markup to represent an arm s length fee. The management fee is charged by Wachovia to affiliates that have over $10 million in assets and over $2 million in estimated annual noninterest expense. In 2001, we did not meet the second of those criteria and were not charged a management fee. We anticipate that we will meet both of these criteria in the future, and accordingly, we will continue to incur management fee expense.

*Other Expense*. Other expense increased $0.6 million, or 97%, to $1.1 million in the first nine months of 2002. Foreclosure expense increased $0.7 million due to additional costs associated with foreclosures related to a declining residential portfolio. Additionally, 2001 included $0.3 million for net losses on loan sales, of which there were none in the first nine months of 2002.

*Income Tax Expense.* Income tax expense decreased $136.7 million to a benefit of $124.1 million in the first nine months of 2002 from the first nine months of 2001 as a result of a change in tax status from a taxable corporation to a REIT in 2002. The benefit of $124.1 million in the first nine months of 2002 relates to the reversal of the net deferred tax liability as of December 31, 2001 in January 2002 on our becoming a REIT.

*2001 to 2000 Twelve Month Comparison*

*Interest Income.* Interest income increased $10.9 million from 2000, or 19%, to $68.2 million in 2001. Interest income on commercial loans increased to $12.5 million in 2001 from zero in 2000 representing one month of interest in 2001 on commercial loans that were contributed by the Bank in December 2001. Interest income on residential loans increased $4.5 million, or 11.3%, from 2000 to $44.8 million in 2001 as a result of a full year of interest on $400 million in higher yielding home equity loans purchased from the Bank in August 2000. Interest income on cash invested in overnight eurodollar investments decreased $6.1 million, or 35.7%, from 2000 to $10.9 million in 2001 due to the lower interest rate environment.

The average balances, interest income and rates related to interest-earning assets for the two years ended December 31, 2001, are presented below.

| | Year Ended December 31, 2001 | | | Year Ended December 31, 2000 | | |
|---|---|---|---|---|---|---|
| **(In thousands)** | **Average Balance** | **Interest Income** | **Rate** | Average Balance | Interest Income | Rate |

| | | | | | | |
|---|---|---|---|---|---|---|
| Loan participations | | | | | | |
| Commercial and commercial real estate loans | $ 338,233 | 12,456 | 3.68% | $ | | % |
| Home equity loans | 352,778 | 35,098 | 9.95 | 174,750 | 20,659 | 11.82 |
| Total loan participations | 691,011 | 47,554 | 6.88 | 174,750 | 20,659 | 11.82 |
| Residential mortgages | 131,756 | 9,714 | 7.37 | 276,777 | 19,621 | 7.09 |
| Interest-bearing deposits in banks | 269,689 | 10,911 | 4.05 | 273,008 | 16,977 | 6.22 |
| Total interest-earning assets | $ 1,092,456 | 68,179 | 6.24% | $ 724,535 | 57,257 | 7.90% |

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The dollar amount of change in interest income related to our interest-earning assets for the two years ended December 31, 2001, is presented below.

| | 2001 Compared to 2000 | | | 2000 Compared to 1999 | | |
|---|---|---|---|---|---|---|
| | | Variance Attributable to (a) | | | Variance Attributable to (a) | |
| (In thousands) | Interest Income Variance | Rate | Volume | Interest Income Variance | Rate | Volume |
| **Earning Assets** | | | | | | |
| Commercial and commercial real estate loans | $ 12,456 | 6,228 | 6,228 | | | |
| Home equity loans | 14,439 | (4,940) | 19,379 | 15,822 | 3,576 | 12,246 |
| Residential mortgages | (9,907) | 579 | (10,486) | (13,662) | (202) | (13,460) |
| Interest-bearing deposits in banks | (6,066) | (5,896) | (170) | 8,037 | 2,918 | 5,119 |
| Total earning assets | $ 10,922 | (4,029) | 14,951 | 10,197 | 6,292 | 3,905 |

(a) Changes attributable to rate/volume are allocated to both rate and volume on an equal basis.

*Interest Expense.* Interest expense increased to $0.9 million in 2001 from zero in 2000 representing approximately one month of interest paid on cash collateral received related to interest rate swaps that were contributed in December 2001. Interest is paid based on a short-term market rate.

*Loss on Interest Rate Swaps.* The loss on interest rate swaps was $95.9 million in 2001 representing the decrease in fair value of the receive-fixed interest rate swaps contributed to us by the Bank in December 2001 between the time the contribution was made and the time we entered into pay-fixed interest rate swaps that serve as an economic hedge of the contributed receive-fixed interest rate swaps. See Critical Accounting Policies Derivatives above for more information.

*Loan Servicing Costs.* Loan servicing costs decreased $0.8 million, or 57%, to $0.6 million in 2001 from $1.4 million in 2000 due to the Bank entering into a lower cost sub-servicing agreement in February 2001. The loans are serviced by the Bank pursuant to our participation and servicing agreements. For commercial loans, the fee is equal to the average outstanding principal balance of each loan multiplied by 0.03%.

*Management Fees.* Management fees were zero in 2001 compared with $0.8 million in 2000. As described above, in 2001 we did not meet the second of Wachovia s criteria for assessment of a management fee.

*Other Income.* Other income decreased to zero in 2001 from $0.4 million in 2000 due to 2000 including $0.5 million net gains on loan sales of which there were none in 2001.

*Other Expense.* Other expense increased to $1.8 million in 2001 from zero in 2000 primarily due to $0.4 million in increased foreclosure expense, $0.4 million in losses on loan sales, and $1 million paid to the Bank in consideration for the Bank providing a guaranty of our obligations under the receive-fixed interest rate swaps before we entered into the pay-fixed interest rate swaps. The guaranty fee is equal to 0.03% multiplied by the absolute value of the net notional amount of the interest rate swaps.

*2000 to 1999 Twelve Month Comparison*

*Interest Income.* Interest income increased $10.2 million from 1999, or 22%, to $57.3 million in 2000. Interest income on residential loans increased $2.2 million, or 5.7%, from 1999 to $40.3 million in 2000 due to four months of interest on $400 million of a participation interest in higher yielding home equity loans purchased from the Bank in August 2000, slightly offset by lower residential mortgage loan balances and a declining interest rate environment. Interest income on cash invested in overnight eurodollar investments increased $8 million in 2000 to $17 million from 1999 due to higher cash investment balances.

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The average balances, interest income and rates related to interest-earning assets for the two years ended December 31, 2000, are presented below.

| (In thousands) | Year Ended December 31, 2000 Average Balance | Interest Income | Rate | Year Ended December 31, 1999 Average Balance | Interest Income | Rate |
|---|---|---|---|---|---|---|
| Loan participations | | | | | | |
| Commercial and commercial real estate loans | $ | | % | $ | | % |
| Home equity loans | 174,750 | 20,659 | 11.82 | 55,496 | 4,837 | 8.72 |
| Total loan participations | 174,750 | 20,659 | 11.82 | 55,496 | 4,837 | 8.72 |
| Residential mortgages | 276,777 | 19,621 | 7.09 | 465,924 | 33,283 | 7.14 |
| Interest-bearing deposits in banks | 273,008 | 16,977 | 6.22 | 181,202 | 8,940 | 4.93 |
| Total interest-earning assets | $ 724,535 | 57,257 | 7.90% | $ 702,622 | 47,060 | 6.70% |

*Loan Servicing Costs.* Loan servicing costs decreased $0.5 million, or 27%, to $1.4 million in 2000 from $1.9 million in 1999 due to lower average loan balances. The loans are serviced by the Bank pursuant to our servicing agreement. For residential mortgages and home equity loans, the fee was equal to the average outstanding principal balance of each loan multiplied by 0.38%.

*Management Fees.* Management fees decreased $0.2 million from 1999, or 22%, to $0.8 million in 2000 as a result of lower fees assessed by Wachovia.

*Other Income.* Other income increased $0.3 million in 2000 from 1999 representing gains on loan sales.

**Balance Sheet Analysis**

*September 30, 2002 to September 30, 2001*

At September 30, 2002, total assets were $6.1 billion compared with $775 million at September 30, 2001. As of September 30, 2002, $4.0 billion, or 66% of our assets, consisted of a 100% participation interest in commercial loans, and $205 million, or 3.4% of our assets, consisted of a 100% participation interest in home equity loans, before the allowance for loan losses.

*Loans.* Net loans increased $3.8 billion to $4.3 billion at September 30, 2002, compared with September 30, 2001, due to a $4.0 billion increase in commercial loans contributed to us by the Bank in December 2001 partially offset by decreased residential loans.

*Allowance for Loan Losses.* The allowance for loan losses increased $31.7 million from September 30, 2001, to $37.3 million at September 30, 2002, as a result of allowance transferred with the commercial loans contributed to us by the Bank in December 2001. The allowance was 1.0% of loans at September 30, 2002, and 1.3% at September 30, 2001. See Table 2 in Accounting and Regulatory Matters for additional information.

*Interest Rate Swaps.* Interest rate swaps increased to $605 million at September 30, 2002, from zero at September 30, 2001, which represents fair value of our net position in interest rate swaps.

*Accounts Receivable-Affiliates.* Accounts receivable from affiliates increased to $22.3 million at September 30, 2002, from September 30, 2001, as a result of intercompany transactions related to income tax allocations for the 2001 tax year which represent receivables for taxes paid prior to our becoming a REIT.

*Other Assets.* Other assets increased $2.4 million, or 21%, to $14 million at September 30, 2002, from $11.7 million at September 30, 2001, due to a $6.6 million increase in interest receivables and a $1.2 million increase in foreclosed property, offset by a $5.3 million decrease in loans held for sale.

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*Collateral Held on Interest Rate Swaps.* Collateral held on interest rate swaps increased to $599.6 million at September 30, 2002, from zero at September 30, 2001. As part of the receive-fixed interest rate swaps contributed to us by the Bank in December 2001, the unaffiliated counterparty to the swaps provided collateral that we hold. The cash collateral is recorded at fair value.

*Other Liabilities.* Other liabilities increased to $7.4 million at September 30, 2002, from $89 thousand at September 30, 2001, due to the increase in minority interests after the sale of a 1% interest in our subsidiary s common stock to Wachovia in exchange for cash in December 2001.

*December 31, 2001 to December 31, 2000*

At December 31, 2001, total assets were $5.9 billion compared with $746.8 million at December 31, 2000. As of December 31, 2001, $4 billion, or 68% of our assets, consisted of a 100% participation interest in commercial loans and $286 million, or 5% of our assets, consisted of a 100% participation interest in home equity loans, before the allowance for loan losses.

*Loans.* Net loans were $4.3 billion at December 31, 2001, up $3.8 billion from December 31, 2000, due to the December 2001 contribution to us of $4 billion of commercial loans by the Bank offset by a $156.8 million decrease in residential loans.

Commercial loan maturities on a historical and pro forma basis for the year ended December 31, 2001 are presented below.

| | December 31, 2001 | |
|---|---|---|
| | Commercial and Commercial Real Estate | |
| **(In thousands)** | **Actual** | **Pro Forma** |
| **Fixed Rate** | | |
| 1 year or less | $ | 40,280 |
| 1-5 years | 37,833 | 130,196 |
| After 5 years | 30,570 | 342,935 |
| Total fixed rate | 68,403 | 513,411 |
| **Adjustable Rate** | | |
| 1 year or less | 401,889 | 603,154 |
| 1-5 years | 2,575,536 | 4,063,069 |
| After 5 years | 944,528 | 3,970,651 |
| Total adjustable rate | 3,921,953 | 8,636,874 |

| | | |
|---|---|---|
| Total | $ 3,990,356 | 9,150,285 |

*Allowance for Loan Losses.* The allowance for loan losses increased $33.3 million December 31, 2000 to $37.2 million at December 31, 2001, as a result of the allowance transferred with the commercial loans contributed to us by the Bank in December 2001. The allowance was 0.9% of loans at December 31, 2001, and 0.7% at December 31, 2000. See Table 2 in Accounting and Regulatory Matters for additional information on allowance for loan losses.

*Interest Rate Swaps*. Interest rate swaps increased to $573.6 million at December 31, 2001, from zero at December 31, 2000, from the contribution of the receive-fixed interest rate swaps to us by the Bank in December 2001. Interest rate swaps are recorded at fair value. Subsequent to the contribution, we entered into pay-fixed interest rate swaps that serve as an economic hedge to the receive-fixed interest rate swaps.

*Other Assets.* Other assets increased $9.3 million to $16.8 million at December 31, 2001, from $7.5 million at December 31, 2000, due to a $9.6 million increase in interest receivable, related to the contribution of commercial loans in December 2001, offset by a $0.7 million decrease in consumer interest receivable due to lower consumer loan balances.

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*Collateral Held on Interest Rate Swaps.* Collateral held on interest rate swaps increased to $570.3 million at December 31, 2001, from zero at December 31, 2000. As part of the receive-fixed interest rate swaps contributed to us by the Bank in December 2001, the unaffiliated counterparty to the swaps provided collateral that we hold. The cash collateral is recorded at fair value.

*Other Liabilities.* Other liabilities increased $7.5 million at December 31, 2001, from $0.1 million at December 31, 2000, due to the increase in minority interests after the sale of a 1% interest in our subsidiary s common stock to Wachovia in exchange for cash in December 2001**.**

**Commitments**

Our commercial loan portfolio includes unfunded loan commitments and standby and commercial letters of credit that are provided in the normal course of business. For commercial customers, loan commitments generally take the form of revolving credit arrangements to finance customers working capital requirements. These instruments are not recorded on the balance sheet until funds are advanced under the commitment. For lending commitments, the contractual amount of a commitment represents the maximum potential credit risk if the entire commitment is funded and the borrower does not perform according to the terms of the contract. A large majority of these commitments expire without being funded, and accordingly, total contractual amounts are not representative of our actual future credit exposure or liquidity requirements. The Risk Governance and Administration Credit Risk Management section below describes how the Bank, which originates and services the loans, manages credit risk when extending credit.

Loan commitments and letters of credit create credit risk in the event that the counterparty draws on the commitment and subsequently fails to perform under the terms of the lending agreement. This risk is incorporated into an overall evaluation of credit risk and to the extent necessary, reserves are recorded on these commitments. Uncertainties around the timing and amount of funding under these commitments may create liquidity risk. The Risk Governance and Administration Liquidity Risk Management section below describes the way we manage liquidity and fund these commitments, to the extent funding is required. At September 30, 2002, commitments to extend credit and letters of credit were $1.5 billion and $216 million, respectively. At December 31, 2001, commitments to extend credit and letters of credit were $1.2 billion and $39 million, respectively.

**Liquidity and Capital Resources**

Our internal sources of liquidity generally include cash generated from our operations and principal repaid on loans. In addition, any necessary liquidity could be obtained by drawing on the line of credit that we have with the Bank. Under the terms of that facility, we can borrow up to $2.0 billion under a revolving demand note at a rate of interest equal to the Federal funds rate. Further, we could issue additional common or preferred stock, subject to any pre-approval rights of our shareholders. We believe that our existing sources of liquidity are sufficient to meet our funding needs.

**Risk Governance and Administration**

*Credit Risk Management*

Credit risk is the risk of loss due to adverse changes in a borrower s ability to meet its financial obligations under agreed upon terms. We incur credit risk by investing in lending and lending-related assets. The nature and amount of credit risk depends on the types of transactions pursued, the structure of those transactions and the parties involved. Credit risk is central to the profit strategy in lending. Since our assets are primarily participation interests in loans originated by the Bank, the following is a discussion of the Bank s credit risk management strategies.

Credit risk is managed through a combination of policies and procedures and risk-taking or commitment authorities that are tracked and regularly updated in a centralized database. All credit authorities

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are delegated through the independent risk management organization. Most officers who are authorized to incur credit exposure are in the risk management organization and are independent of the officers who are responsible for generating new business.

The maximum level of credit exposure to individual commercial borrowers is limited by policy guidelines, or house limits . These limits are based on the default probabilities associated with the credit facilities extended to each borrower or related group of borrowers. Concentration risk is managed through geographic and industry diversification, country limits and loan quality factors.

*Commercial Credit.* All commercial loans are assigned internal risk ratings reflecting the probability of the borrower defaulting on any obligation, the probability of a default on any particular Wachovia credit facility and the probable loss in the event of a default.

Commercial credit extensions are also evaluated using a Risk Adjusted Return on Capital model that considers pricing, internal risk ratings, loan structure and tenor, among other variables. This produces a risk/return analysis, enabling the efficient use of economic capital attributable to credit risk. Economic capital is allocated to all credit commitments, whether fully funded or not. The same credit processes and checks and balances are used for unfunded commitments as well as for funded exposures.

Economic capital for all credit risk assets is calculated by the portfolio management group within the risk management organization. As part of their annual capital level review, this group analyzes factors that are used to determine the amount of economic capital needed to support credit risk in the loan portfolio.

Credit Risk Review is an independent unit that performs risk process reviews and evaluates a representative sample of credit extensions after the fact. Credit Risk Review has the authority to change internal risk ratings and is responsible for assessing the adequacy of credit underwriting and servicing practices. This unit reports directly to the Credit and Finance Committee of the Wachovia board of directors.

Credit approvals are based, among other things, on the financial strength of the borrower, assessment of the borrower s management, industry sector trends, the type of exposure, the transaction structure and the general economic outlook. There are two processes for approving credit risk exposures. The first involves standard approval structures for use in retail, certain small business lending and most trading activities. The second, and more prevalent approach, involves individual approval of exposures consistent with the authority delegated to officers experienced in the industries and loan structures over which they have responsibility.

In commercial lending, servicing of credit exposure may be as often as weekly for certain types of asset-based lending, to annually for certain term loans. Some term loans having characteristics similar to retail loans are monitored for delinquencies only. In general, quarterly servicing is normal for all significant exposures. The internal risk ratings are confirmed with each major servicing event. In addition portfolio modeling is employed to verify default probabilities and to estimate losses.

Borrower exposures may be designated as watch list accounts when warranted by either environmental factors or individual company performance. Such accounts are subjected to additional quarterly reviews by the business line management, risk management and credit risk review staff and our chief risk management officer in order to adequately assess the borrower s credit status and to take appropriate action. In addition projections of both nonperforming assets and losses for future quarters are performed monthly. This process is considered essential to the effective management of our credit risk.

The Bank has also established special teams composed of skilled and experienced lenders to manage problem credits. These teams handle commercial recoveries, workouts and problem loan sales.

Commercial credit checks and balances, the independence of risk management functions and specialized processes are all designed to avoid problems where possible and to recognize and address problems early in the cycle when they do occur.

*Retail Credit.* In retail lending, the Bank manages credit risk from a portfolio view rather than by specific borrower as in commercial lending. The risk management division, working with the line of business, determines the appropriate risk/return profile for each portfolio, utilizing a variety of tools including quantitative models and scorecards tailored to meet the Bank s specific needs.

By incorporating these models and policies into computer programs or decisioning engines , much of the underwriting is automated. Once a line of credit or other retail loan is extended, it is included in the overall portfolio, which is continuously monitored for changes in delinquency trends and other asset quality indicators. Delinquency action on individual credits is taken monthly or as needed if collection efforts are necessary. The independent credit risk review unit also has a retail component to ensure adequacy and timeliness of retail credit processes.

*Concentration of Credit Risk*

Concentration of credit risk generally arises with respect to our participation interests when a significant number of underlying loans have borrowers that engage in similar business activities or activities in the same geographical region. Concentration of credit risk indicates the relative sensitivity of performance to both positive and negative developments affecting a particular industry.

*Interest Rate Risk Management*

Interest rate risk is the sensitivity of earnings to changes in interest rates. Our income consists primarily of interest income on our variable rate loans. If there is a further decline in market interest rates, we may experience a reduction in interest income on our loan portfolio and a corresponding decrease in funds available to be distributed to our stockholders. The reduction in interest income may result from downward adjustments of the indices upon which the interest rates on loans are based and from prepayments of loans with fixed interest rates, resulting in reinvestment of the proceeds in lower yielding assets. In December 2001, the Bank contributed receive-fixed interest rate swaps to us in exchange for common stock. Subsequent to the contribution, we entered into pay-fixed interest rate swaps that serve as an economic hedge to the receive-fixed interest rate swaps. Currently, we do not expect to enter into additional derivative transactions.

At September 30, 2002, approximately 6.9% of the loans in our portfolio had fixed interest rates. Such loans tend to increase our interest rate risk. Management monitors the rate sensitivity of assets acquired. Our methods for evaluating interest rate risk include an analysis of interest-rate sensitivity gap , which is defined as the difference between interest-earning assets and interest-bearing liabilities maturing or repricing within a given time period. A gap is considered positive when the amount of interest-rate-sensitive assets exceeds the amount of interest-rate-sensitive liabilities. A gap is considered negative when the amount of interest-rate-sensitive liabilities exceeds interest-rate-sensitive assets.

During a period of rising interest rates, a negative gap would tend to adversely affect net interest income, while a positive gap would tend to result in an increase in interest income. During a period of falling interest rates, a negative gap would tend to result in an increase in net interest income, while a positive gap would tend to affect net interest income adversely. Because different types of assets and liabilities with the same or similar maturities may react differently to changes in overall market rates or conditions, changes in interest rates may affect net interest income positively or negatively even if an institution is perfectly matched in each maturity category.

As of September 30, 2002, $5.1 billion, or 85% of our assets, were variable rate and could be expected to reprice with changes in interest rates. As of September 30, 2002, our liabilities were $607 million, or 10% of our assets, while stockholders equity was $5.5 billion, or 90% of our assets. This positive gap between our assets and liabilities indicates that an increase in interest rates would result in an increase in net interest income and a decrease in interest rates would result in a decrease in net interest income.

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Our rate-sensitive assets and liabilities at September 30, 2002, are presented below. Assets that immediately reprice are placed in the overnight column. The fair value of the $336 million of fixed rate loans and loan participations was approximately $337 million at September 30, 2002. The fair value of the $4.0 billion of variable rate loans and loan participations approximated their book value at September 20, 2002.

| (In thousands) | Overnight | Within One Year | One to Three Years | Three to Five Years | Over Five Years | Total |
|---|---|---|---|---|---|---|
| Rate-sensitive assets | | | | | | |
| Interest bearing deposits in banks | $ 1,154,451 | | | | | 1,154,451 |
| Loans and loan participations: | | | | | | |
| Fixed rate | | 41,217 | 1,697 | 14,075 | 278,939 | 335,928 |
| Variable rate | 966,059 | 2,983,750 | 11,543 | | | 3,961,352 |
| Total rate-sensitive assets | $ 2,120,510 | 3,024,967 | 13,240 | 14,075 | 278,939 | 5,451,731 |
| Total rate-sensitive liabilities | $ 599,570 | | | | | |

At September 30, 2002, our position in interest rate swaps was an asset of $1.2 billion and a liability of $579 million, which is recorded on our balance sheet at fair value. The following table presents interest rate swap maturities.

| (In thousands) | 1 Year or Less | 1-2 Years | 2-5 Years | 5-10 Years | After 10 Years | Total |
|---|---|---|---|---|---|---|
| **Interest Rate Swap Assets** | | | | | | |
| Notional amount | $ | | 150,000 | 4,100,000 | | 4,250,000 |
| Weighted average receive rate (a) | % | | 6.10 | 7.46 | | 7.41 |
| Weighted average pay rate (a) | % | | 1.74 | 1.82 | | 1.82 |
| **Interest Rate Swap Liabilities** | | | | | | |
| Notional amount | $ | | 150,000 | 4,100,000 | | 4,250,000 |
| Weighted average receive rate (a) | % | | 1.74 | 1.82 | | 1.82 |
| Weighted average pay rate (a) | % | | 4.84 | 5.72 | | 5.69 |

(a) All of the interest rate swaps have variable pay or receive rates based on one- to six-month LIBOR, and they are the pay or receive rates in effect at September 30, 2002.

*Market Risk Management*

Market risk is the risk of loss from adverse changes in market prices and interest rates. Market risk arises primarily from interest rate risk inherent in lending, investing in marketable securities, deposit taking and borrowing activities.

At September 30, 2002, our receive-fixed interest rate swaps with a notional amount of $4.25 billion had a weighted average maturity of 9.50 years, weighted average receive rate of 7.41% and weighted average pay rate of 1.82%. Our pay-fixed interest rate swaps with a notional amount of $4.25 billion had a weighted average maturity of 9.50 years, weighted average receive rate of 1.82% and weighted average pay rate of 5.69% at September 30, 2002. All of the interest rate swaps have variable pay or receive rates based on three- or six-month LIBOR, and they are the pay or receive rates in effect at September 30, 2002.

Due to the difference in fixed rates in our interest rate swaps, volatility is expected given certain interest rate fluctuations. If market rates were to decrease 100 basis points or 200 basis points, we would realize short-term net gains on our interest rate swaps of $28 million or $57 million, respectively. If market rates were to increase 100 basis points or 200 basis points, we would realize short-term net losses on our interest rate swaps of $26 million or $50 million, respectively. These short-term fluctuations will eventually offset over the life of the interest rate swaps, with no change in cash flow occurring for the net positions. The changes in value of the net swap positions were calculated under the assumption there was a parallel shift in the LIBOR curve using 100 basis point and 200 basis point shifts, respectively.

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*Liquidity Risk Management*

Liquidity risk involves the risk of being unable to fund assets with the appropriate duration and rate-based liability, as well as the risk of not being able to meet unexpected cash needs. Liquidity planning and management are necessary to ensure we maintain the ability to fund operations cost-effectively and to meet current and future potential obligations. In managing liquidity, we take into account various legal limitations placed on us.

Our principal liquidity needs are to pay operating expenses and dividends, fund commitments under our loans, and acquire additional participation interests as the underlying loans mature or prepay. Operating expenses and dividends are expected to be funded through cash generated by operations, while funding commitments and the acquisition of additional participation interests in loans is intended to be funded with the proceeds obtained from repayment of principal balances by individual borrowers. We do not have and do not anticipate having any material capital expenditures.

To the extent that our board of directors determines that additional funding is required, we may raise funds through additional equity offerings, debt financings, or retention of cash flow, or a combination of these methods. However, any cash flow retention must be consistent with the provisions of the Code requiring the distribution by a REIT of at least 90% of its REIT taxable income, excluding capital gains, and must take into account taxes that would be imposed on undistributed income.

At September 30, 2002, our liabilities consist of cash collateral held on the receive-fixed interest rate swaps that we have invested in eurodollar investments. Our certificate of incorporation does not contain any limitation on the amount or percentage of debt, funded or otherwise, we may incur, except the incurrence of debt for borrowed money or our guarantee of debt for borrowed money in excess of amounts borrowed or guaranteed.

**Transactions with Related Parties**

We are subject to certain income and expense allocations from affiliated parties for various services received. In addition, we enter into transactions with affiliated parties in the normal course of business. The nature of the transactions with affiliated parties is discussed below. Further information, including amounts involved, is presented in Note 5 of our consolidated financial statements.

Affiliates of Wachovia service our loans on our behalf. We are also subject to Wachovia s management fee policy and therefore reimburse Wachovia for general overhead expenses paid on our behalf. We did not meet Wachovia s criteria for being assessed a fee in 2001, and therefore no fee was charged. We also have a swap servicing and fee arrangement with the Bank, whereby the Bank provides operations, back office, book entry, record keeping and valuation services related to our interest rate swaps, for which we pay a fee to the Bank.

Interest-bearing and noninterest-bearing deposits with the Bank are our primary cash management vehicle. In addition, we have certain eurodollar investments with the Bank. In 2001, we entered into certain loan participations with affiliates and are allocated a portion of all income associated with these loans.

The Bank acts as our collateral custodian in connection with collateral pledged to us related to our interest rate swaps. For this service, we pay the Bank a fee based on the value of the collateral. In addition, the Bank is permitted to rehypothecate and use as its own the collateral held by the Bank as our custodian. The Bank pays us a fee based on the value of the collateral involved for this right. The Bank also provides a guaranty of our obligations under the interest rate swaps, for which we pay a monthly fee based on the absolute value of the net notional amount of the interest rate swaps.

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**Accounting and Regulatory Matters**

The following information addresses new or proposed accounting pronouncements related to our industry as well as legislation that has had a significant impact on our industry.

*Derivatives and Hedging.* In 1998 the Financial Accounting Standards Board issued SFAS 133, *Accounting for Derivative Instruments and Hedging Activities*, which was subsequently amended by SFAS 137 and SFAS 138. These standards establish the accounting and reporting model for derivatives and hedging activities. SFAS 133 requires that all derivatives be recognized as assets or liabilities on the balance sheet and that these instruments be measured at fair value through adjustments to either other comprehensive income or to current earnings, depending on the purpose for which the derivative is held.

*Regulatory Matters.* On July 30, 2002, President Bush signed the Sarbanes-Oxley Act of 2002 into law. The intent of this law is to reform specific matters pertaining to public accounting oversight, auditor independence and corporate responsibility. Requirements in the act will affect certain of Wachovia s corporate governance policies and certain of Wachovia s business lines, such as securities analysis. We do not believe we will need to make material modifications to our corporate governance policies in response to the act or do we believe the act will negatively affect our financial condition or results of operations.

Various legislative and regulatory proposals concerning the financial services industry are pending in Congress, the legislatures in states in which we conduct operations and before various regulatory agencies that supervise our operations. Given the uncertainty of the legislative and regulatory process, we cannot assess the impact of any such legislation or regulations on our financial condition or results of operations.

**Table 1**

**Performance and Dividend Payout Ratios**

| | Nine Months Ended September 30, | | Years Ended December 31, | |
|---|---|---|---|---|
| | **2002** | **2001** | **2001** | **2000** |
| **Ratios** | | | | |
| Return on assets | 5.12% | 3.08 | (0.71) | 3.83 |
| Return on stockholders equity | 5.76 | 3.09 | (0.80) | 3.83 |
| Stockholders equity to assets | 88.80 | 99.65 | 88.96 | 97.82 |
| Dividend payout ratio | % | 0.04 | | 0.03 |

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**Table 2**

**Loan Losses and Recoveries and Past Due Loans**

| | Nine Months Ended September 30, | | Years Ended December 31, | |
|---|---|---|---|---|
| **(In thousands)** | **2002** | **2001** | **2001** | **2000** |
| **Allowance for Loan Losses** | | | | |
| Balance, beginning of period | $ 37,158 | 3,833 | 3,833 | 1,285 |
| Provision for loan losses | 7,033 | 6,290 | 5,262 | 3,602 |
| Allowance relating to loans contributed from the Bank | | | 33,681 | |
| Allowance related to loans transferred or sold | (2,005) | (482) | (515) | |